

CONDITIONS FOR ISSUING A “CLEAN ON BOARD” BILL OF LADING; ISSUANCE OF A ‘CLEAN ON BOARD’ BILL OF LADING AGAINST RECEIPT OF A “LETTER OF INDEMNITY” FROM THE CONSIGNOR ¹

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Abstract: *A bill of lading plays a crucial role as evidence in international trade and transport. After the goods are loaded and the bill of lading is signed, it serves various functions and involves multiple parties in the commercial and transport contract, including the shipper and the consignee of the goods. The master of the ship is the person who receives the goods on behalf of the consignee and is responsible for their delivery in the quantity and condition in which they are loaded. Since the consignee of the goods does not participate during loading, they can protect their interests by demanding that a "clean on board" bill of lading be issued. It is the shipper's duty to ensure the loading of sound goods. If the goods meet this requirement, the master can sign a "clean on board" bill of lading. However, it is considered a bad and inadmissible practice for the master of the vessel to sign a "clean on board" bill of lading solely based on receiving a consignor „letter of indemnity“, especially if the loaded goods do not meet the relevant requirements of the commercial contract and the charter party.*

Keywords: *Bill of Lading, Clean on board, Claused bill of lading, Letter of Indemnity*

1. Introduction

In the dynamic world of international trade and shipping, the bill of lading takes center stage as a critical document that shapes the course of transactions and deliveries. This document not only represents proof of the cargo's shipment but also plays a multifaceted role in commercial contracts, involving a spectrum of parties (Dimitrakieva et al. 2023, Fedotova et al. 2019). The master of the ship, acting on behalf of the consignee, shoulders the responsibility of ensuring that the goods are loaded and delivered in the same condition as they were received (Tsonev, 2021). To safeguard the consignee's interests, a "clean on board" bill of lading is often sought, but its issuance is contingent on the shipper's duty to load sound goods. In this context, the use of a "clean on board" bill of lading based solely on a consignor's "letter of indemnity" when the loaded goods fail to meet the contractual requisites remains a contentious issue. This article explores the significance of the bill of lading, the distinctions between "clean" and "claused" bills, and the role of letters of indemnity in international shipping. Additionally, it delves into the consequences of a master signing a "clean on board" bill of lading under such circumstances, ultimately shedding light on the ramifications that could extend to the realm of P&I Club coverage.

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1.1. Bill of Lading and "Hague Rules"

The Bill of Lading is a cargo document introduced by the **International Convention for the Unification of Certain Rules of Law relating to Bills of Lading ("Hague Rules")**, and **Protocol of Signature** (Brussels, 25 August 1924).

According to Article 3 of the Convention,

3. After receiving the goods into his charge the carrier or the master or agent of the carrier shall, on demand of the shipper, issue to the shipper a bill of lading showing among other things:

(a) The leading marks necessary for identification of the goods as the same are furnished in writing by the shipper before the loading of such goods starts, provided such marks are stamped or otherwise shown clearly upon the goods if uncovered, or on the cases or coverings in which such goods are contained, in such a manner as should ordinarily remain legible until the end of the voyage.

(b) Either the number of packages or pieces, or the quantity, or weight, as the case may be, as furnished in writing by the shipper.

(c) The apparent order and condition of the goods (Hague Rules, 2023).

1.2. Obligations of the master with regard to clausing the bill of lading

According to Cooke, J., Kimball, J., Young, T., Martowksi, D., Ashcroft, M., Lamber, L., Taylor, A., Sturley, M., (2014): 18.22 *Article III rule 3 of the Hague and Hague-Visby Rules imposes a contractual duty on the carrier to issue to the shipper on demand a bill of lading showing the specified information, including the "apparent order and condition" of the cargo loaded. The refusal to issue a bill which makes any statement as to the apparent order and condition of the goods is a breach of contract*, but that does not answer the question of the nature and extent of the master's duty as to the accuracy of the statement.

Conclusion: The carrier or the master or the agent of the carrier is obliged to issue a Bill of Lading in return for the loaded goods on board the vessel. The Bill of Lading should identify the goods, their marks and number or quantity or weight, as well as ***The apparent order and condition of the goods***.

1.3. Functions of the bill of lading

The bill of lading is regarded as a "Common Export Document" by International the Trade Administration. It is a legally binding document that is used in foreign trade and international transport (International Trade Administration, 2023).

It has three main functions:

- *It is a receipt for the shipped goods.*
- *It is a document of title to the goods described in the bill of lading.*
- *It is evidence of an existing contract of carriage for the goods on it (Kenton, 2023).*

Definition for a title:

- *A title is a document that shows legal ownership of a property or asset. A title can represent ownership of a real asset such as a car or an intangible property or asset such as a trademark (Gard Guidance, 2011).*

Meaning of "Clean on board"

Generally speaking, any bill of lading related to the carriage of certain cargo and duly signed by the master of the vessel is considered "clean on board," provided that there are no remarks by the master related to the quantity and conditions of the cargo. It is common practice for shippers to request from carriers that the bill of lading be marked as "Clean on board."

According to Kenton, W., (2023): *If a clean Bill of Lading is issued with the added term "clean on board", this means that the goods have been received in good order and in good condition, as far as the shipping company can see.*

This term dates back to the days when every shipment was physically loaded by crew members. In those days, cargo could be physically inspected for discrepancies. Due to modern containerization, it is frequently impossible to inspect the condition of goods. Therefore, from a legal standpoint, the term shipped on board, along with said to contain (stc) and shipper's load, stowage, and count, is frequently used. As a result, the shipping company protects itself against shipment shortages and damage (Logistics Glossary, 2023).

According to Alkens, R., Lord, R., Bools, M. (2016): 2.82 Article 27 of UCP 600 defines a clean transport document as *"one which bears no clause or notation which expressly declares a defective condition of the goods and/or the packaging"* (Alkens et al. 2016).

2. Application of Clean Onboard Bill of Lading. How does a Clean Onboard Bill of Lading work?

In international trade, goods are always traded and delivered by some means of transport. It is also a common practice for goods to be transshipped to other vehicles or storage facilities. All of this means that there are transportation agents between the seller and the buyer who are responsible for the carriage and delivery of the goods (Gramchev et al. 2023, Narleva, Gancheva, 2023). On the other hand, it is difficult and uncomfortable for buyers to participate directly. This is why the master of the ship is the person who receives the goods on behalf of the consignee and is responsible for their delivery in the quantity and condition in which they were loaded. Since the consignee of the goods does not participate during loading, they can protect their interests by demanding that a "clean on board" bill of lading be issued. This stipulation always affects the sales contract and the charter party for the carriage of the purchased goods.

It is the reason that a Clean On Board Bill of Lading is usually required under a contract of Letter of Credit between buyer and seller in terms of Transport Document under shipment of sale carriers. It is a tool in the hands of the buyers to order the carriers to check cargo conditions before loading and take all precautions in case of any damages to cargo including handing over a letter of protest to the shippers.

According to Kollerath, S., (2023): *A clean bill of Lading means, the carrier of goods has received the cargo in good condition with proper packaging. In other words, the cargo received under a clean bill of lading has no clause, notation or remarks on the quantity or quality of goods as well as packing. After issuing a clean bill of lading by the carrier, the responsibility for poor packing, damage of goods and other handling defective falls on the carrier.*

Once the goods are received in good condition with proper packing on board the vessel, the carrier issues a Clean Onboard Bill of Lading. Clean Onboard Bill of Lading certifies that the cargo on board has no negative clause, notation or remarks on the quantity, quality or packaging of goods. In other words, when issuing a clean onboard bill of lading, the carrier certifies that the goods gone on board the vessel are in good condition with proper packing (Kollerath, 2023).

3. Clausing bills of lading

According to The Swedish Club: *When the loaded cargo is not in apparent good order and condition then the master must insert an appropriate clause in the bill of lading, otherwise bears the responsibility for all damages on it which are not included as remark in the bill of lading.*

- *'Clausing' a bill of lading is the act of inserting written remarks about the apparent order and condition of the cargo on loading.*

- *If the cargo is only subsequently damaged on the ship, the bills of lading will need to be issued 'clean'.*

- *If there are apparent defects on the cargo on loading, the bills of lading must be claused.*

- *The Master is not expected to be an expert, just observant: if it looks like bulk sugar but smells like salt, the Master is on notice (The Swedish Club, 2023).*

According to the Swedish Club: *Clausing a bill of lading is the process of inserting written remarks on the bill of lading regarding the quality or condition of the cargo on loading.*

For example, *The MV TSC is to load 650 steel coils. 250 of the steel coils are wet and rust-stained on loading. Since 250 steel coils contain defects – being wet and rust stained – the Master must clause the bills of lading by inserting a remark about the condition of the cargo.*

The bills of lading may therefore describe the cargo along the below lines (with the yellow highlighted part being the claused remarks (The Swedish Club, 2023).

4. Different types of Onboard bills of lading

According to Trade Finance Global: *Once the goods are received by the carrier, the condition of the goods is analyzed before preparing the onboard bill of lading.*

If the quality of the goods is not up to the mark, the carriers must add a clause to the onboard bill of lading signifying that the received goods were not in good condition when they were received.

On the other hand, the goods that pass all the quality tests should be given a clean bill of lading. The diagram below sums up the entire process.

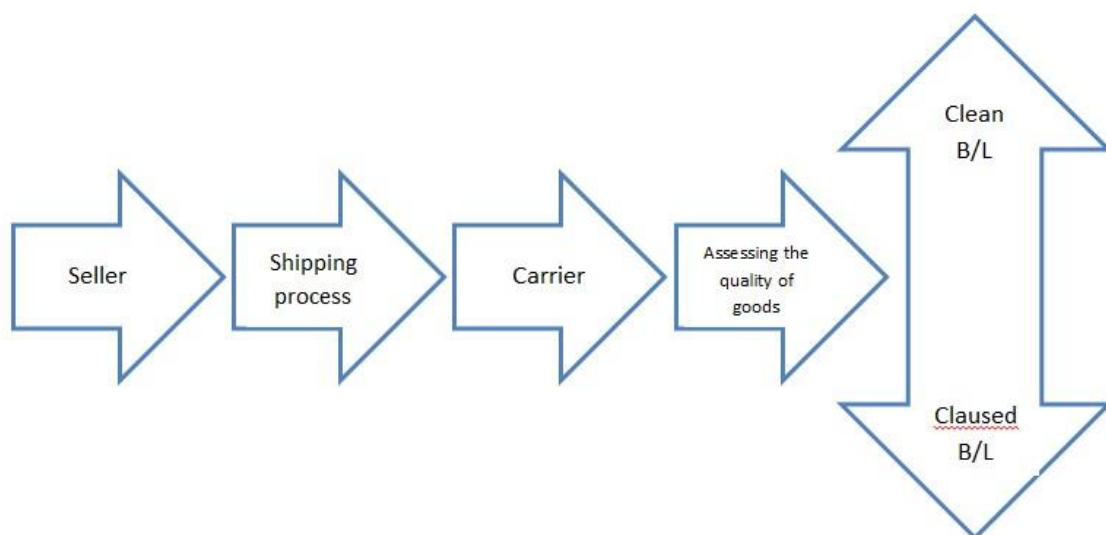


Fig. 1 – Diagram for the process of issuing a “clean on board” or “claused” bill of lading (Abrams, 2023)

4.1. Clean Onboard Bill of Lading

A clean bill of lading is the desired outcome for sellers because once it is issued, they no longer have to worry about the quality of the goods. This is because, with the release of a clean bill of lading, the responsibility for maintaining the quality of the goods falls on the shoulders of the carrier. Not only is it their desired outcome, but a clean bill of lading is also very important for sellers to obtain in cases where banks have guaranteed payment for the goods, as the contract is formalized in the form of a 'letter of credit'. Banks usually reserve the right to demand a clean bill of lading as a prerequisite for finalizing the deal, making it necessary for sellers to obtain one.

4.2. Claused Onboard Bill of Lading

Carriers have the right to thoroughly inspect the goods before issuing an onboard bill of lading, and meticulous checking may reveal defects in the cargo. If this is the case, contractors have the right to add a clause to the onboard bill of lading. This should serve as a red flag for sellers, indicating that the goods do not match the provided description. The clause protects carriers from the buyer's claims, and the blame for poor handling of goods does not fall on them during the delivery phase. It is the carrier's choice to add additional remarks specifying the defect, such as 'decaying goods' and 'damaged cargo'. However, this practice is acceptable only when the

carrier and the booking party have agreed upon the claused onboard bill of lading. It is possible for the bank funding the deal to reject the claused bill of lading, as the shipping documents must be prepared according to the bank's demands. Shipping documents are considered evidence of the deal (Abrams, 2023).

5. Letter of indemnity

According to the Logistics Glossary: A letter of indemnity (LOI) is a document by which the shipper indemnifies the shipping company against the implications of claims that may arise from the issue of a clean Bill of Lading when the goods were not loaded in accordance with the description in the Bill of Lading.

There are two different kinds of letters of indemnity: letters of indemnity for quantitative clauses and letters of indemnity for non-quantitative clauses. When the Bill of Lading forms the basis of a documentary credit, the bank usually demands a clean Bill of Lading. This is a Bill of Lading signed by the Master without any remarks.

If for one reason or another, the goods were not loaded as prescribed, the captain may want to put remarks on the Bill of Lading. By doing so, the Bill of Lading is no longer clean and the bank will not give documentary credit. In order to remedy this, it is custom to put the remarks not on the Bill of Lading, but on the mate's receipt and to draw up a letter of indemnity in which the shipper indemnifies the captain (the shipping company) against the potential implications thereof (West, 2023).

5.1. Indemnity arising from the signing of bills of lading

According to Coghlin, T., Kimbal, J., Baker, A., Belknap, T. JR., Kenny, J. (2014): 19.22 If the master is required by the charterers to sign or permit to be signed bills of lading which impose on the owners greater liability than that which they have assumed under the charter, the owners will usually be entitled to be indemnified by the charterers in respect of their additional liability: see paragraphs 21.31 to 21.36. But the right to indemnity may be lost if the master signs bills in circumstances where it was his duty to refuse to sign: a number of possible such circumstances are considered in paragraphs 21.37 to 21.60 (Coghlin et al. 2014).

Primary Conclusion: If the master of the ship is required by the charterers to sign or allow the signing of bills of lading that impose greater liability on the owners than what the owners have assumed under the charter, the owners typically have the right to be indemnified by the charterers for the additional liability. This is detailed in paragraphs 21.31 to 21.36.

Loss of the Right to Indemnity: The right to indemnification may be lost if the master signs bills of lading in circumstances where it was his duty to refuse to sign.

This quote underscores the importance of the accurate execution of contracts and the responsibilities of the ship's master in relation to signing bills of lading. It appears that the legislation takes into account specific situations in which the master may require indemnification, but it also acknowledges the possibility of losing that right if he fails to act in accordance with his duties.

6. Common practices in shipping

According to West P&I Club: Owners are obligated to follow charterers' lawful instructions as per the terms of the charter party. English law implies a general indemnity for owners to recover losses incurred due to adhering to charterers' instructions. However, this implied indemnity does not cover all scenarios.

Owners often receive Letters of Indemnity (LOIs) from charterers or third parties to secure explicit indemnity for obeying charterers' instructions. These LOIs are crucial in situations that might pose insurance or cargo claim risks. LOIs are commonly requested in the following instances:

a) Issuing bills of lading, either clean or containing inaccuracies, against letters of indemnity: The Shipper or charterer pressures the master to issue clean bills of lading, even when cargo is damaged during loading, or bills showing a different shipment date. They do this to

present the bills to banks under the letter of credit system and receive payment under the sale contract.

The shippers'/charterers' interests under letters of credit do not concern the carrier, who should focus on their responsibilities under the contract of carriage and charter party. Owners must ensure that bills of lading issued "for and on behalf of the master" contain accurate information.

In some cases, the shipper or charterer may request the master to issue bills of lading with inaccurate details regarding the cargo's condition, quantity, or order, in exchange for an LOI. The charter party might explicitly state that the master can only issue a clean bill of lading against an LOI. In such situations, if there are concerns about the quantity, order, or condition of the goods, the master should consider:

- (i) Issuing a clean bill and rejecting non-conforming goods; or*
- (ii) Accepting the goods but issuing a bill of lading with specific clauses indicating the issues.*

If the master issues a clean bill of lading despite knowing or having reason to believe it does not accurately represent the cargo's true condition (i.e., not rejecting non-conforming goods), P&I insurance cover related to ensuing cargo claims might be compromised. For example, if the shipper's figures are clearly incorrect, and bills of lading are issued using those figures, P&I cover may be affected, especially for shortage claims.

Bills of lading with inaccuracies, known by the carrier, could be used against them by innocent third-party receivers or transferees. P&I cover for such cargo claims might also be compromised. In such cases, any provided LOI might not be legally enforceable.

These restrictions or even exclusion from Club cover are set out in Rule 2 Section 16 (C) (e).

After all, several conclusions and insights can be drawn:

- **Legal Obligations:** The text emphasizes that owners of vessels are legally obligated to adhere to the lawful instructions given by charterers in accordance with the terms of the charter party.
- **Implied Indemnity:** English law implies a general indemnity for owners, which allows them to recover losses incurred as a result of following charterers' instructions. This indemnity can provide a measure of protection to owners in the course of their business operations.
- **Limitations of Implied Indemnity:** While the implied indemnity is a valuable safeguard, the text points out that it does not cover all situations or scenarios. This suggests that there may be exceptions or conditions where owners cannot rely on this implied indemnity.
- **Use of Letters of Indemnity (LOIs):** To address specific situations that might pose insurance or cargo claim risks, owners often receive Letters of Indemnity (LOIs) from charterers or third parties. These LOIs serve to secure explicit indemnity for owners when they follow charterers' instructions.
- **Crucial Role of LOIs:** LOIs are considered crucial, especially in cases where charterers or shippers pressure the ship's master to issue clean bills of lading, even if the cargo has sustained damage during loading or if there are inaccuracies in the bills, such as discrepancies in the shipment date.
- **Protection of Interests:** The text highlights that the interests of shippers and charterers under letters of credit do not necessarily align with the carrier's interests. It underscores the importance of owners ensuring that bills of lading issued "for and on behalf of the master" contain accurate information.
- **Consequences of Inaccurate Bills of Lading:** If the master issues a clean bill of lading despite having knowledge or reason to believe that it does not accurately represent the cargo's true condition (e.g., by not rejecting non-conforming goods), it can have significant consequences. This

includes the potential compromise of P&I insurance cover, particularly for claims related to cargo shortages.

- **Risks of Inaccuracies:** Bills of lading with inaccuracies, known by the carrier but issued regardless, could be used against the carrier by innocent third-party receivers or transferees. This can further compromise P&I insurance cover for cargo claims.

- **Exclusion from Club Cover:** The text mentions that restrictions or even exclusion from Club cover for such situations are specified in Rule 2 Section 16 (C) (e), indicating that the consequences for failing to adhere to proper procedures can be significant.

7. Conclusion

The bill of lading is considered one of the most important documents in world trade because it is proof of the traded merchandise being transferred or transported. It also provides legally binding information about the traded goods as cargo on board the transporting vessel. Any incorrect information related to the cargo and its condition could damage the interests of the receiver, who ultimately pays all bills, including the price of the goods and their transportation.

Signing a "clean on board" bill of lading by the Master based on receiving a consignor's "letter of indemnity," especially if the loaded goods do not meet the relevant requirements of the commercial contract and the charter party, is considered misrepresentation and is regarded as a wrongful action for which the Master and the carriers are fully responsible. In such a case, they may not receive any P&I Club coverage.

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