# A Legal and Economic Analysis of the Volume Contract Concept under the Rotterdam Rules: Selected Issues in Perspective

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***Abstract***

*The prevailing regimes for the carriage of goods by sea are "one-way mandatory," which means that contracts must not derogate from the convention to the shipper's detriment, but derogation that increases the carrier's obligations is allowed. The Rotterdam Rules provides for volume contracts that allow the parties to enter into mutually negotiated agreements through which they can derogate from the Rules, subject to certain safeguards, regardless of whether such derogation increases or decreases the carrier's obligations.*

*This article attempts to probe into the emergence of the contract paradigm of free bargaining norms where there is in place a volume contract. The uniqueness of individual contracts between shippers and carriers has long been recognized in the United States. This uniqueness, it would appear, has influenced the development of the volume contract concept in the Rotterdam Rules and has provided the impetus for introducing bargaining freedom in carriage of goods wholly or partly by sea.*

*The article analyzes the various economic and legal implications associated with volume contracts such as distributional consequences among shippers, the trade-off between efficiency and equity, and the connection between freedom of contract and discrimination in terms of trade practices inherent in the liner conference system. Furthermore, an examination is made of the co-related issues such as implications of volume contracts on the global supply chain management and explores its future role in international trade.*

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## 1. Introduction and Background

Evolving from an original initiative of the Comité Maritime International (CMI), Working Group III (Transport Law) of the United Nations Commission on International Trade Law (UNCITRAL) has spearheaded the creation of a new international regime for the carriage of goods by sea, the ultimate objective of which is to replace the present fragmentation[1] in this area of maritime law. This state of affairs manifested in the coexistence of three sets of international convention rules, namely the Hague Rules[2], the Hague-Visby Rules[3] and the Hamburg Rules[4] and the proliferation of national "hybrid" regimes[5]. The situation is worsened by these hybrid regimes often applying inwards and outwards, thus creating a nightmare for legal practitioners and their clients in terms of conflict of laws issues.[6] In view of the urgency of the situation, two international bodies, the CMI and UNCITRAL joined forces to promote reform in the law of international sea carriage of goods.[7]

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[1] See Michael F. Sturley, "Uniformity in the Law Governing the Carriage of Goods by Sea" (1995) 26 J. Mar. L. & Com., at p. 553; Paul Myburgh, "Uniformity or Unilateralism in the Law of Carriage of Goods by Sea?" (2000) 31 VUWLR, at p. 355; William Tetley, "The Proposed New United States Senate COGSA: The Disintegration of Uniform Carriage of Goods by Sea Law" (1999) 30 J. Mar. L. & Com., at p. 595.

[2] The International Convention for the Unification of Certain Rules Relating to Bills of Lading, 25 August 1924, 1924, 51 Stat. 233, T.S. No. 931, 120 L.N.T.S. 155, hereinafter referred to as the "Hague Rules".

[3] The Protocol to Amend the International Convention for the Unification of Certain Rules Relating to Bills of Lading 1924, 23 February 1968, 1421 U.N.T.S. 121, 1977 Gr. Brit. T.S. No. 83 (Cmnd. 6944) (entered into force 23 June 1977), hereinafter referred to as the "Hague-Visby Rules.

[4] United Nations Convention on the Carriage of Goods by Sea, 31 March 1978, 17 I.L.M. 608, hereinafter referred to as the "Hamburg Rules". The Hamburg Rules was a product of the efforts of United Nations Conference on Trade and Development (UNCTAD) and UNCITRAL with little input from the CMI. See David C. Frederick, "Political Participation and Legal Reform in the International Maritime Rulemaking Process: From the Hague Rules to the Hamburg Rules", (1991) 22 J. Mar. L. & Com. 81, at pp. 103-106 (contrasting the U.N. negotiating process that produced the Hamburg Rules with the earlier processes that produced the Hague and Hague-Visby Rules).

[5] China, one of the world's largest trading nations, has a national maritime code that incorporates elements of both the Hague-Visby and Hamburg Rules along with domestic elements that are unique to Chinese law. The Nordic countries have incorporated significant elements of the Hamburg rules into their domestic versions of the Hague-Visby Rules. See for example, S. Hetherington, "Australian Hybrid Cargo Liability Regime" (1999) LMCLQ, at p. 12; J. Ramberg, "New Scandinavian Maritime Codes" (1994) Dir. Mar., at p. 1222; Rok Sang Yu & Jongkwan Peck, "The Revised Maritime Section of the Korean Commercial Code" (1999) LMCLQ, at p. 403; Li, "The Maritime Code of the People's Republic of China" (1993) LMCLQ, at p. 204, In Hyeon Kim, "Korean Maritime Law Update: 2007 - Focused on the Revised Maritime Law Section in the Korean Commercial Code", (2008) 39 J. Mar. L. & Com., at p. 433.

[6] See for example, Francesco Berlingieri, "The Hamburg Rules: A Choice for the EEC?", International Colloquium held by European Institute of Maritime and Transport Law on 18 and 19 November, 1993.

[7] For much of the 1980s and 1990s, while advocates of the Hague-Visby and Hamburg Rules battled over the direction that cargo liability law should take many observers viewed the CMI and UNCITRAL as rivals, at least on this issue. But UNCITRAL's return to the field of transport law has been in active partnership with the CMI. Since 1998, the two organizations have been fully cooperative allies seeking to develop a new international convention that will be widely acceptable to the world maritime community. The two organizations have their unique strengths; CMI has greater access to industry representatives, while UNCITRAL mainly works with government representatives and international organizations. Thus, by joining their efforts they have paved the path for building necessary consensus for the widespread adoption of a new convention. For a comprehensive explanation of the interrelationship between these two bodies, see Michael F. Sturley, "The United Nations Commission on International Trade Law's Transport Law Project: An Interim View of a Work In Progress", (2003) 39 Tex. Int'l L.J. 65, at p. 69.

The final product after almost a decade of deliberations has crystallized through the adoption of a convention instrument called the "United Nations Convention on Contracts for the International Carriage of Goods Wholly or Partly by Sea"[8], otherwise referred to as the "Rotterdam Rules".

In private law conventions, national and private interests with commercial, economic and other implications are at stake, with the result that international rule-making is often fragmented. In the law of carriage of goods by sea, the lack of uniformity in the international law is glaringly obvious. As witnessed in recent times, when discussions on the law of carriage of goods by sea under bills of lading reach the stage of a diplomatic conference, the characters of the play are mainly restricted to the shipper and the carrier. The storyline is mainly focused on the debate surrounding the contractual imbalance between carrier and shipper due to the unequal bargaining power in relation to clauses which define and limit the liabilities of the parties to the contract of carriage. The implicit metaphor epitomizes a world of conflict rather than cooperation, a confrontation rather than a deal, in which only if a side is sufficiently powerful can it expect its concerns to be included in the final convention.

Since the time of the Harter Act the debate on contractual imbalance has revolved around the need to protect cargo interests by certain mandatory minimum liability rules for the carrier. The contractual imbalance, it is alleged, is attributable to the philosophy underlying the Hague Rules or the Hague-Visby Rules which dominate current carriage transactions. With the demise of colonialism and the emergence of independent sovereign states which were at the time referred to as the third world states, the Hamburg Rules were developed to accommodate their interests. From a macro perspective, the imbalance is recognized as a function of the conflict between states whose international trade is based on cargo owning interests, namely shipper or consignee, and states whose international trade is based on carrier interests, *i.e.*, shipowners, charterers and the like. It must be appreciated in this context that ships of a large flag state are not necessarily owned by individuals who are nationals of that state or companies incorporated in and directed from that state. Indeed in the realm of open registries today in many instances, neither is the individual shipowner a national of the flag state, nor is the mind and management of a shipowning company resident there even if the company is incorporated in the flag state.[9]

It is also to be noted that states which identify themselves primarily with cargo owning interests may also be major flag states regardless of whether they operate in an open or closed registry system or any other alternative type of registry. Therefore, the assumption that there is an irreconcilable divide between traditional maritime states as representing carrier interests and developing countries with primarily cargo owning interests is no longer valid. The advent of multiple registry types leading to varieties of flag states has in practical terms obliterated the original polarized

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[8] The final text of the Convention (hereinafter Rotterdam Rules) is annexed to General Assembly Resolution 63/122, UN Doc A/RES/63/122. It was also annexed to the "Report of the United Nations Commission on International Trade Law on the work of its forty-first session", UN Doc A/63/17 (2008), Annex I.

[9] In present times, more than half of the world's merchant ships (measured by tonnage) are registered under open registries. Panama, Liberia and Bahamas, all developing states are the leading open registries in the world.

characteristics of states opting for the Hague/Hague-Visby regimes or the Hamburg regime.

The mandatory minimum liability for the carrier under the Hague and Hague-Visby Rules, was also created to enhance the negotiability function of the bill of lading. The Hague/Hague-Visby regimes follow the "documentary" approach, under which the application of the convention would turn on the issuing of a particular type of document. A bill of lading issued under the Hague and Hague-Visby regimes extend certain protections to third party bill of lading holders not only as a negotiable document which ensures control over the disposition of the goods, but also protection in terms of carrier liability. The Hamburg regime follows the "contractual" approach, under which application of the Rules would depend on the parties concluding a particular type of contract, without regard to whether a particular document was issued. The Rotterdam Rules follows a hybrid approach but the application of the Rules is mainly contractual which is defined by the contract of carriage itself.[10]

The prevailing regimes of the Hague Rules, the Hague-Visby Rules and the Hamburg Rules are aptly described as "one-way mandatory," which means that the contracts must not derogate from the convention to the shipper's detriment; but derogation that increases the carrier's obligations is allowed.[11] Consistent with the approach of the existing regimes, the Rotterdam Rules was originally conceived as a convention incorporating essentially mandatory rules for all parties.[12]

It is of utmost importance, however, to recognize that in the carrier-shipper relationship there is another dimension which is the trade relationship. This component is equally important as the liability regime, if not more so, in terms of the wider picture of international trade enmeshed with carriage of goods across continents. This article focuses on this second component through a discussion of volume contracts as that concept is placed within the legal framework of the Rotterdam Rules embracing carriage of goods by sea as well as non-maritime modes in their proper perspective.

The uniqueness of individual contracts between shippers and carriers has long been recognized in the United States. This uniqueness, it would appear, has influenced the development of the volume contract concept in the Rotterdam Rules and has provided the impetus for resorting to bargaining freedom in carriage of goods wholly or partly by sea in certain instances.

Against the above background the remainder of the article proceeds in six sections. The concept of service contracts as practiced in the United States is discussed in section 2. In section 3 the volume contract concept which flows from the

[10] Article 1(1) of the Rotterdam Rules defines "contract of carriage" as "a contract in which a carrier, against the payment of freight, undertakes to carry goods from one place to another. The contract shall provide for carriage by sea and may provide for carriage by other modes of transport in addition to the sea carriage."

[11] See in particular article 3(8) of the Hague/Hague-Visby Rules and article 23 of the Hamburg Rules.

[12] See "Preliminary draft instrument on the carriage of goods by sea", UN Doc A/CN.9/WG.III/WP.21, article 17.1, "…. any contractual stipulation that derogates from this instrument is null and void, if and to the extent that it is intended or has as its effect, directly or indirectly, to exclude, [or] limit [, or increase] the liability for breach of any obligation of the carrier, a performing party, the shipper, the controlling party, or the consignee".

service contract is critically analyzed through the examination of a number of hypothetical business scenarios. The implications of volume contracts on shippers and carriers from the perspective of global supply chain management and its necessity to support the present day business model of carriers and shippers are also explored in this section. The current model evolved from the time containerization started to predominate in the mid twentieth century. A critical legal analysis of the volume contract provisions under the Rotterdam Rules is provided in section 4. These provisions were carefully crafted after long deliberations at the Working Group III meetings of UNCITRAL to strike a delicate balance between shipper and carrier interests. In section 5, a comparative analysis of the positions of the parties to a volume contract is presented by reference to the Rotterdam Rules and other existing carriage of goods by sea regimes. In section 6, a critique of the volume contract concept is presented. The final section provides a summary of the discussion on volume contracts and certain conclusions with respect to the Rotterdam Rules as a whole.

## 2. The United States Concept of Service Contracts

At the twelfth session of the Working Group III meetings, the United States delegation made a proposal regarding the so-called "Ocean Liner Service Agreement" (OSLA) otherwise known as service contracts, suggesting that it be included within the scope of the Rules but that in respect of such agreements certain provisions of the Rules be made non-mandatory. [13] A "service contract" in the United States is defined under the Shipping Act of 1984[14] and the draft version of the United States Carriage of Goods by Sea Act of 1999[15]. It is defined by section 3(19) of the Shipping Act of 1984 as –

> a written contract, other than a bill of lading or a receipt, between one or more shippers and an individual ocean common carrier or an agreement between or among ocean common carriers in which the shipper or shippers makes a commitment to provide a certain volume or portion of cargo over a fixed time period, and the ocean common carrier or the agreement commits to a certain rate or rate schedule and a defined service level, such as assured space, transit time, port rotation, or similar service features. The contract may also specify provisions in the event of non-performance on the part of any party.

The proposal contemplated allowing more flexibility to the parties resorting to OSLAs in the allocation of their rights, obligations and liabilities. In their view, parties should enjoy the freedom to derogate from the provisions of the Rules, under certain circumstances.[16]

Based on this proposal, the Rotterdam Rules provide for volume contracts that allow the parties to enter into mutually negotiated agreements, subject to certain

[13] See, "Proposal by the United States of America, Ocean liner service agreements", UN Doc A/CN.9/WG.III/WP.34, paras. 18-29, at pp. 6-9.
[14] The Shipping Act of 1984 of the United States, 46 U.S.C. App. § 1701-1719, as amended by the Ocean Shipping Reform Act of 1998, .Pub. L. 105-258, 112 Stat. 1902 (1998).
[15] The U.S. Senate COGSA '99 (September 24, 1999) defines service contract by reference to the Shipping Act of 1984.
[16] *Ibid.*

safeguards to derogate from the terms of the Rotterdam Rules, regardless of whether such derogation increases or decreases the carrier's obligations.

The United States proposal on the OLSA emphasized that flexibility should be granted whenever one or more shippers and one or more carriers enter into agreements providing for the transportation of a minimum volume of cargo in a series of shipments on vessels used in a liner service, and for which the shipper or shippers agree to pay a negotiated rate and tender a minimum volume of cargo. It is to be noted that the definition of volume contract as found in the Rotterdam Rules is broader than that of service contract under the United States Shipping Act of 1984, as it does not require the carrier to undertake any 'defined service level' or to commit to a certain rate or rate schedule. Instead, volume contract is defined solely by reference to the undertakings of the shipper to provide a certain quantity of goods for shipment.

Before delving into the intricacies of the relationship between shipper and carrier entering into a volume contract under the Rotterdam Rules, it would be of interest to trace the origins of service contracts in the United States. This discussion will provide an understanding of the vital need to include volume contracts in the Rotterdam Rules.

The differential treatment of apparently similarly situated shippers was not allowed in the United States for nearly a century. Equal treatment of all shippers, strictly based on published prices and terms of service, was in popular belief considered essential for a fair shipping market.[17] However, the economic wisdom of deregulation of the seaborne cargo regime in the United States between 1984 and 1998 was borne out by the superior performance of the ocean liner market under normal price competition, contrary to long-standing claims from the shipping industry and various academics.[18] Some scholars have concluded that the most important result of freight deregulation was the end of the ban on discrimination which has substantial aggregate benefits for shippers and the economy.[19] However, little has been said in

[17] See Marc Levinson, "Two Cheers for Discrimination: Deregulation and Efficiency in the Reform of U.S. Freight Transportation, 1976–1998" published by Oxford University Press on behalf of the Business History Conference (2008), at p.178.

[18] Prior to the deregulation process in the United States, a body of theoretical work grew to support claims from ocean carriers, bolstering the argument that they required antitrust immunity. See Stephen Craig Pirrong, "An Application of Core Theory to the Analysis of Ocean Shipping Markets", 35 J.L. & Econ. 89 (1992); William Sjostrom, "Antitrust Immunity for Shipping Conferences: An Empty Core Approach", *Antitrust Bull*., Summer 1993, at p. 419.

[19] For example, Elizabeth E. Bailey, 'Price and Productivity Change Following Deregulation: The US Experience' *The Economic Journal*, Vol. 96, No. 381 (1986), at p. 15, asserts that "the 'losers' from deregulation have been far fewer than might have been imagined… the 'gainers' have included business users most of all as cross-subsidy has ended …" A criticism against Bailey is that she ignores the possibility that businesses could lose from deregulation if their relative freight costs rose as compared to other domestic companies or to competing importers, even if their freight costs fell in absolute terms. Paul W. MacAvoy, *Industry regulation and the performance of the American economy* New York: W.W. Norton, (1992), focuses entirely on the efficiency gains from a macro perspective. From a road transport perspective some authors find that freight transport deregulation brought large economic gains to shippers but add that "the distributional effects that probably exist between small and large shippers make it very unlikely that all shippers have shared in the benefits;" on the distributional point, however, they present no evidence; see Clifford Winston, Thomas M. Corsi, Curtis M. Grimm, Carol A. Evans, *The Economic Effects of Surface Freight Deregulation*, Brookings Institution Press (1990), at p. 41. Mark H. Rose, Bruce E. Seely, and Paul F. Barrett, *The Best Transportation System in the World: Railroads, Trucks, Airlines, and American Public Policy in the*

the United States in published literature or court decisions on the distributional consequences of service contracts among shippers and the communities in which they are located. The incorporation of volume contracts in the Rotterdam Rules has brought this issue into the forefront internationally. The distributional consequences are difficult to measure even though information on average ocean shipping rates for containers on certain trade routes is available, because there is no information available in the public domain on rates paid by individual shippers or the service terms associated with the published prices.

Prior to 1984, all ocean freight to or from the United States moved under published tariffs and most international shipping lines belonged to liner conferences. These conferences are cartels whose memberships comprise seagoing common carriers engaged in providing sea transport services under a common tariff, deriving their legitimacy largely from statutory enactments supporting their contractual arrangements.[20] The genesis of the conference system dates back to 1875. The first liner conferences covered trade in routes between Britain and India at the behest of leading British carrier companies.[21] Carriers in the United States followed the British example around the turn of the century. Liner shipping progressed under the conference system and remained largely unchanged until the mid-twentieth century when containerization became predominant.

In the United States a shipping line could choose to join a liner conference or operate outside it if it so wished but the conferences were under compulsion to make themselves available to all shipping lines. The rate structure for goods comprised three levels of possibilities, the first being the standard rate. If a shipper signed a loyalty contract with the carrier, it could gain a benefit of some 15 percent.[22] Under this second level arrangement, the shipper would have to commit the whole of the cargo to the conference or a fixed portion thereof. This arrangement could be risky for the shipper if the first available conference ship happened to be fully booked resulting in a waiting period for the next conference ship with sufficient available space. The third option, the most economical one, would be for the shipper to go with an independent carrier who was not a member of a conference and pay the published

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*Twentieth Century*, Columbus: Ohio State University Press, (2006) at pp. 212–239, ignore discrimination in the wake of deregulation altogether. Richard Vietor, *Contrived Competition: Regulation and Deregulation in America*, Belknap Press (1996) at p. 320, emphasizes that deregulation destroyed existing market segmentation and forced companies to devise new strategies for segmenting markets, although he does not discuss freight specifically. Laurence T. Phillips, 'Contractual Relationships in the Deregulated Transportation Marketplace' 34 *Journal of Law and Economics*, (1992), at pp. 535-564, undertakes a many-faceted examination of the role of contracts in freight transportation, albeit with only minimal evidence on contracts between carriers and shippers. Marc Levinson, *supra* note 17, at p. 179 asserts that studies of the cost impact of maritime deregulation are almost totally lacking, due to unavailability of accurate public information about freight costs.

[20] The Shipping Act of 1984 of the United States, 46 U.S.C. app. § 1702 (7) (2001) defines conference as "an association of ocean common carriers permitted, pursuant to an approved or effective agreement, to engage in concerted activity and utilize a common tariff; but the term does not include a joint service, consortium, pooling, sailing, or transhipment arrangement."

[21] The Calcutta Conference was the first and was created at the urging of the steamship leader Sir Samuel Cunard. There is evidence of prototypical conferences existing as early as the 1850s, though they were not modern in the sense that they seem never to have agreed on prices or output. See Chris Sagers, 'The Demise of Regulation in Ocean Shipping: A Study in the Evolution of Competition Policy and the Predictive Power of Microeconomics' 39 Vand. J. Transnat'l L. 779, footnote 37.

[22] See *supra* note 17, at p. 201.

rate, provided the carrier was able to handle the business. The risk involved in this option was the possibility of the independent carrier's under-capacity compelling the shipper to ship some of its cargo with a conference carrier. In that case the shipper would have to pay the standard tariff and its overall cost would be considerably higher than the cost it would have incurred under a loyalty contract.

All the above-noted arrangements required the publication of tariffs for all commodities which had to be filed with the Federal Maritime Commission (FMC). As such, the tariffs were publicly available to all prospective shippers and no special treatment by the carrier was allowed in the form of a volume discount or provision of some other preferential service.

Then the 1984 Shipping Act was enacted which was a pioneering piece of legislation heralded as the start of the deregulation process in the United States. Shipping lines were permitted to offer rates based on time and volume of cargo so that the rates varied with cargo volume tendered over a specified period. Obviously, it was the large shippers who benefitted from this liberalization and unsurprisingly, those who opposed it were the same ones who were against any discrimination benefitting large shippers. These were the traditional supporters of regulation in the field of seaborne trade.

Furthermore, under the Act, shipping lines and liner conferences were allowed to enter into arrangements known as service contracts with shippers under which the shipper would agree to provide a designated volume of cargo over a specified period of time. By so doing, it was envisaged that the shipper would secure preferential freight rates as well as a host of other positive returns such as shipboard guarantee of space, orderly sailings and overall reliability of service. Often these contracts would provide coverage of service extending to shore side transportation; in other words, the entire logistical chain could be rendered undivided in so far as billing was concerned. Liquidated damages provisions in the contract were permissible under the legislation for failure of performance of obligations.

The 1984 Act also permitted a departure from the published conference rates through "independent action". Tariffs published under independent action averaged 11-25 percent below standard conference tariffs with respect to a specified commodity.[23] These independently generated rates could force conference carriers to bring down their own published rates in order to compete. Thus the Act engendered a system whereby shippers could freely negotiate rates to their advantage but the necessary terms of a contract had to be made public without discrimination. The hallmarks of common carriage were thus preserved in conjunction with a considerable degree of deregulation of economic transactions between carriers and shippers such as discrimination in relation to volume of cargo. Although the Shipping Act of 1984 permitted service contracts, the effect of that permission was very limited, because of the requirement in the statute that the terms and conditions of the contract had to be publicly available and could be demanded by other similarly-situated shippers. But, it was often not clear what attributes constituted a "similarly-situated" shipper. Of course, the market forces reacted; when a shipping line offered a rate reduction from

[23] U.S. Federal Maritime Commission, "Section 18 Report on the Shipping Act of 1984," September 1989 at p. 130.

the conference rate, several small volume shippers wanted to jump on the bandwagon with the so-called "me too" contracts causing carriers to recoil so that only large volume shippers who quickly moved in on the action succeeded. Thus, the 1984 Shipping Act by legitimizing rate discrimination was viewed as favouring large shippers against the interests of their smaller counterparts. It would appear that technically the service contract concept endorsed and supported by legislation largely benefitted the major shippers who had considerably more bargaining clout. However, the conditions under which such discrimination took place was conceivably narrow which made the possibility of such discrimination not widely practical. In fact, it is argued that the "me too" provision in the statute really re-established with the left hand the anti-rate discrimination policy which the service contract provision in the Shipping Act tried to give with the right hand.

Finally, the Ocean Shipping Reform Act enacted in 1998 allowed confidentiality of rates in service contracts and abolished the requirement for carriers to cater to small shippers who wanted similar rates. The new Act by removing the "me-too" requirement and providing for confidentiality fulfilled the formal promise that was in the Shipping Act of 1984 but which was never actualized by the restrictions in that Act. As a result, service contracts came into more frequent use and virtually became the norm through which rates were set.[24] These contracts could cover even a unit as low as a single container.[25] Removal of all of the regulatory strictures made possible by this Act including the legitimization of confidentiality and elimination of the compulsion to offer similar terms to similar shippers became most advantageous for the mega shippers who had negotiating power far in excess of small shippers.

The reduction in barriers to world trade and the emergence of international production centres in Asia impacted the flow of global trade and strategic approaches to international maritime transport. The reforms in 1998 enabled globalized manufacturers and retailers to gain advantageous contractual arrangements which were based on market reference points. While the cost to the shipping line was the base for these arrangements, they were essentially according to market reference points. In other words, the price set was the cost to the manufacturer as the floor, but the actual price established was often well above this level; as high as the market would bear. This shift in philosophy was largely seen as benefitting the major players among the shippers simply because they were the ones who could on a temporal basis supply large volumes of commodities. This in turn enabled carriers to benefit from lower costs.[26] A relevant question in this regard was whether the arrangements engendered by the service contract concept strongly endorsed by legislation exemplified a balance of bargaining power between carriers and shippers or whether it manifested itself as an enhancement of the commercial powers of large shippers. Information itself became a valuable commodity for both parties concerned since rates were no longer required to be published and confidentiality became the rule of the day. Again it was the larger shippers who were better equipped to access

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[24] U.S. Federal Maritime Commission, "The Impact of the Ocean Shipping Reform Act of 1998," September 2001, at p. 84.

[25] *Ibid.*, at pp. 21–22.

[26] See Hayden G. Stewart, and Fred S. Inaba, "Ocean Liner Shipping: Organizational and Contractual Response by Agribusiness Shippers to Regulatory Change." *Agribusiness* 19 (2003) at p. 462. Data on contracts signed by shipper associations are from *American Shipper*, Feb. 1992, at p. 42.

information pertaining to the market better than their smaller counterparts.[27] The information in turn became a formidable bargaining tool.

While it is recognized that the service contract concept has benefited large shippers, there has been a strong complementary trend that has benefited smaller shippers through the growth of large consolidators such as FedEx, UPS and DHL as well as others, on the international scene. Some of these consolidators have evolved from small entities operating out of a basement or small office to large and sophisticated shipping, logistics management and supply chain management service providers with operations and offices all across the globe. There is considerable competition among these consolidators which have given them every incentive to negotiate major discounts with asset-based ocean carriers and to pass a good portion of those savings on to their own customers. These have enabled many smaller shippers to get at least part of the benefit of the volume discounts experienced by large shippers. Moreover, as indicated earlier these large consolidators often offer supply-chain management services as well, to the benefit of smaller shippers.[28]

The service contract arrangement based on time-volume supply of goods enabled shippers to make substantial savings on their inventories which in some instances were higher than their savings on freight. This major advantage in the context of service contracts can easily be transposed into the volume contract regime introduced through the Rotterdam Rules. Similar advantages can be gained through a typical volume contract arrangement not only in terms of savings as indicated above, but also provide carriers the opportunity to integrate their operations into the land based logistics side of the global supply chain. Viewed in this light, the management of logistical arrangements can and is gradually becoming an industry in its own right. Such management would include a variety of logistical activities including shore side transportation, warehousing and reduction of inventory costs. It is stated that advantages such as this would not have been possible without arrangements typical of the volume contract as they can provide commodity owners protection against the risks of stocking and restocking their inventories without the disadvantage of irregularity of shipments.

## 3. Evolution of the Volume Contract Concept and its Economic Implications

A volume contract is defined in article 1(2) of the Rotterdam Rules as "a contract of carriage that provides for the carriage of a specified quantity of cargo in a series of shipments during an agreed period of time. The specification of the quantity may include a minimum, a maximum or a certain range." A transport document[29] or electronic transport record[30] may be issued in respect of each shipment. The word

[27] See *supra*, note 25.

[28] Information gleaned through personal communications with Mr. Nicholas DiMichael.

[29] Article 1(14) of the Rotterdam Rules defines "transport document" as a document issued under a contract of carriage by the carrier that: (a) Evidences the carrier's or a performing party's receipt of goods under a contract of carriage; and (b) Evidences or contains a contract of carriage.

[30] Article 1(18) of the Rotterdam Rules defines "electronic transport record" as information in one or more messages issued by electronic communication under a contract of carriage by a carrier, including information logically associated with the electronic transport record by attachments or otherwise linked to the electronic transport record contemporaneously with or subsequent to its issue by the carrier, so as to become part of the electronic transport record, that: (a) Evidences the carrier's or a performing

‘quantity’ and the illustrated methods of measurement, suggest bulk cargo carried in the hold of a ship or containerized goods. Based on such presumptions a volume contract might take the form of a liner contract[31] or a non-liner contract[32].

An initial observation in this context is that the term volume contract is used in commercial transactions to refer to a particular variety of contract of affreightment (CoA). As pointed out by one distinguished commentator the chosen terminology has the potential to lead to convolution by virtue of a specific definition given to that term in the Rotterdam Rules.[33] This is apart from the fact that there is the parallel concept of service contracts in the United States as discussed above. It is apparent from the discussion in section 2 above that the introduction of the contract paradigm of free bargaining norms where there is in place a volume contract in the Rotterdam Rules is quintessentially similar to service contracts in the United States.

In the context of the above noted definition of volume contracts it is important to distinguish between volume contracts and rate agreements. In the latter case, a shipper asks for a price quotation for an ‘estimated but not guaranteed’ quantity of goods to be shipped during a certain period in the future. If the carrier provides such a quotation, it is not an offer for a volume contract because the quantity is not guaranteed. Even when the shipper makes use of the offered tariff for an individual shipment, there is still no volume contract. In practice, as soon as another carrier offers a lower rate, the shipper may decide to use such other carrier because there is no commitment to the first carrier regarding any volume. In practical economic terms, this practice of rate agreements results in the agreed rate being the maximum rate over a certain period. If and when the spot rate is lower than the contract rate, the shipper chooses the spot rate; and vice versa if the spot rate is higher. It is in the interest of shippers to conclude this type of rate agreement with several carriers on a certain trade.[34]

The following hypothetical business scenarios illustrate typical situations in which volume contracts are used as defined in the Rotterdam Rules.[35]

*Illustration 1:*

A steel mill in Belgium (B) buys 1 million tons (plus/minus 5 per cent) iron ore from an Australian (A) mining company under FOB terms, to be delivered during

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party’s receipt of goods under a contract of carriage; and (b) Evidences or contains a contract of carriage.

[31] “Liner shipping” is an industry term of art which means regularly scheduled common carriage of cargo by sea, which is now by far the predominant means of ocean transport but which has only existed since about the time of the Civil War; see Amos Herman, *Shipping Conferences*, Deventer, Netherlands; Boston: Kluwer Law and Taxation Publishers, (1983). Article 1(3) of the Rotterdam Rules defines “liner transportation” as a transportation service that is offered to the public through publication or similar means and includes transportation by ships operating on a regular schedule between specified ports in accordance with publicly available timetables of sailing dates.

[32] Article 1(4) of the Rotterdam Rules defines “non-liner transportation” as any transportation that is not liner transportation.

[33] See D Rhidian Thomas, “The Emergence and Application of the Rotterdam Rules”, Proceedings from the International Colloquium on Cargo Claims under the International Conventions from the Hague to the proposed Rotterdam Rules, 10-11 September 2009, at p.7.

[34] Gleaned from personal communications with Professor G. J. van der Ziel.

[35] *Ibid.*

the next calendar year. After conclusion of the sale/purchase contract, the FOB buyer asks for a quotation in the shipping market for the carriage of 1 million tons of iron ore, to be shipped from A to B in six voyages evenly spread over the year. Often, such tender includes a sample contract with numerous charterparty-type clauses. The transportation need is for six cape size bulkers every two months to carry the total shipments. This type of contract is referred to as a 'contract of affreightment' (CoA). For the steel mill the business purpose is to secure cargo space and to obtain certainty regarding the rate involved. For the carrier the purpose is to obtain certainty of employment of its own or chartered tonnage. It is estimated that most of the world trade in raw materials is carried by sea under such CoA's which are port-to-port contracts in almost all cases. Aside from the particulars of the vessels such as type, size, maximum draft, age, *etc*., there are no particular logistical issues involved in such contracts.

In some instances a charterparty is used for each shipment; sometimes the CoA itself functions as a charterparty. In both cases, a bill of lading is issued for each individual shipment. Under a typical standard FOB contract, the FOB buyer is the contractual shipper, but the shipper named in the bill of lading usually will be the FOB seller[36] because this person needs the bill of lading for the purpose of submitting it to the bank indicated by the FOB buyer. This bank is often referred to in the 'consignee box' as "to the order of the ABC Bank". In this scenario, the Rotterdam Rules do not apply to the CoA and the charterparty, because according to article 6 (1) such contracts are excluded from its scope of application[37]. By virtue of article 7, however, the Rotterdam Rules apply to the bill of lading when this document is in the hands of the FOB seller/shipper, the bank and any other holder except the FOB buyer who is the contractual shipper. When the contract of sale is not a typical standard FOB contract but another type of FOB contract[38], the seller may have to conclude the contract of carriage on behalf of the FOB buyer. Then, such seller acts as agent of the fob buyer and, as a consequence thereof, the Rotterdam Rules also do not apply as between the carrier and the FOB seller.

*Illustration 2:*

A large exporter of manufactured non-consumer goods in South Africa sells its products to many buyers in various parts of the world on delivered terms, C or D terms of INCOTERMS. The exporter invites quotations for all shipments to be carried out over the next calendar year to destinations in Europe (estimated 20,000 TEU), to the United States (estimated 30,000 TEU) and to the Far East (estimated 40,000 TEU). The cargo is to be shipped in certain minimum/maximum quantities on a weekly basis. This is a typical requirement for a container liner volume contract. For each of the three destinations a different carrier may be chosen. The carrier that wins the Far East contract has to carry on average 770 TEU per week in total to different destinations in the Far East, say Singapore, Djakarta, Manila, Hong Kong, Shanghai, Pusan and two Japanese ports, and sometimes with different liner services. These contracts may include port-to-port carriage or multimodal carriage at one end or at both ends.

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[36] In terms of the Rotterdam Rules such FOB seller is a 'documentary shipper'.
[37] The CoA is viewed as a contract for the use of a ship which in this example is six ships.
[38] In *Pyrene Co Ltd* v. S*cindia Navigation Co Ltd* [1954] 2 Q.B. 402 Devlin J. identifies three varieties of FOB contract of sale. See also Charles Debattista, *Bills of lading in Export Trade*, Tottel Publishing (2008), at p. 9 – 11.

This is a type of volume contract which may involve varieties of logistical requirements such as shipment of the cargo from an irregular port of call and, in the event that the consignee has no storage space, delivery on a daily basis. The business purpose for the shipper/seller is to secure cargo space for its exports, to obtain certainty about the transport rates as part of his cost price of the product to be sold and, if applicable, to agree on special logistical requirements. Usually, for each shipment and each destination a regular bill of lading will be issued, in which the shipper is the seller and the goods are consigned to the buyer or 'buyer's bank or order'.

In this illustration, whether or not the Rotterdam Rules apply to the volume contract depends on its wording. If it is worded as the hire of space in a vessel ('slot charter') the Rules will not apply to the volume contract itself pursuant to article 6 (1) (b), but according to article 7 the Rules will apply as between the carrier and the third party holder of the bill of lading, such as the consignee/buyer of the goods. If the volume contract is not worded as hire of space in a vessel the Rotterdam Rules will apply to the volume contract and to each individual shipment made under this contract. Although under this type of volume contract the seller bears the transport risk because the goods are sold under delivered terms, it is hardly ever the case that the exporter asks for carrier liability at a level less than what is provided under the Hague-Visby Rules. This is because under D-INCOTERMS a seller must conclude the contract of carriage under 'the usual terms'.

*Illustration 3:*

A variant of *Illustration 2* may be the case of a manufacturer of consumer goods located in a high cost country, such as the United States. Such a manufacturer will often farm out the actual production of these goods to a facility located in a low cost country, for example in Asia, and transport them in large quantities to high cost areas where they will be retailed. Under these contracts there may be different destinations. The purchase contracts of such goods will mostly be made on an FOB basis. The volume contracts in question may be concluded by a carrier and the central purchase department of the manufacturer, which contracts on behalf of its local subsidiaries who eventually sell the goods to the retailers. Shippers under the bills of lading are the sellers/actual manufacturers of the consumer goods in the low cost country and consignees are the local subsidiaries in the destination country. Under this variant the logistical elements and the business purpose may be the same as under *Illustration 2*.

The application of the Rotterdam Rules, again, depends on the wording of the volume contract. If it is worded as the hire of space in a vessel ('slot charter') the Rules would not apply to the volume contract itself pursuant to article 6 (1) (b). To what extent the Rotterdam Rules apply to an individual shipment will depend on the type of FOB contract of sale. If this contract is a typical standard FOB contract, the seller, mentioned as (documentary) shipper in the bill of lading, is not an original party to the contract of carriage and, pursuant to article 7, the Rotterdam Rules will apply as between the carrier and such shipper as well as between the carrier and any other holder of the bill of lading except the consignee on whose behalf the contract of carriage has been concluded by the above-mentioned central purchase department. If the contract of sale is not a typical standard FOB contract and the FOB seller,

mentioned as (documentary) shipper in the bill of lading, concludes the contract of carriage with the carrier nominated by the consignee or the above mentioned central purchase department on behalf of or any of the latter two, pursuant to article 7, the Rotterdam Rules will not apply as between the carrier and the (documentary) shipper and as between the carrier and the consignee because both the (documentary) shipper and the consignee have to be regarded as the original party to the contract of carriage. In the latter case, however, the Rotterdam Rules will apply as between the carrier and any third party holder of such bill of lading, such as the buyer's bank to which the seller has to submit the bill of lading in order to obtain the purchase price of the goods. If the volume contract is not worded as the hire of space in a vessel the Rotterdam Rules apply to the volume contract and to each individual shipment made under this contract. Under this type of volume contract the buyer bears the transport risk because the goods are sold under FOB terms. This buyer may agree any special terms with the carrier within the limits of article 80. Often, the balance of bargaining power between the carrier and the cargo interest is on the side of the latter, which may result in the cargo interest dictating terms to the carrier.

*Illustration 4:*

An automobile manufacturer wishes to send automobile parts to an overseas assembly plant. The transportation contracts may involve large quantities and special logistical features. In such cases the shipper and consignee usually belong to the same economic entity and no trade financing bank is involved. When the volume contract is worded as a contract for the hire of a vessel, the Rotterdam Rules will not apply. If the seller concludes the volume contract on behalf of the consignee which is often the case in these types of volume contracts, the Rules will not apply to the bill of lading issued under the individual shipment because there is no third party involved. If the contract is not worded as a contract for the hire of a vessel, the Rules will apply to the volume contract and the individual shipments made thereunder. In such a case, the seller may agree any special terms with the carrier within the limits of article 80. As in *Illustration 3* above, the balance of power is often on the side of the cargo interests with all the consequences thereof.

It is apparent from the above practical illustrations of scenarios compatible with the volume contract concept that efficiency in seamless transportation which forms part of the global supply chain management is greatly enhanced. The object of global supply chain management is to link the market place, distribution network, manufacturing or processing or assembly process and procurement activity in such a way that customers are serviced at a higher level, yet at a lower cost, in a computer literate environment operating within a global infrastructure.[39] Volume contracts can also serve as the potential backbone for multimodal carriage of goods facilitated by

[39] The preface to the resolution adopted by the General Assembly during the adoption of the Rotterdam Rules considers this by pointing out "... Believing that the adoption of uniform rules to govern international contracts of carriage wholly or partly by sea will promote legal certainty, improve the efficiency of international carriage of goods and facilitate new access opportunities for previously remote parties and markets, thus playing a fundamental role in promoting trade and economic development, both domestically and internationally, …"; see Resolution adopted by the General Assembly on the report of the Sixth Committee (A/63/438), United Nations Convention on Contracts for the International Carriage of Goods Wholly or Partly by Sea, UN Doc. A/RES/63/122.

containerisation which has become the norm for movement of non-bulk goods worldwide.

Containerised seaborne trade is served by shipping lines offering scheduled services and their operations are evolving as part of the global supply chain management. Thus, apart from providing traditional maritime services, carriers are entering into international logistics activities, impacting on the role of traditional logistics providers whose core activities have not been in the maritime segment of international transport.[40] This process allows shippers the advantage of comparing through-rates rather than rates of different unimodal legs of one shipment which is generally more complex. But comparisons of unimodal leg rates have become easier with increasing sophistication in computers. Furthermore, a recent counter-trend seems to have emerged where shipping lines do not want to be responsible for the through movement, but only for the part they can control, *i.e.*, the sea leg.

The above observations indicate that the tripartite phenomena of technological advancement, current business models and globalization of trade have created the need for contractual arrangements between carriers and shippers which is best served by the volume contract concept. It is envisaged that volume contracts being contracts of carriage will not only foster economic efficiency but will also provide the advantage of a legal framework within which those trading through volume contracts can operate under the carriage liability regime of the Rotterdam Rules. It is also of significance that volume contracts and the maritime-plus[41] approach being within the scope of application of the Rotterdam Rules, the global supply chain management phenomenon is well served.

## 4. Legal Analysis of Volume Contracts under the Rotterdam Rules

The service contract concept which recognizes the uniqueness of individual contracts entered into between different parties, influences and justifies bargaining freedom in carriage of goods by sea under the Rotterdam Rules in respect of the trade relationship between shipper and carrier, namely the volume contract.

Article 79 of the Rotterdam Rules lays down a minimum mandatory regime which is similar to the existing carriage regimes. Article 79 deals with carriers'[42] and cargo interests' obligations and liabilities. Maritime performing parties[43] are also

[40] See Peter Marlow, Rawindaran Naira, "Service contracts - An instrument of international logistics supply chain: Under United States and European Union regulatory frameworks", *Marine Policy* 32 (2008) at p. 493.

[41] See for example, Proposal by the Netherlands on the application door-to-door of the instrument, UN Doc A/CN.9/WG.III/WP.33, para. 1(c).

[42] Article 1(5) of the Rotterdam Rules defines "carrier" as a person that enters into a contract of carriage with a shipper.

[43] Article 1(7) of the Rotterdam Rules defines "maritime performing party" as "a performing party to the extent that it performs or undertakes to perform any of the carrier's obligations during the period between the arrival of the goods at the port of loading of a ship and their departure from the port of discharge of a ship. An inland carrier is a maritime performing party only if it performs or undertakes to perform its services exclusively within a port area."

included under this article. The cargo interests enumerated are shipper[44], consignee[45], controlling party[46], holder[47] and documentary shipper[48]. The cargo interests' obligations and liabilities can neither be decreased nor increased but the carriers' or maritime performing parties' obligations and liabilities can be increased.

The references in article 79 to "indirectly" exclude or limit obligations and liabilities and reflect the intention in the Rules to prohibit the carrier from avoiding the mandatory system by making arrangements in the carriage contract to that effect. It is through the wording "[u]nless otherwise provided in this Convention" in article 79 that derogation from the Rules is permitted.

Under article 80(1), volume contracts are subject to the Rotterdam Rules as a default rule where the parties have the freedom to contract out of most of that coverage if they so choose. Article 80(2) allows the possibility to deviate from the provisions of the Rules to the extent that those provisions otherwise would be mandatory. It covers carrier and shipper by reference to paragraph 1.[49] There are four preconditions in article 80(2) and all of them must be fulfilled for the provisions in the Rules not to apply mandatorily.

Article 80(2)(a) requires that the derogation must be set forth in the volume contract as a prominent statement. In subparagraph (b) there is the requirement that the volume contract is either individually negotiated or prominently specifies the sections of the volume contract containing the derogations. The first part of subparagraph (b) requires that any derogation must be negotiated on an individual basis and not just incorporated in accordance with a standard form. The alternative second part of subparagraph (b) requires a prominent specification of the sections of the volume contract containing the derogations. Subparagraph (c) allows the shipper to be notified that he has a real choice whether or not to enter into a volume contract and he must on the basis of that notification be able to make a choice. Subparagraph (c) essentially requires the carrier to give to the shipper an opportunity to contract on the terms of the Rules without any derogation, and to give notice of such opportunity. The first part of paragraph (d) does not allow incorporation of a derogation clause by reference to another document. It is notable in this context that whereas subparagraph (b) provides for individual negotiations as an alternative, by contrast, subparagraph (d) does not permit both incorporation of the derogation by reference as well as by insertion in a contract of adhesion. Subparagraph (d) was drafted in this particular

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[44] Article 1(8) of the Rotterdam Rules defines "shipper" as "a person that enters into a contract of carriage with a carrier."

[45] Article 1(11) of the Rotterdam Rules defines "consignee" as "a person entitled to delivery of the goods under a contract of carriage or a transport document or electronic transport record."

[46] Article 1(13) of the Rotterdam Rules defines "controlling party" as "the person that pursuant to article 51 is entitled to exercise the right of control."

[47] Article 1(10) of the Rotterdam Rules defines "holder" as: "(a) A person that is in possession of a negotiable transport document; and (i) if the document is an order document, is identified in it as the shipper or the consignee, or is the person to which the document is duly endorsed; or (ii) if the document is a blank endorsed order document or bearer document, is the bearer thereof; or (b) The person to which a negotiable electronic transport record has been issued or transferred in accordance with the procedures referred to in article 9, paragraph 1."

[48] Article 1(9) of the Rotterdam Rules defines "documentary shipper" as "a person, other than the shipper, that accepts to be named as "shipper" in the transport document or electronic transport record."

[49] The status of a third party is regulated in article 80(5). See *infra*, p. 17.

way to reach a compromise.[50] The use of the term 'contract of adhesion' was included to depict the notion that the use of standard terms or a boilerplate clause for derogation which are not freely bargained is not to be allowed under subparagraph (d)(ii). There must be a sufficient individual element involved for including a derogation clause in the volume contract. The whole of article 80(2) must be read in light of article 3 of the Rules according to which the relevant communication has to take place in writing or by electronic communication as specified in that article.

Article 80(3) provides that such documents as a carrier's public schedule of prices and services, transport document, electronic transport record or similar document may be incorporated in a volume contract, but for purposes of the permissibility to derogate from the mandatory provisions of the Rules, those documents per se do not qualify as volume contracts. Article 80(3) thus illustrates a further limitation on the freedom of contract to derogate from the Rules. Pursuant to article 80(4) certain provisions which are of fundamental importance within the Rotterdam Rules cannot be derogated from in a volume contract even if all the requirements in article 80 are fulfilled. These so-called "super mandatory" rules cover two references concerning the carrier and two references concerning the shipper. Perhaps the most important super mandatory provision is that the carrier has a non-delegable duty to provide and maintain a seaworthy ship according to article 14, subparagraphs (a) and (b). The other relates to a carrier's conduct that would lead to loss of limitation of liability in article 61. The shipper cannot derogate from the rights and liabilities arising under articles 29 and 32. This paragraph exemplifies yet another significant limiting device in relation to derogation.

Article 80(5) deals with derogation possibilities in relation to third parties other than the shipper. There are specific requirements in article 80(5) aimed at taking into consideration the specific status of third parties and to provide protection respectively. The chapeau of this paragraph shows that the requirements mentioned in view of the relationship between the shipper and the carrier must be satisfied. Added to this, there are specific rules in the two subparagraphs. Subparagraph (a) requires that prominent information has been received by the third party on the fact that the volume contract derogates from the Convention. When this information has been received it is also required that the third party has expressly consented to be bound by such derogations in accordance with article 3.

Article 80(5)(b) sets up restrictions on the express consent stating that it does not suffice to set forth such consent in a carrier's public schedule of prices and services, transport document or electronic transport record. The whole of paragraph 5 must be read in light of article 3 according to which the relevant communication must be in writing or by electronic communication. If there is a dispute on the validity of any derogation, the written document will be used for evidentiary purposes. Paragraph 6 provides that the party claiming the benefit of derogation bears the burden of proof that the conditions for derogation have been fulfilled. It seems that in most jurisdictions such burden of proof would apply in any case.

[50] See, "Report of Working Group III (Transport Law) on the work of its twenty-first session", UN Doc A/CN.9/645, paras. 243-245.

## 5. Rotterdam Rules and the Existing Carriage Regimes: Comparative Analysis

It is notable that by contrast the Hague/ Hague-Visby Rules have no provision allowing derogation from the mandatory regimes. Article 2, paragraph 4 of the Hamburg Rules has a reference to carriage of goods in a series of shipments, but that provision is not comparable with article 80 of the Rotterdam Rules.

The Hague/Hague-Visby Rules apply only when a bill of lading or a similar document of title is issued.[51] Thus, in the first instance, volume contracts are outside the scope of these instruments and are not subject to any mandatory convention law. When under a volume contract a bill of lading is issued for an individual shipment, in the relationship between the carrier and the shipper, the terms of the volume contract will prevail over those of the terms of the bill of lading. When such a bill of lading is held by a consignee or third party, the mandatory provisions of the Hague/Hague-Visby Rules prevail over the terms of the volume contract[52].

To reach a meaningful comparative analysis in relation to the three sets of Rules, two scenarios may be considered; one where a volume contract is worded as a contract for the hire of a ship, such as a consecutive voyage charter or a consecutive slot charter, and another where the volume contract is not so worded.

In terms of the first scenario, neither the Hamburg Rules nor the Rotterdam Rules can apply in the relationship between the carrier and the shipper, but will apply mandatorily to the relationship between the carrier and a third party, same as in the case of the Hague/Hague-Visby Rules.

In the second scenario, where the volume contract is not worded as the hire of a ship, the Hamburg Rules will apply mandatorily to each shipment made under such a contract, both in the relationship between the carrier and the shipper as well as between the carrier and a consignee or third party.

Under the Rotterdam Rules the position in the second scenario will lie somewhere in between the Hague/Hague-Visby Rules and the Hamburg Rules. The Rotterdam Rules will apply to such volume contracts and to each shipment made thereunder, but according to article 80 the carrier and the shipper may agree on certain derogations provided there is compliance with the strict conditions set out in that article. A consignee or third party must be advised on such derogations and will only be bound by them if there is express agreement to that effect.

In some quarters it is alleged that the liability regime in the Rotterdam Rules is such that its mandatory character can be easily diluted in the context of volume contracts. As a result, shippers will be hurled back to the chaotic pre-1924 era of freedom of contract.[53] It is submitted that this notion is a misconception because the

[51] See definition of contract of carriage in article 1(b) of the Hague/Hague-Visby Rules.
[52] But, as said previously, often there is no genuine third party involved.
[53] See for example, "View of the European Shippers' Council on the Convention on Contracts for the International Carrying of Goods Wholly or Partly by Sea also known as the 'Rotterdam Rules'", March 2009 (hereinafter view of the ESC on Rotterdam Rules) and the CLECAT Position Paper "The European Voice of Freight Logistics and Customs Representatives", 11 May 2009, both available online at http://www.uncitral.org/uncitral/en/uncitral_texts/transport_goods/2008rotterdam_rules.html.

Hague/Hague-Visby Rules do not deal with volume contracts at all, and therefore, there is complete freedom of contract in that respect. However, if under a volume contract a bill of lading is issued for an individual shipment, the relationship between the carrier and the third party can be governed by the Hague/Hague-Visby Rules; and any derogation from the Rules cannot prejudice a consignee, unless he voluntarily accepts it. The situation under the Rotterdam Rules will virtually be the same. The Rules require the consignee to be informed of the derogation which will only be binding if he provides express consent to be bound by it.[54]

## 6. Critique of the Volume Contract concept

Several criticisms of the volume contract regime in the Rotterdam Rules have emanated from views expressed by delegations during deliberations at UNCITRAL Working Group III as well as in print media and academic publications. There are many who support its inclusion in principle and there are others who do not. Some of the antagonists consider the definition of volume contract to be imprecise. They are of the opinion that it is detrimental to the interests of small shippers and opens up the possibility of abuse by their carriers. One argument advanced in favour of the inclusion of volume contracts in the Rules is that the existing mandatory regimes were developed in a commercial environment that is no longer pertinent, and that they are inadequate to meet present day commercial needs. Opponents of the volume contract regime prefer a more regulatory approach to trade issues. As indicated above, they view its inclusion in the Rules as fostering through freedom of contract a return to the situation prevailing in the pre-Hague era for small shippers.[55]

The inclusion of the volume contract provision in the Rotterdam Rules has reignited the long standing debate over contractual imbalance between carrier and shipper due to unequal bargaining power. Related to this is the allegation of whether transport contracts are contracts of adhesion, which the shipper is compelled to accept or quit the transaction. Fears were also expressed in the Working Group III sessions that approximately 90 per cent of the liner trade might be encompassed by volume contracts, leaving only 10 per cent to be fully regulated by the new convention.[56] Some industry groups and commentators have contended that in practice volume contracts will allow the shipper to be offered two freight rates by the carrier, one where the Rotterdam Rules apply mandatorily, and the other where there are derogations.[57] Opponents of the Rules also contend that the reduced freight rates generated by volume contracts will be offset by higher insurance rates. Furthermore, disadvantageous jurisdiction provisions will make legal action more expensive in cases of disputes with the carrier.

[54] See article 80 (5) of the Rotterdam Rules.
[55] See "Comments received from Governments and intergovernmental organizations – States – Australia – 14 April 2008", UNICTRAL 41st session, New York, 16 June - 3 July 2008, UN Doc A/CN.9/658, para. 9.
[56] See "Comments from the UNCTAD Secretariat on Freedom of Contract", UN Doc A/CN.9/WG.III/WP.46, paras 5 and 12. Also see "Report of Working Group III (Transport Law) on the work of its eleventh session", UN Doc. A/CN.9/526, para 209.
[57] See for example, view of the ESC on Rotterdam Rules, *supra* note 59. See also, Hannu Honka, "Scope of Application, Freedom of Contract", CMI Year Book 2009, p. 266.

At the Working Group sessions a number of delegations who were of a contrary view endorsed the need for a free-market approach.[58] Supporters of the Rotterdam Rules have taken the position that being a new convention it should be forward-looking and must be able to respond to the changing needs of industry. Together with providing a strong framework of generally applicable rules, the convention should have the flexibility needed by those engaged in trade and commerce.[59]

It is apparent from the illustrations provided in section 3 and the discussion in section 5 above, escaping mandatory provisions whether of the Hague/Hague-Visby Rules or the Rotterdam Rules, is not an onerous task. It can be achieved by simply using appropriate charterparty wording in the volume contract. This assertion is also valid for individual shipments made under such volume contract when the relationship in question is between a carrier and shipper or between a carrier and consignee in case they are the same or one is the agent of the other, which is fairly common practice. When the shipper and consignee belong to the same economic entity, there is no economic need to 'protect' the consignee either.

However, it is not necessarily the case that a carrier can compel an unwilling shipper to accept a volume contract derogation. In this regard, the protections contained in article 80 of the Rules operate equitably in favour of shippers. A carrier attempting to impose a volume contract on an unwilling small shipper may face challenges to the legitimacy of the derogations from a legal standpoint. In one instance there could be a finding by a court that the contract was a "contract of adhesion" under article 80(2)(d) of the Rules. Indeed, the very vagueness of the wording in a volume contract, as mentioned above, may backfire and add to the risk of the carrier, especially if a small shipper is involved. In another instance, there may be a finding by a court that the shipper was not given a real "opportunity" and "notice" of concluding a contract with full protection as required under article 80(2)(c). Furthermore, there may be a finding by a court that the derogation was not sufficiently "prominent" as required under article 80(2)(a) of the Rules and that the specific sections were not "sufficiently identified" as required by subparagraph (b) of that article. Because of these risks the probability is that the derogation provision will be used primarily by large shippers in complex commercial negotiations with carriers, where the scope and complexity of the negotiations and the sizes of the parties will suggest that they entered into a derogation willingly.[60]

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[58] See *supra* note 56, para. 245. In the interest of obtaining a consensus on volume contracts, the delegations of France, the United States of America, Denmark, Finland, Japan, the Netherlands, Norway, Spain and Sweden circulated a revised text of article 80 during the final reading of the draft convention at the 21st session of Working Group III in Vienna. It was circulated as a conference room paper contained in A/CN.9/WGIII/XXI/CRP.4. The definition of volume contract in article 1(2) was made acceptable to the Working Group as a part of the compromise package regarding the limitation on the carrier's liability. This compromise was based on a proposal submitted by 33 delegations and it was agreed among them that no aspect of the compromise package would be reopened at the 41st session of the UNCITRAL Commission; see A/CN.9/WG.III/XXI/CRP.5.

[59]The United States delegation persistently attempted to persuade the Working Group to adopt this view. See Mary Helen Carlson, "U.S. Participation in the International Unification of Private Law: The Making of The UNCITRAL Draft Carriage of Goods by Sea Convention", 31 Tul. Mar. L.J. 615, (2007) at p. 636.

[60] The authors acknowledge the contribution of Mr. Nicholas DiMichael to the information and opinions expressed in this paragraph.

The issue of pricing in volume contracts is one of several concerns which have emanated from certain quarters of the industry. It is alleged that carriers may seduce shippers to enter into volume contracts by offering a contract with minimal liability conditions against a lower rate than would have been valid for a normal shipment under normal liability conditions.

While it is true that in most cases of carriage under a volume contract a rate applies that is different from that for ordinary shipments, there are some good economic reasons including the following:

(i) The volume contract market, being a future market is different from the spot market. In a future market the expectations on future price increases or decreases are reflected in the actual prices.

(ii) In the spot market sometimes 'marginal pricing', *i.e.*, the price not covering the fixed costs, occurs. For large quantities in a future market, marginal pricing is unusual because pricing below costs can lead to insolvency of the carrier.

(iii) Large quantities may lead to economics of scale with a corresponding price decreasing effect.[61]

(iv) Special logistical requirements may lead to additional costs and, therefore, may have a price increasing effect.

(v) The carriage of large volumes may cause fierce competition, which may have a price decreasing effect.

All of the above mentioned factors lead to the result that the price per unit in a volume contract will be different from an ordinary shipment on the spot market. Whether the freight rate for shipments under a volume contract will be higher or lower than for shipments on the spot market will depend on the combined effect of factors (i) to (v) above.

A possible difference in liability conditions alone will not lead to a price difference simply because there is no significant monetary gain in terms of liability. For a container carrier the P&I premium if calculated on a per container basis is remarkably low in terms of the cost price of the carriage. The exact premium is dependent on the carrier's deductible, damage statistics and other factors.[62] In view of the fact that P&I premiums cover many other risks of the carrier which may be even greater than the cargo liability risk, the theoretical savings for a carrier if it does not assume liability under a volume contract will be minimal; so little so that it would not justify any rate reduction, in particular with respect to small volumes that a small shipper may have available for carriage.

Another relevant issue is whether volume contracts are a dominant factor in the market. In the non-United States trades, provided shippers are free under the law or commercial considerations to select their carriers, it is estimated that some 50 to 70

[61] Long-term, larger quantities may lead to economics of scale because larger ships may result in lower costs per TEU. Short-term, larger quantities will increase the level of occupancy of a vessel. Each vessel, however, has in a certain trade an optimal occupancy level in the order of 85 – 90 per cent of its theoretical total capacity. When the occupancy increases beyond such optimum, the costs connected with shifting containers in ports during loading/unloading operations may become higher than the gross profit margin of the containers that are carried beyond the optimal number.

[62] It may be as low as 0.1 per cent of the cost price of carriage. *Supra*, note 34.

per cent of the total number of shipments[63] are carried under the rate agreement system[64]. Even where volumes are large, relatively speaking not many such consignments are carried under volume contracts. Only when there is a scarcity of shipping space there is a tendency for an increase in the numbers of volume contracts. This is because under such circumstances, certainty of space may become more important for shippers than it would have been otherwise. However, under normal circumstances if the average occupancy level of liner ships is around 75 per cent, it is estimated that no more than 20 to 25 per cent of the total number of shipments would be carried under volume contracts.[65]

In the United States trade these figures are completely different. As explained in section 2 above, for regulatory reasons, almost all shippers in this trade opt for a service contract. Under the Rotterdam Rules, such service contracts qualify as volume contracts. Therefore, in the United States trade the percentage of volume contracts amount to 95 to 100 per cent of the total trade.[66]

In the context of the above, the following observations are pertinent. Under articles 1(1), 1(2) and 5 of the Rotterdam Rules, an individual contract between shipper and carrier for the carriage of goods (so long as it is not a contract for the use of a ship) falls within the scope of the Rules; and if it is a volume contract, the Rules will apply mandatorily unless the parties contract out by taking positive steps to that effect.[67] Thus, it is submitted, they can create their own liability regime; but if they do not do so, the liability provisions of the Rules will apply by default. It is quite possible that many volume contracts will only address the transportation aspects, (*i.e.*, shipper will commit itself to a specified quantity of cargo if carrier agrees to a certain rate), without ever dealing with liability, which will be covered by the Rules. Small shippers are the ones most likely to have these kinds of arrangements which will be covered by the Rules. Any contention that only 10 percent of cargo movements will be covered by the Rotterdam Rules and 90 percent of shipments will be under volume contracts outside the scope of the Rules may well be a fallacy simply because the vast majority of those volume contracts may not deal with liability at all and therefore will fall under the Rules.[68]

Undoubtedly, the United States delegation with its experience in the realm of service contracts was the driving force at the negotiations in the Working Group sessions in promoting the inclusion of volume contracts in the Rotterdam Rules. It is apparent that the thinking of the United States delegation centered not only on the commercial and trade dimension of volume contracts but also on whether in the final analysis, benefits would accrue to the society at large, in particular, consumers. Such an approach to law-making is consistent with the legal maxim *salus populi suprema*

[63] *Supra*, note 34.
[64] As explained earlier in section 3 above, "rate agreements" here refers to cargo carried either under the agreed rates or under lower spot rates.
[65] *Supra*, note 34.
[66] *Ibid.*
[67] During the UNCITRAL Working Group III deliberations some delegations favoured complete exclusion of volume contracts from the reach of the Rules. Incidentally, the United States delegation was opposed to this view. See *supra*, note 56, paras. 235 - 242.
[68] *Supra*, note 66.

*lex.*[69] This line of thinking also reflects a holistic approach to the balancing of interests between shipper and carrier in terms of both trade and liability aspects.

Thus, the freedom of contract allowed to the parties, being subject to various preconditions, should not be deemed to be in conflict with or threaten the social good regardless of whether or not any of the proponents of volume contracts had consciously considered this social welfare approach in supporting the concept. In this respect there is merit in the regime of volume contracts as articulated in the Rules.

In a macroeconomic sense changes in transport costs occurring through volume contracts are indeed beneficial to the consumer and society at large. However, it is arguable that the benefit is not universal. The position of large shippers who are also large traders will be enhanced, but small shippers who are also small traders will remain in the same position because they will be unable to bargain for the best possible terms of transportation due to size, scale or location. The latter will thus be left at a competitive disadvantage.

## 7. Summary and Conclusion

The changing dynamics of trade have made the application of the volume contract concept inevitable and inescapable. The development of the Rotterdam Rules has been a major undertaking in law reform in the international regime of carriage of goods. The perceived optimal or efficient balancing of risks between carrier and shipper interests was often the result of compromise reached after protracted debates at the negotiations. Such compromises have raised questions on whether a proper balance of risk between shipper and carrier interests has been struck, or whether the balance has unreasonably shifted in favour of one side, or whether the exercise is simply a fine tuning of the existing law. Its adoption by the maritime community is evidence that the opportunity to articulate a carriage regime focusing essentially on a balanced allocation of obligation and liability between carriers and shippers has not been missed.

In addition, the Rules govern the legal relationship between carriers and shippers in terms of facilitating the free flow of trade in a manner as economically efficient as possible. As has been discussed, within the service contract regime from which the volume contract concept is derived there are some winners and some losers. There is an air of functional tension between equity and efficiency fostering healthy debate. But on the whole the volume contract regime even with its permissible deviations from the mainstream of the Rules is a good one.

The allegation that through the volume contract regime the Rotterdam Rules have hurled us back to the chaotic domain of freedom of contract that prevailed in the pre-Hague Rules era is patently misconceived. Indeed such would have been the case only if unbridled freedom of contract was allowed to prevail in all situations contemplated by the Rules beyond those involving volume contracts. The freedom to derogate from the Rules in instances of volume contracts is premised on the trade aspect of the contractual relationship between carrier and shipper. No derogation is

[69] This expression simply means that the welfare of the people is the supreme law.

allowed from those of the liabilities and obligations of the Rules that are of the essence of all carriage conventions; and the Rotterdam Rules are no exception.

In the context of this discussion it is important to recognize the fact that the service contract regime is simply one that provides for open market negotiation of economic trade advantages between carrier and shipper which in effect stimulates competition. It is recognized in this vein that the liner conference system on the face of it is discriminatory in nature; it runs afoul of the basic tenets of anti-trust or anti-combines laws. Even so, governments recognize that while competition is a good thing, cutthroat competition spells inefficiency. They have thus in their wisdom caused legislation to be enacted which endorses the conference system and provides it immunity from the anti-trust or anti-combines laws in their jurisdictions.

In the normal course, within a service contract regime which lies outside the scope of any convention liability regime, the parties have the freedom to align their trade transactions according to any carriage liability regime that may be suitable and available. However, there is no carriage liability regime established through international convention or national legislation that takes account of the economic efficiency factor in the trade relationships between carriers and shippers. Thus, those who are trading through service contracts lose some of the economic efficiency benefits when they submit themselves to any existing carriage of goods regime. The Rotterdam Rules provides an opportunity to create a legal framework within which those trading through volume contracts can operate within a carriage liability regime that is adequately flexible so that certain derogations can be made which will inure to the benefit of the parties in terms of economic efficiency and at the end of the day benefit international trade and the trading community as a whole.

It is hoped that this realization will influence and guide those who are responsible on behalf of their governments to subscribe to the Rotterdam Rules, and also those in the private sector in every jurisdiction whose support is necessary for governments to make a reasoned policy decision. The Convention is imperfect but that is a trait it shares with virtually all international instruments aimed at harmonization. This Convention even with its imperfections is an all-embracing, comprehensive and well-balanced regime for international carriage of goods. Its strength lies in its singularity designed to replace three conventions[70] for one with the addition of another convention[71] that never was. Only time will tell whether this herculean law reform exercise was worth the effort expended. Meanwhile no stone should be left unturned to examine the instrument with a fine toothcomb and critically analyze it for the benefit of policy makers, lawyers, judges, practitioners and scholars alike whose interests and responsibilities lie in this intricate and challenging field of maritime law.

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[70] The Hague Rules, the Hague-Visby Rules and the Hamburg Rules.

[71] United Nations Convention on International Multimodal Transport of Goods, May 24, 1980, U.N. Doc. TD/MT/CONF/16 (1980)