The Meaning of "Freight Pre-Paid" in International Shipping Contracts

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> "When *I* use a word," Humpty Dumpty said, in a rather a scornful tone, "it means just what I choose it to mean—neither more nor less."
> "The question is," said Alice, "whether you *can* make words mean so many different things."
> "The question is," said Humpty Dumpty, "which is to be master—that's all."
>
> Alice was too much puzzled to say anything, …[1]

Consignees may rightfully feel that they too have gone "through the looking glass" after having received their cargo, shipped under a document marked "freight pre-paid", and then faced with a demand for the payment of freight.

The traditional role of a freight forwarder has been evolving in recent years into that of a Non Vessel Owning Common Carrier (NVOCC). Its role is dual, acting both as an agent vis-à-vis its client, the shipper, and as a principal, vis-à-vis the carrier. Professor Tetley, describing this phenomenon, identified the following characteristics that make a freight forwarder a NVOCC[2]:

- It acts as a principal contractor arranging the carriage in its own name;
- The fee payable by the shipper is a straight freight charge;
- It arranges to pay lower freight rates to the carrier and makes its profit from the difference between the two;
- It often consolidates the cargoes of a number of clients into a single container, resulting in savings which benefit both the freight forwarder and its clients.

In these circumstances, the consignee or the shipper of the cargo often has no idea who is performing the carriage. The shipper pays the freight charges directly to NVOCC and waits for

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[1] Lewis Carroll, *Through the Looking Glass*, 1872.
[2] William Tetley, Marine Cargo Claims, 3rd ed. (Montréal: Les Éditions Yvon Blais Inc., 1988) at p. 692.

the cargo to show up at its warehouse. What happens if, after the NVOCC is paid but before it pays its agents or the performing carrier, the NVOCC goes bankrupt? Does the shipper or a consignee of the goods have to pay the freight charges the second time around?

This issue was first considered by the Federal Court in 1982, in *C.P. Ships v. Les Industries Lyon Corduroys Ltée.*[3] The Court held that, as a general rule, where a debtor, instead of paying his creditor, chooses to pay a third party, he does so at his peril. To avoid having to pay twice, the Court held that debtor must establish either:

(1) that the creditor actually authorized the third party to receive the money on his behalf, or

(2) that the creditor held the third party out as being so authorized, or

(3) that the creditor by his conduct or otherwise induced the debtor to come to that conclusion, or

(4) that a custom of the trade exists to the effect that in that particular trade and in those particular circumstances, both the creditor and the debtor normally would expect the payment to be made to the third party.

In the 1980s, when freight forwarders generally performed a straight forward agency role, it was difficult for the shipper to establish the necessary elements of the test. The shipper generally knew who the carrier was and a contract was established as between the shipper and the carrier, as principal parties. The freight forwarder acted as a match maker, never a bride. It remained the shipper's responsibility to ensure that the carrier was paid. In this context, it is not surprising that the Court held that a notation "freight prepaid" in the circumstances where the shipper knew that it had not paid the carrier could not be taken at face value, and was to be distinguished from a notation such as "freight paid in advance."

However, as the freight forwarders role evolved into that of NVOCC, the relationships between the parties became less clear. The NVOCC was no longer just an agent who brought together principal parties to strike a bargain. Rather, he now dealt in his own name, as a principal, in a multilayered world of agency relationships established to meet the demands of increased volume at ever decreasing price.

In 1999, the Federal Court revisited this issue in *Morlines Maritime Agency Ltd. v. IKO Industries Ltd.*[4] The Court applied the *C.P. Ships* test, and found that the carrier did not notify the shipper, in a reasonable period of time, that it did not receive payment. Accordingly, the carrier was held to have conducted itself in such a way that the shipper would be induced to

[3] [1983] 1.F.C. 736.
[4] [1999] F.C.J. No. 1939; 180 F.T.R. 12; 94 A.C.W.S. (3d) 413.

believe that the freight forwarder was authorized to receive payments. The Court also found that given the relationships between the parties, the carrier expected that payment would in fact be made by the freight forwarder. Given that both the shipper and the carrier were held to have understood and expected that the payment was to be made to the freight forwarder, the carrier's action against the shipper failed. However, the Court did not resolve the ambiguities which, at that time, existed with respect to the interpretation of the phrase "freight prepaid," which were generated by the *C.P. Ships* decision. Notwithstanding the holding in favour of the shipper, the Court had not, at that time, gone so far as to affirm that the notation "freight prepaid" indeed meant what it said.

It took another ten years for the phrase "freight prepaid" to receive a second look by the Federal Court. In *H. Paulin & Co. v. A Plus Freight Forwarder Co.*[5], H. Paulin & Co., an Ontario based consignee and a manufacturer and importer of hardware, retained A Plus Freight Forwarding, a Taiwan based freight forwarder, to arrange for shipments of various cargo from Asia to Canada. A Plus made all necessary arrangements for the shipment of the cargo and, in so doing, acted as NVOCC. The goods to be moved were of different weight, size and description. Some were dense and heavy whereas others had already been packaged for retail sale and thus were lighter but more voluminous. Since all goods had to be moved in containers, which have both volume and weight limitations, A Plus was hired to arrange for the consolidation of a mixture of light and heavy goods in the same container to maximize efficiencies within the weight and space restrictions. A Plus accepted this assignment, charged payment for the freight and marked the straight bills of lading it issued with a notation "freight prepaid." The Federal Court found that A Plus undertook to perform, or in its own name to procure, the performance of the entire transport and assumed personal responsibility for it.

A Plus, in turn, retained the services of Scanwell Logistics, a larger Taiwan based logistics company. Vis-à-vis Scanwell, A Plus acted as a principal. Scanwell issued "Forwarder's Cargo Receipts" with respect to the cargo, identifying itself as a carrier. Scanwell, in turn, retained an ocean carrier to move the cargo to Canada and paid the freight, expecting that its bill would be paid by A Plus. All receipts were marked with a notation "freight prepaid."

The inevitable happened. A Plus went out of business before it paid Scanwell's accounts. Scanwell, the middleman in this transaction, was truly caught in the middle. It had paid the ocean line for actually performing the carriage but had not yet received payment from its contractual client. Scanwell obtained judgment in Taiwan against A Plus, which was returned unsatisfied. Looking to collect on its account, Scanwell sued H. Paulin for the freight charges. The theory was that H. Paulin, the owner and the consignee, was the one who benefited from the transportation and should be the one to bear the loss.

[5] [2009] F.C.J. No. 899.

Justice Harrington noted that although H. Paulin was aware that A Plus was not a carrier in its own right, it dealt with and paid A Plus to exclusion of all others. H. Paulin was not even aware of the existence of Scanwell. During the more than two years that A Plus did business with Scanwell, the latter never made enquiries as to who was behind A Plus. Scanwell chose to deal with A Plus on credit and issue "freight prepaid" documents having not received payment and hoping to be paid in future. Scanwell appealed to the Court's sense of "equitable justice," on the theory that it was an innocent party who performed the contract, but the Court dismissed this theory out of hand, commenting that Scanwell must live with the consequences of the risks it chose to take.

The Federal Court then turned its attention to the interpretation of the term "freight prepaid" on bills of lading and similar receipts. Justice Harrington ruled that, in a maritime context, marking the bills with the notation "freight prepaid" has the opposite effect than marking them as "freight collect." Had the receipts been so marked, H. Paulin would not have been entitled to delivery and Scanwell would have been entitled to insist on payment. However, the contracts as drafted clearly stated that freight had been prepaid. It was held to be a clear representation by a carrier, to be relied on by all the world, in the same way as statements as to apparent good order and condition of the cargo. Any notation on a bill of lading or similar type receipt is made as a representations vis-à-vis the world, not just the shipper and the carrier. In the same way as a deliberate misrepresentation by the issuance of a clean bill of lading when the cargo is obviously damaged would be seen as a conspiracy between the shipper and the carrier, to be relied on by others to their detriment, a notation "freight prepaid" must be taken at face value when appearing on a bill of lading.

The Federal Court's rationale makes good commercial sense, facilitating international commerce and the worldwide movement of goods. While Cargo may move on the sea, international commerce floats on paperwork. Commercial actors must be able to rely, prima facie, on the representations found on Bills of Lading and similar documents. They must mean what they say, or commerce fails and international trade becomes a journey "down the rabbit hole".

The Federal Court rejected the analysis set out in two decisions of the Quebec Court of Appeal in *2318-1654 Quebec inc. c. Swiss Bank Corp. (Canada)*[6] and *SGT 2000 inc. c. Molson Breweries of Canada Ltd.*[7] The Quebec Court of Appeal, on similar facts, but in trucking context, ruled that the consignees became subject to the same liabilities as the shipper, including the obligation to pay freight. The Quebec Court of Appeal held that the statutory liability of a consignee is created by section 2 of the *Bills of Lading Act*,[8] which states that every consignee of goods named in a bill of lading is subject to all liabilities in respect of those goods as if the contract contained in the bill of lading had been made with himself. The Quebec Court of Appeal

[6] [2000] J.Q. no 2059, J.E. 2000-1475.
[7] 2007 QCCA 1364, J.E. 2007-2013.
[8] R.S.C. 1985, c. B-5.

acknowledged that there is an exception to this rule, since it is not a rule in the nature of public policy, such that the parties could agree to "another arrangement" and thereby avoid the statutory liability of the consignee. The burden of establishing "another arrangement" falls squarely on the shoulders of the consignee. Alas, the Quebec Court of Appeal found that the consignee was unable to meet this burden in the case at bar. Given these facts, the phrase "freight prepaid" was held not to, in and of itself, constitute a waiver by the carrier of its rights under section 2 to be paid by consignee.

The Federal Court distinguished these decisions on the ground that H. Paulin did not become owner of the cargo by virtue of the bills of lading which were not negotiable and apparently were never in the shippers' hands. The Federal Court specifically rejected the presumption, common in trucking cases by virtue of section 2 of the *Bills of Lading Act*, that the contract is made between the owner of the goods and the carrier. The Federal Court stated that "there is no such presumption in carriage by sea."

We are thus left with two lines of authorities, one from the Federal Court and the other from the Quebec Court of Appeal, which at first glance appear to stand in opposition to each other. On the surface, the Federal Court, over the past 30 years, has been steadily moving toward a pragmatic, commercially based reading of bills of lading, requiring a strict, literal interpretation of their terms. The Quebec Court of Appeal, on the other hand, relies heavily on statutory authority, which can be portrayed as lagging behind commercial realities. However, while the Quebec decisions do not affirm a literal interpretation of phrases such as "freight prepaid" found on bills of lading, they recognize that shippers and consignees may enforce such terms if they can demonstrate evidence of "another arrangement," to displace the statutory presumption of liability of the consignees. Looking at the Quebec decisions in this light, they may not, after all, be contradictory to those of the Federal Court. While "freight prepaid" does not automatically acquire its literal meaning in Quebec, consignees can seek to establish such reading of the bill of lading if they can establish "another arrangement," which looks similar to the test established in *C.P. Ships* almost 28 years ago. It seems that in so doing, the Quebec decisions are a step behind the Federal Court, rather than in opposition to it.

The lesson to be drawn from the *H. Paulin* and other cases referred to above is that freight forwarders, NVOCCs and carriers ought not to be cavalier about the use of the phrase "freight prepaid" on bills of lading. Unless the party issuing the bill of lading was actually paid, has an established relationship with the retaining party or, at the least, is reasonably certain of its creditworthiness, these notations should not be used. Failing to heed to this advice may cost them dearly, as "freight prepaid" likely means just that: no further payments will be forthcoming.