



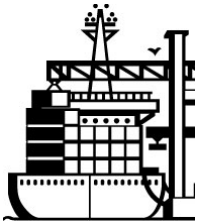
SURF & TURF

Legal News in Transportation & Logistics

A bimonthly newsletter published by the BPM Transportation & Logistics Practice Group

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No Class Act: A Bad Survey Lands a Classification Society in Hot Water

BY STEVEN W. BLOCK

Classification societies are independently operated, vessel survey organizations that publish sets of rules and standards for various classes of watercraft. When hired, they dispatch specialized surveyors to look over ships in the context of their designs and proposed operations, then issue certificates proclaiming boats fit for duty or in need of specified attention.

Having operated (in one form or another) for centuries, classification societies serve the ocean shipping industry's various sectors. Banks and vessel finance concerns, insurers and P&I clubs, vessel buyers, charterers, and others usually rely on a classification society's seal of approval in conducting their maritime transactions. In fact, the blessings of a recognized society (there are only a handful of well-regarded ones) often are requisite to salty contracts.

A number of federal court decisions have addressed classification society liability. What happens when a society's glossy certificate, beaming a ship's

unambiguous endorsement for operations, is based on an erroneous survey? Does the society have to pay for repair of deficiencies it should have discovered and warned about? The answer isn't entirely clear, and may depend on what part of the country you live in. The U.S. Court of Appeals for the Fifth Circuit (comprised of the south central states) recently took a look at what it deems the "novel but not entirely uncharted territory" of classification society liability.

Otto Candies bought Diamond Ferry Co.'s high speed passenger vessel *Speeder*. The two companies shook hands over a memorandum of agreement providing that the sales terms were contingent on classification society Nippon Kaiji Kyokai Corp (NKK) issuing a clean bill of health to *Speeder's* hull and engines. NKK, copy of the Otto Candies-Diamond Ferries memo in hand, sent its surveyors to the Japan-flagged vessel. The society issued its Class Maintenance Certificate, saluting *Speeder* as well-suited for coastal passenger ferry service. NKK even had a few chats with Otto Candies along the way.

When the vessel was looked over stateside, a panoply of vessel deficiencies were readily apparent to the surveyors of another classification society, the American Bureau of Shipping (engaged to facilitate hoisting of the Stars and Stripes over *Speeder*). There was some pretty serious stuff wrong with the ferry, dealing with its hull integrity and sensitive

equipment, that shouldn't have escaped NKK's detection. Otto Candies forked over some 328 grand in repair costs to make the vessel seaworthy. It promptly looked to NKK for reimbursement, alleging negligent misrepresentation of *Speeder's* seaworthiness. The lawsuit wound its way to the Fifth Circuit.

Some courts, most notably those in the Second Circuit (which encompasses the northeast states, including New York), don't recognize such liability theories against classification societies. A precept of maritime law is that ship owners bear a nondelegable duty to run only seaworthy vessels, and the ability to deflect liability onto a survey organization's shoulders might encourage lackadaisical attitudes about the issue. Classification societies might be reluctant to inspect and bless older or inherently risky vessels if significant liability might attach to a slip-up. Lastly, a survey shouldn't be taken as a "guarantee" that a vessel's innards are hunky-dory; they're just an inspector's best opinion after a once over.

Moreover, the elements of negligent misrepresentation usually aren't satisfied in classification society cases. That's because only a "limited group of persons" can avail themselves of the legal principle, i.e., those "for whose benefit and guidance the defendant either intends to supply the information or knows that the recipient intends to supply it." Societies typically don't know all details of why an inspection has been ordered, so they rarely have "misrepresented" anything to the aggrieved party.

In this case, however, NKK knew exactly what was afoot, having communicated with Otto Candies and been copied on the sales memo. The court also seemed particularly moved by how obvious and egregious *Speeder's* mechanical and structural shortcomings were. Concluding Otto Candies wouldn't have gone through with the deal absent an NKK certificate, the court ordered the society to pay all costs incurred for repair of the undisclosed vessel deficiencies.

Revisiting the "novel" nature of this legal territory, the Fifth Circuit hastened to emphasize that classification society liability "should be strictly and carefully limited" for much the same reasons as the Second Circuit and other courts have cold-shouldered the concept altogether.

Oh, shippers and forwarders? Don't get your hopes too high about pegging a classification society for your lost/damaged cargo. The court spoke about one

instance when a shipper tried that route (unsuccessfully), and recognized the unlikelihood a cargo owner could show sufficient reliance on a classification society's certificate to substantiate negligent misrepresentation. Just asking for a copy isn't enough; the society pretty much has to have advance notice it's doing a job for someone in addition to the ship owner that hired it. Charterers might have better luck, as the court pointed out, when the survey organization issues specialized documentation for the charter.

But classification societies should recognize that documentation they're provided in support of a requested survey might bring potential plaintiffs into the loop. A vessel's owner stands first in the liability line when it comes to vessel seaworthiness. However, other affected players might seek recourse against anyone with deep enough pockets.

Ref: *Otto Candies v. Nippon Kaiji Kyokai Corp.*, 2003 WL 22137861 (5th Cir. 2003).

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Maritime Negligence: Who Gets to Pay When Something Goes Wrong, and How Legal Liability Can Be Dodged

BY STEVEN W. BLOCK

Two recent federal court decisions addressing maritime law's approach to negligence provide some good pointers for those harmed by, or accused of causing, mishaps at sea. For purposes of admiralty jurisdiction (i.e., maritime law applicability), vessels "at sea" include those floating at marinas, piers, wharves and other mooring stations.

Admiralty doesn't treat negligence actions much differently than does other law, although there are a few twists, turns and name changes in the process. At the heart of the concept are four "elements," or things a plaintiff must prove to win: Duty, Breach, Causation and Damages. "Duty" is an obligation not to do something harmful that you owe customers, contractors, partners, innocent bystanders and many others. The concept of "duty" is broadly construed; pretty much anyone you come in contact with has a

right to assume you won't be negligent. However, it still must be demonstrated.

Next on the laundry list is "breach," or the violation of the duty described above. You have a duty not to crash into someone else's vessel, lose your shipper's cargo, or provide incorrect shipper's instructions to your customer's carrier; you breach that duty when you collide, drop a container overboard, or tell a carrier to maintain a chemical cargo at 20° Celsius instead of Fahrenheit (yes, it's happened).

But just because a duty's been breached, a no-no has occurred, and something needs to be done better next time, doesn't necessarily mean liability. To satisfy the element of causation, a plaintiff has to show that the breach of a duty actually caused harm. It makes no difference if an equipment supplier negligently sold a vessel operator faulty positioning equipment, if the vessel wouldn't have avoided that storm even with appropriate gear because a crewmember was too snookered to use it (yes, that's happened too). Generally, causation requires that the variety of harm caused was foreseeable to the wrongdoer.

Lastly, a plaintiff alleging negligence has to show the extent of damages caused by a breached duty. Some leeway is given when an exact figure is unascertainable, but you're supposed to point to the size of your loss with specificity.

The federal court sitting in Delaware recently reaffirmed these principles in the context of an electrical fire on one yacht, which spread to another boat moored next to it. Both vessels found their way to Davie Jones' Locker, and a lawsuit followed. Duty? Sure. You have a duty not to endanger another vessel by having a fire-hazard condition on your own boat. Damages? Of course. A yacht's acquaintance with the seabed is a loss in anybody's book.

But in this case, the plaintiff couldn't show breach. A licensed marine electrician had just blessed the defendant vessel's wiring, which allegedly started the fire. That's all a pleasure craft owner needs to do (a different standard might apply to commercial vessels). There's no automatic liability just because a fire breaks out on your yacht; if you did what the Coast Guard requires, and what a phantom character the law knows as "the reasonably prudent man" would have done, you're probably okay.

That was enough to end the matter, but the court, just to make its point clear, also addressed the absence of causation. The plaintiff couldn't show sufficient

evidence that the defendant vessel's bad wiring actually sparked the fire. Expert witnesses differed. Even if a hazardous condition existed, it didn't necessarily cause the problem.

In this era of contractual freedom, shouldn't players be free to strike a deal regarding who shoulders risk during the course of a business relationship? Certainly those writing standardized contracts have long thought so. Most everyone has encountered a contractual "exculpatory clause," or a term that basically says, "even if I cause you harm by my own negligence, I won't be liable for it."

The law has long looked at exculpatory agreements with a jaundiced eye, and for many years wouldn't enforce them at all as contrary to public policy. We just don't want folks feeling free not to worry about keeping things safe. But recognizing economic realities and business trends, courts, including those sitting in admiralty, reluctantly enforce exculpatory clauses. However, they must be clear and precise under the circumstances. In other words, there has to be no doubt that the party giving up its right to sue for negligence knew just what it was doing. The contract language has to be almost nauseating precise.

When scrutinizing exculpatory agreements, judges are far more loath to throw out of court an individual plaintiff naïve to the business world than a sophisticated company experienced in negotiating deals. The former need the benefit of public policy protection; the latter are presumed capable of taking care of themselves (and to have gained some benefit by agreeing to the term in the first place). Still, there must be some basis for a court to ignore an exculpatory clause, and inadequate specificity is the most common.

That's pretty much what recently happened in the Empire State, as addressed by the federal court for the Eastern District of New York. There, an exculpatory clause provided that a marina wouldn't be liable for any loss "irrespective of how the same is caused." That wasn't good enough, as it was unclear that negligence was encompassed by the term "irrespective." The marina gets to pay for fire damage. Note also that courts won't enforce an agreement that purports to exculpate really bad ("gross" in legal-ese) negligence or intentional acts.

The moral of the stories: live defensively and safely, and don't rely on exculpatory clauses. Recovery of damages by way of a maritime negligence claim often hinges on proving elements beyond your control.

Ref: *Commercial Union Insurance Co. v. Blue Water Yacht Club Assoc.*, 239 F.Supp. 316 (EDNY 2003); and *Galentine v. Estate of Stekervetz*, 2003 WL 21729781 (D. Del. 2003).

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Hot Recent Cases in Motor Carrier Law

BY STEPHEN L. DAY
AND STEVEN W. BLOCK

Federal law governs interstate trucking injuries, even in the unloading phase

Smart v. American Welding & Tank Co., 826 A.2d 570 (NH 2003)

A truck had transported a cargo of propane tanks from Georgia to New Hampshire. An employee of the consignee, located in the Granite State, helped offload the cargo. Apparently, a tank hadn't been secured properly. It unexpectedly rolled forwards, knocking Mr. Smart from the flatbed. Tragically, he died from his injuries. His estate sued both shipper and carrier.

The shipper asserted that federal law relieved it from any liability for improper loading once the carrier accepted the load. A state trial court ruled that New Hampshire law governed the rights of Mr. Smart's claims because the accident happened after the truck's arrival, and determined that New Hampshire hadn't adopted the federal rule. Instead, the trial court ruled that carriers are not liable for shippers' mistakes, even if they accept the cargo, and shippers stay on the hook.

The case wound its way to New Hampshire's Supreme Court, where the ruling was reversed. Analyzing the federal concept that carriers are responsible only for visible packing defects (the "Savage rule," after a precedent so ruling), the court found no reason to end the federal rule's applicability until after cargo had been safely offloaded. Questions of fact remain as to whether the packing problem was discernible, so the matter goes back

down the hill to determine whether the shipper and/or the carrier are liable.

A driver must jump administrative hoops before bringing an ADA claim in court

Harris v. P.A.M. Transport, 339 F.3d (8th Cir. 2003)

Prospective driver Harris began a driving course with training outfit MTC for carrier P.A.M. He had gotten a new set of kidneys, and had to take medicine to keep them working. That medication caused problems a P.A.M. examiner concluded were disqualifiers for a commercial truck driver (per DOT regs). An MTC doc disagreed. Nonetheless, P.A.M. refused to hire Harris on that basis. Even though not getting a driving job, Harris still got MTC's bills for his training, no doubt further encouraging Harris to seek redress.

Harris sued in an Arkansas federal court under the Americans with Disabilities Act, and the matter went to the Eighth Circuit. The Court of Appeals, agreeing with the district court, threw Mr. Harris out of the federal court system. He'd not been through administrative proceedings at DOT, which is far more able to scrutinize its own medical standards than would be a court. The fact that MTC and P.A.M.'s doctors disagreed was irrelevant because the DOT provides an appeals process to resolve just these controversies – which Harris did not follow. Harris also could not prove an essential ADA element, i.e., that he was qualified to work as a driver, because P.A.M.'s refusal to hire him was based on established DOT standards and was not of the carrier's "own devising."

You snooze, you lose: A pumped up shipper is bounced out of court

Kvaerner E&C Metals v. Yellow Freight Systems, pending in the U.S. District Court for the Northern District of California, Cause No. C02-1202 BZ

Shipper Kvaerner hired Yellow to move a cargo of pumps, which arrived damaged. A few weeks later Kvaerner sent Yellow a "notice of freight claim" which didn't include the repair costs. A few more weeks later, Kvaerner got a repair invoice for some 65 grand, and prepared a spreadsheet explaining them. Yellow asked for the damages to be presented on a Yellow claim form. Kvaerner's project manager found the forms tricky and confusing, but claims he filled them out and Fed Ex'ed them to Yellow. The project manager quit Kvaerner, didn't keep a copy of what

he'd sent Yellow (right, buddy), and Yellow denied ever receiving the claims forms.

Nine months passed, the matter went to federal court in California, and Yellow argued that timely notice of claim hadn't been provided (within the nine months allowed by Carmack and Yellow's shipping documentation). Kvaerner pointed to liberal 9th Circuit law regarding "substantial compliance" with notice requirements. Even if the Fed Ex wasn't sent or received, urged the shipper, Yellow had enough information to process the claim.

Surprisingly, the court disagreed and dismissed the action. Without the numbers, Yellow could not have settled the freight claim. Thus, this court (at least) believes some specification of the claim's size is essential even in the West. Delay occasioned by Yellow's tricky forms was no excuse (c'mon, Kvaerner, this was a big claim).

Blanked: A shipper's failure to declare value results in limited carrier liability

J.C. Research v. Global Overland Delivery, pending in the Court of Appeal of the State of California, Sixth Appellate District, H024119

Shipper JCR produced software and sold it around the country. It usually shipped its freight by air booked by air freight forwarder Global. Per practice, Global sent JCR bills of lading containing blank spaces for the shipper to declare value. Otherwise, said the document, liability would be limited to peanuts.

In this case, JCR's product assembler CMT tendered a load to motor carrier Covenant Transport (why this one went by road isn't clear), booked by Global. The cargo was stolen, and JCR was out 176 grand. Everyone went to Golden State court.

Global and Covenant moved to enforce limitation of liability. JCR's first response was that CMT wasn't authorized to enter into contractual arrangements with Global, Covenant or anyone else on behalf of JCR. That didn't work because JCR's complaint itself alleged CMT was JCR's agent.

JCR also urged that Global's representative had told JCR that it was insured. Nope, said the court. Even if that were enforceable, nothing suggests the cargo was fully "insured."

JCR argued that it didn't have a reasonable opportunity to choose full liability over limited liability. After taking a refreshing look at modern-day Carmack, the court found that the bill's blank space asking for declared value, made known to JCR through repetitious shipments, was all that was needed. Shippers only need be offered a choice, and the ability to declare value was enough of a choice under Carmack. Liability was limited.

A carrier is likely to prevail in business dispute

Hoover Transportation Services v. Frye, 2003 WL 22128759 (6th Cir. 2003)

This one doesn't much deal with transportation law, but it presents an interesting analysis of business relationships in the trucking context. Carrier Hoover struck a deal with one Mr. Frye whereby he would serve as an independent agent for Hoover in Charlotte, North Carolina. Somehow, things fell apart, and Frye allegedly started booking loads for another carrier. Hoover sued, alleging breach of contract, breach of a non-comp clause, misappropriation of trade secrets, unfair competition, and a host of other theories. It then got a preliminary injunction pending trial, preventing Frye from doing business with the other carrier.

To get a preliminary injunction, a plaintiff has to show it likely will prevail on the merits. That determination is within the trial judge's discretion – a pretty tough standard to beat on appeal. Frye tried anyway, taking the matter from the Southern District of Ohio to the Sixth Circuit.

The Sixth Circuit found that, true, Frye probably wouldn't be liable under the non-comp clause (it just wasn't worded well). Courts have ruled that contract rates, driver information, and shipper information within the trucking industry are trade secrets. Frye was spilling the beans, pretty much by his own admission. But nothing in the record suggested Hoover took steps to keep this info under wraps.

That's where Frye's luck ran out. Frye apparently had been telling the Tar Heel State's shipping world some fibs about Hoover and its business practices. On that basis, the court ruled that the trial judge was within his discretion in deciding Hoover probably would prevail. The preliminary injunction was upheld.

Logo Liability takes another shot

Mercer Transportation Co. v. Greentree Transportation Co., 341 F.3d 1192 (10th Cir. 2003)

A shipper booked cargo through broker Mercer with carrier McClellan, which was operating with carrier Greentree's logo nailed to its doors. A one-vehicle accident damaged the cargo. Mercer paid the shipper one hundred fifty thousand (presumably for business reasons), and went after Greentree for indemnity.

The theory: logo liability, based on *Rodriguez v. Ager*, 705 F.2d 1229 (10th Cir. 1983)(yep, it's been that

long). After reviewing *Rodriguez*' history, the court rejected logo liability. The principle applies only to personal injuries. Carriers are not logo liable for cargo damage.

Instead, you pretty much have to stick with Carmack, which relieved shippers of having to discover and chase down a carrier who actually had the freight when it was damaged. There was no privity between Mercer and Greentree, so the latter isn't liable.

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UPCOMING EVENTS

Attorneys in the Betts Patterson Mines' Transportation & Logistics Practice Group are regular speakers at events throughout the country. Upcoming events include:

Steve Block to Present Continuing Education Class

Steve Block will present a continuing education class to the Marine Insurance Association of Seattle entitled "Current Maritime Security Requirements and Programs" in Seattle, on November 18th, 2003.

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