Shipowners may not rely solely upon a Certificate of Class for their vessel as evidence of seaworthiness in defence of claims and it is not independent verification that an owner has properly maintained his vessel.

It has been recognised that shipowners may not rely solely upon a Certificate of Class for their vessel as evidence of seaworthiness in defence of claims. A Certificate of Class does not represent independent verification that an owner has properly maintained his vessel, nor that he has exercised due diligence to make the vessel seaworthy. As stated by the International Association of Classification Societies (IACS): “...such a certificate does not imply, and should not be construed as, a warranty of safety, fitness for purpose or seaworthiness of the ship. It is an attestation only that the vessel is in compliance with the Rules that have been developed and published by the Society issuing the classification certificate.”

Rarely has a classification society been held responsible to compensate a third party for the omissions of the shipowner.
One US court\(^1\) summarised the rationale for preserving classification societies from undue liability as follows:

> "Imposition of undue liability on classification societies could be harmful in several ways. The societies could be deterred by the prospect of liability from performing work on old or damaged vessels that most need their advice. The spreading of liability could diminish owners' sense of responsibility for vessel safety even as it complicates liability determinations. Ultimately, broader imposition of liability upon classification societies would increase their risk management costs and rebound in higher fees charged to the societies' clients throughout the maritime industry. Whether such risk-spreading is cost-efficient in an industry with well-developed legal duties and insurance requirements is doubtful."

Arguments have been advanced that damage to cargo or pollution damage was proximately caused by the inferior condition of the ship that had been 'approved' by class. Third party claimants have occasionally pursued legal action against classification societies, when a recourse action has limited prospects for financial recovery against an owner.\(^2\)

In the case of the PRESTIGE, US litigation initiated by the Kingdom of Spain against American Bureau of Shipping (ABS) failed primarily on these historical principles.

In several major and high profile casualties, such as the AMOCO CADIZ, ERIKA, PRESTIGE and more recently MOL COMFORT, questions have been raised about the independent role played by classification societies in vetting the design, construction and maintenance of vessels. However, with the exception of the ERIKA, courts have been reluctant to hold that classification societies owe obligations to third parties simply by their granting class status to a vessel.

**Sale & Purchase – a recommendation of class**

A notable exception to the 'virtual immunity from liability' of classification societies is their role and responsibility in ship sale and purchase transactions. A good illustration is a recent arbitration award from the New York Society of Maritime Arbitrators, Inc. (SMA) where ABS was held liable to Picture Maritime Corp. (PMC), the purchaser of a second hand vessel, the "PANOSTAR".

Classification societies are aware that the buyer of a ship will rely on the statements made by the society concerning the condition of the ship, i.e. the asset involved in the sale and purchase transaction. It follows that the classification society concerned owes certain legal responsibilities to the buyer (as well as the seller). A Class Certificate is a statement that the vessel has been surveyed in compliance with the society's own rules and regulations. The Norwegian Sale Form (NSF) is the most widely used form of contract for selling/buying a ship and it contemplates a two-stage process. The negotiated terms are recorded in the

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\(^1\) Otto Candies LLC v. Nippon Kajii Kyokai Corporation, 346 F 3d 530 (5th Cir 2003), where a classification society was found liable to a vessel purchaser where, having actual knowledge that the purchaser was relying upon its surveys, negligently failed to discover defects that led to damages to the purchaser; Sundance Cruises v American Bureau of Shipping, 7 F.3d 1077, 1084; Cargill Inc. v Bureau Veritas, 902 F.Supp 49, 52 (S.D.N.Y.1995); Great American Ins. Co. v Bureau Veritas, 338 F.Supp 999, 1012 (S.D.N.Y.1972)).

Memorandum of Agreement (MoA) which regulates payment of the deposit, when and where delivery of the vessel to the Buyer will occur. It usually sets out the documentation required to be produced upon closing, where a bill of sale is executed and the balance of the purchase price transferred. This interim period of time permits a buyer to inspect confidential class records. The MoA contains a statement by the seller that the vessel shall delivered to the buyer in a similar condition as when inspected and with her present class maintained, free from outstanding recommendations. Invariably, the MoA will also contain a term that the seller will provide a Class Certificate confirming this fact upon, or 48 hours prior to, delivery. Clause 11 regulates the condition on delivery of vessels on NSF terms.

The Memorandum of Agreement permits a buyer to inspect confidential class records and contains a statement by the seller that the vessel shall delivered to the buyer at a date in the future in a similar condition as when inspected and with her present class maintained, free from outstanding recommendations. Invariably the MoA will also contain a term that the seller will provide a Class Maintenance Certificate confirming this fact upon, or 48 hours prior to, delivery. Clause 11 regulates the condition on delivery of vessels on NSF terms.3

The facts recited in the PANOSTAR award are straightforward. The vessel underwent an annual hull survey in January 2010 which resulted in a local ABS surveyor recording a series of outstanding recommendations, which apparently were acceptable at the time to the sellers’ operations department. In March 2010, an MoA was signed under which the sellers agreed to deliver the vessel free of outstanding recommendations except for those contained in an earlier ABS report of October 2009. The January 2010 recommendations were apparently overlooked by the sellers, and not referred to in the MoA.

The terms of the MoA permitted the buyers to inspect class records. By doing so they became aware of the existence of the January 2010 recommendations. PMC requested the Sellers to advise how they intended to rectify the recommendations. The consequence was that the sellers either had to carry out the repairs recommended by ABS in January 2010, or renegotiate the price with buyers, or face the vessel being rejected on delivery. The sellers argued towards ABS that their January 2010 recommendations were not justified based on ABS’ own rules, regulations and practices. The award cites the following extract from correspondence submitted to ABS at the time:

“My and the Owners [Sellers] request is, that if you agree,... you can persuade the attending Surveyor to revise the report in such a way that there will be no outstanding recommendations against the vessel…”

The buyers next heard that the January 2010 ABS findings no longer appeared as recommendations but were shown in class records as Additional Requirements. PMC enquired of the sellers why the January 2010 recommendations had been deleted and the sellers responded they “… wished to clarify this is a Class matter, so we cannot respond on behalf of Class.” The Award does not record what exchanges may have ensued between PMC and ABS. In the event, ABS issued a Confirmation of Class certificate stating there were no outstanding recommendations (apart from the contractually permissible October 2009 recommendations).

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3 NSF 2012 made only minor amends to Clause 11. The amends provide that the Vessel is also to be delivered free of cargo and free of stowaways. The terms ‘Class’ and ‘the Classification Society’ have been used to distinguish between the notation and the society.
PMC were accordingly obliged to accept the vessel upon delivery as being compliant with sellers’ duties under the MoA.

Subsequently, in November 2010, ABS re-inspected the vessel whilst in its new ownership of PMC. The tribunal held that, following that re-inspection, ABS in effect reinstated the January 2010 recommendations without the vessel having suffered any material deterioration in its condition since it had been taken over by PMC and that this resulted in PMC being obliged to carry out remedial repairs relating to defects which existed before they bought the vessel and which would, but for ABS’s decision to re-classify them as Additional Requirements, have appeared in Class records at the time of the sale as Recommendations.

PMC sought in arbitration to recover their repair costs from ABS and the tribunal found in their favour. The tribunal held that ABS had adjusted and subsequently reinstated recommendations without just cause and that, as a result, PMC had incurred repair costs which would have been avoided had ABS acted correctly.

The Award

The Award follows existing US law principles that classification societies can face liabilities towards third parties in sale and purchase transactions. A buyer can rely upon Confirmation of Class certificates that there are no outstanding recommendations based upon a proper implementation of the class societies’ own regulations.

The Award also includes a forceful dissenting opinion from one of the three arbitrators on how such damages should be calculated. The majority concluded damages were restricted to the cost of carrying out the repairs which were directly attributable to the adjusted January 2010 recommendation, whereas PMC argued it should recover its loss based on the cost of actual repairs performed because additional works were unnecessary. These additional and related repairs were disallowed. The dissenting view was that ABS had failed to discharge the burden of demonstrating the actual repairs were unnecessary and therefore all costs incurred by PMC should be recoverable.

No argument was apparently advanced in arbitration to the effect that PMC were deprived of their opportunity of rejecting the vessel or achieving a negotiated discount. In a falling market, the right to reject delivery of a vessel at the contract price can be far more significant than the simple costs of repairs.

The Award is interesting given the current fragile state of the ship sale and purchase market, with reports that mortgagee banks may place more tonnage on the market in order to reduce loan book exposure to shipping debt, with sales occurring on NSF terms. Such debt is also being sold to various financial investors including hedge fund operators, whose prime (and natural) interest is to capitalize on the investment through best possible re-sale price. The current market conditions may not, therefore, ease the pressure placed on classification societies.