

WHO PAYS THE FREIGHT?

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It often happens in tougher economic climates that two relatively innocent parties are left to litigate a dispute caused by a third company which has gone out of business. In a recent Federal Court of Canada decision the Court was faced with just this problem.

Mediterranean Shipping Company (“Mediterranean”), an ocean carrier, sought to recover from BPB Westroc Inc. (“Westroc”), the defendant shipper, the sum of \$65,187 for freight in connection with the carriage of Westroc’s goods on three separate occasions. Westroc conceded that the cargoes were theirs and that Mediterranean had carried them to the correct destination in proper condition. However, Westroc denied any liability on the basis that the freight had already been paid to a freight forwarder, J.T. Knight Export Services (“J.T. Knight”), that Westroc believed had the authority to receive payment on Mediterranean’s behalf.

The Federal Court noted that any result reached in the case would necessarily be viewed as unjust by the losing party, particularly as neither party to the action had done other than what was generally expected. In other words, the carrier had transported the goods as arranged by the freight forwarder, and the shipper had paid the freight forwarder upon being invoiced. The Court was left with the unenviable task of deciding whether the shipper should, in the circumstances, be made to pay twice, or whether the carrier would not be paid at all.

The Federal Court discussed two competing principles in the case law. The law generally supported carriers in their efforts to collect freight for the carriage of cargo from shippers where a freight forwarder who made the booking goes bankrupt after having been paid by the shipper. In recent decisions however, the Federal Court has denied recovery to carriers based on equitable considerations. Therefore, the two main issues faced by the Court were:

1. Whether Mediterranean, by its conduct, induced Westroc to conclude that the freight forwarder, J.T. Knight was authorized to receive payment for the shipments; and

2. Whether Mediterranean was estopped or prevented from claiming the freight charges because of its knowledge of J.T. Knight's financial difficulties and its failure to inform Westroc.

The Court heard considerable evidence regarding business practices that are prevalent in the freight forwarding industry. Mediterranean suggested that few shippers were able or willing to devote the resources to keeping abreast of market developments, freight rates and document preparation. As a result Mediterranean's business was primarily conducted with freight forwarders acting on behalf of Canadian shippers. It was Mediterranean's experience that freight forwarders generally insist that carrier representatives not "go behind" the freight forwarder and contact the forwarder's client. Any carrier representative who failed to conform could face serious repercussions, such as loss of future referrals or blacklisting.

J.T. Knight had contracted with Mediterranean over the years in respect of a number of different shippers. Through J.T. Knight's marketing efforts, Westroc began using Mediterranean as its maritime carrier in September 2000. Mediterranean agreed to the same credit terms previously negotiated by J.T. Knight, that is, payment within 30 days from the date of the bill of lading. J.T. Knight provided a corporate guarantee of Westroc's freight charges and an acknowledgement that it was acting as the shipper's agent. From September 2000 to January 2001, eight transactions took place between Mediterranean and Westroc.

According to Mediterranean, the bills of lading also acted as freight invoices. Westroc's name was inserted on all bills of lading as the shipper and, in accordance with the bill of lading terms, as the party responsible for the freight. Even though the bills of lading were addressed to Westroc, they were forwarded to J.T. Knight, as custom dictated.

J.T. Knight was late in making the freight payments to Mediterranean beginning with the first shipment. Mediterranean gave evidence that although there was some tolerance shown towards freight forwarders once the 30 day credit period expired, Mediterranean never willingly agreed to receive payments late from J.T. Knight and the company's leniency did not somehow constitute an extension of credit.

Mediterranean invoiced Westroc for the total amount of \$65,187 for freight earned on three voyages in November and December 2000. Through January and February 2001 Mediterranean insisted on payment in conversations with J.T. Knight and advised that two new bookings would not be released without payment in advance. The witness for Mediterranean testified that he had no reason to suspect that the cause of J.T. Knight's non-payment was something other than the lack of receipt of funds from Westroc although there was an acknowledgement that Mediterranean was aware that J.T. Knight was having cash flow problems.

Ultimately Mediterranean advised J.T. Knight that it would have to contact Westroc directly. J.T. Knight responded immediately requesting Mediterranean not to communicate with Westroc as it would alienate Westroc and could put J.T. Knight out of business. When finally Mediterranean contacted Westroc directly as to why J.T. Knight was not paying Westroc's invoices, Mediterranean was advised that J.T. Knight had already received payment. Westroc's terms with J.T. Knight were payment within seven days of billing.

The Federal Court considered the foregoing circumstances and noted that there is a trend in the Federal Court to avoid imposing on an innocent party an obligation to pay a second time under equitable principles. In *Morlines Maritime Agency v. Iko Industries* the plaintiff agent of a carrier sought recovery of freight from a defendant shipper in circumstances where the shipper had already paid its freight forwarder who had gone bankrupt before paying the carrier's agent. The court held that the shipper did not have to pay the freight to the carrier noting that the carrier agent's conduct had led the shipper to conclude that payment should be made directly to the forwarder as carrier. Therefore, determining whether a payment of freight by the shipper to the freight forwarder is to be considered payment to the carrier can only be answered by delving into the intention of the parties by reviewing the documents and the party's conduct.

In another Federal Court decision in *CP Ships v. Les Industres Lyon*, the Court stated that where a shipper instead of paying the carrier, chooses to pay a freight forwarder, the shipper does so at his peril. Where the money is not turned over to the carrier, the shipper then has the onus to establish either:

1. That the carrier actually authorized the freight forwarder to receive the money, or

2. That the carrier held the freight forwarder out as being so authorized, or
3. That the carrier by his conduct induced the shipper to come to that conclusion, or
4. That a custom exists so that both the shipper and the carrier would normally expect payment to be made to the freight forwarder.

In the case at bar, the Court considered the above principles and observed that since freight forwarders may have few assets, and yet book cargo far exceeding their net worth, there is no economically rational motive for the carrier to release the shipper. It follows that carriers would expect payment to come from the shipper, albeit passing through, and not from, the freight forwarder. The Court then concluded that there are legitimate policy reasons for adopting a rebuttable presumption in favour of shipper liability.

The Court held that the burden was on Westroc, not Mediterranean, to prove that its liability was released. Westroc did not call evidence to establish that it was somehow induced to believe that Mediterranean was not looking to Westroc for payment. The Court also found that Mediterranean was under no obligation to approach Westroc directly when concerns arose about late payments from J.T. Knight, particularly in light of the practice in the industry of not “going behind” a forwarder. Since Westroc appointed J.T. Knight as its agent for purposes of billing and collecting freight charges, and as the party to whom all documents necessary for that purpose would be sent, Mediterranean could not be faulted with following the trade practice of dealing with Westroc solely through its agent. Therefore under the general principles of agency and by operation of law, the Court concluded that non-payment by an agent is deemed non-payment by the principal and Westroc had simply failed to take proper precautions to protect itself.

The trial judge observed that Westroc could have investigated the reputation of its freight forwarder. It could also have insisted that the cheques be payable to the carrier, and not the freight forwarder. In the result, the Federal Court held that the shipper, Westroc, remained liable to the carrier, Mediterranean on the basis that it was unable to present clear and unequivocal evidence that the carrier somehow released it from liability.

In conclusion, shippers will continue, for economic and logistical reasons, to carry out the business of shipping cargo through the use of intermediary companies such as freight forwarders

whose business is to keep on top of market developments, rates and the preparation of documentation. However care must be taken in the choice of freight forwarders. It is a prudent shipper that conducts a due diligence investigation of the forwarder's reputation in the community. Other steps, as suggested by the court, could be taken, such as requesting written assurance that the carrier was looking only to the forwarder for payment.

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