Norwegian Arbitration Award - ND-1989-282

Authority	Norwegian arbitration award
Date	1989-10-24
Doc no./published	ND-1989-282
Key word(s)	(89-37) Escalation clause in catering and housekeeping contract for the Polycastle drilling platform - increase in costs due to reduction in work hours in 1987. Costs.
Summary	A catering and housekeeping contract includes a provision for the half-yearly adjustment of the rates based on changes in the wholesale price index and pay scales. The contractor was of the view that the reduction in work hours in 1987, which involved a 7.14% increase in salary costs, entitled the contractor to a rate increase and, if this was not the case, that the escalation clause had to be modified pursuant to Section 36 of the Norwegian Contracts Act. The profit margin under the catering and housekeeping contract was very modest. The shipowner, which had chartered the rig to Statoil, referred to the fact that Statoil had rejected the claim to adjust the rig rates due to the reduction in work hours. - The Arbitral Tribunal finds in favour of the shipowner. The expression “pay scale” must be understood as being the pay and working conditions that, on a general basis, have specific financial consequences for employers. However, nothing general could be stated about the effects of the reduction in work hours, which could vary considerably for individual companies. The escalation clause was not linked to actual cost increases, but to standardised criteria. A cost increase of 7.14% did not provide grounds for modifying the escalation clause pursuant to Section 36 of the Norwegian Contracts Act. - Costs are awarded. In disputes concerning commercial contracts, the exemption rule in Section 172, paragraph two of the Norwegian Civil Procedure Act must be applied with care.
Proceedings	Norwegian arbitration award of 24 October 1989.
The parties	SAS Service Partner (Attorney Ole Borge Jr.) versus K/S Rasmusen Offshore A/S (Supreme Court Attorney Georg Scheel).
Author	Sole arbitrator: Supreme Court Judge Tore Schei.

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Subject matter of the dispute: Claim for adjustment of payment in catering and housekeeping contract for the accommodation platform “POLYCASTLE”.

K/S Rasmussen Offshore A/S (hereafter referred to as Rasmussen) and SAS Service Partner (hereafter referred to as SSP), entered into an agreement on 17 March 1986 for catering and housekeeping services on board the accommodation platform “POLYCASTLE”. SSP agreed to provide all catering and housekeeping services etc. for all persons, including both those stationed there and visitors, on board the accommodation platform in return for a specified payment from Rasmussen. During the contract period, “POLYCASTLE” was in operation for a group of oil companies, of which Statoil was Rasmussen’s contracting party. It has been reported that this assignment commenced on 29 June 1986 and provisionally ended on 29 June 1988.

Annex C of the contract of 17 March 1986 stipulates detailed rules for the payment SSP was to receive for its services. Clause 9 of this annex stipulates rules for the adjustment of rates. The provision has the following wording:

“Adjustment of rates.

All rates referred to in clauses 1, 2, 3 and 4 in this Annex C are fixed until 1 April 1986. Thereafter, these rates shall be adjusted every six months with effect from 1 April and 1 October each year, and for the first time on 1 April 1986, in accordance with the following formula:

New price = Previous price (0.32 Mn/Mo + 0.68 Ln/Lo)

The basis for adjustment will be as follows:

Previous price = Prices pursuant to the Contract.

Mo = Statistics Norway's wholesale price index for Food Group B for January 1986.

Mn = The above-mentioned index for the month prior to adjustment.

Lo = Pay scales for the respective groups of the Contractor’s personnel in accordance with agreements between the Norwegian Employers’ Confederation (NAF) and the Norwegian Oil and Petrochemical Workers Union (NOPEF)/Catering Workers’ Federation (CAF) as of 1 October 1985 are considered equal to 100.

Ln = 100 +/- average percentage change in the pay scales for the respective groups of the contractor's personnel in accordance with the collective agreement between NAF and NOPEF/CAF as of 1 April and 1 October each year, compared with the corresponding pay scales as of 1 October 1985.”

In the collective pay settlement in 1986 it was agreed to reduce the standard work hours effective from 1 January 1987. Among other things, this resulted in SSP’s employees on board “POLYCASTLE” having their work hours reduced from 36 to 33.6 per week.

A dispute arose between SSP and Rasmussen about whether SSP could claim compensation for increased costs resulting from the reduction in work hours. There was also disagreement between the parties about whether, and if so to what extent, the reduction in work hours resulted in increased costs for SSP.

SSP's position was that the adjustment clause in clause 9 of annex C in the contract authorised compensation for the increase in costs that resulted from the reduction in work hours. Rasmussen’s position, in light of what Statoil asserted to Rasmussen, was that the reduction in work hours did not entail any change to the “pay scale” and that there were therefore no contractual grounds for claiming compensation.

The parties failed to arrive at any solution to the dispute and agreed that the dispute should be decided by arbitration. The parties have jointly appointed Supreme Court Judge Tore Schei as arbitrator. One oral hearing has been held for the case which was attended by the arbitrator and counsels. Pleadings were also exchanged. Both parties have declared that they consider the preparatory proceedings to have concluded and that they understand that the case shall be decided based on how it now stands, without further oral hearings.

The plaintiff, SAS Service Partner Offshore and Industrial Catering A/S, has principally asserted the following to the Arbitral Tribunal:

The intentions of the central organisations when they entered into the agreement to reduce work hours was that this would be implemented with the least possible cost to the companies through increased productivity etc. However, it was clear to everyone that, other than for a small minority, most companies would not be able to compensate for the additional costs from shorter work hours through increased productivity. Together with

CAF and NOPEF, SSP attempted to reduce staffing levels on “POLYCASTLE”, however was unable to do so. Therefore, for this platform, the reduction in work hours alone resulted in an increase in labour costs of 7.14%, due to the fact that the full time equivalent for each employee was reduced by 7.14%.

The plaintiff agrees that when assessing the claim for compensation, clause 9 in annex C of the agreement of 17 March 1986 must be used as a basis. One of the two elements that are part of the adjustment formula is the “pay scale”. It is of vital importance that reference is made to the “pay scale” and not the salary table. Consideration must not only be made to additional krone amounts, but also other collective changes that have financial consequences. Among other things, this is confirmed in calculations by the Norwegian Employers’ Association for Operating Companies (NOAF) of costs in connection with the wage settlement. NOAF calculated the cost increases in connection with a number of changes to the collective agreement which did not apply to the salary table. There has never been any doubt that these types of changes must also be applicable pursuant to clause 9 in annex C. Disagreement has only arisen due to the reduction in work hours. There are no grounds in the contract for any such differentiation between the financial effects of the revision of the work hour provision compared with the financial effects of changes to other parts of the system of agreements

If the “pay scale” is defined more restrictively to what the plaintiff considers correct, the assumption must therefore be that comparable pay scales are being used. When the new annual salary tables for the employees stipulate the salary for 7.14% less work than the previous collective agreement, the new tables cannot be used as a basis in the calculation of SSP’s claim without compensation being given for precisely the difference in the basis for the table. Anything else would be to assign the risk for the consequences of the reduced work hours to SSP and that would not be in accordance with what must have been the preconditions of the parties when the agreement was entered into.

It was correctly claimed by the defendant that SSP bears the risk of, for example, an increase in the employer’s national insurance contribution. However, this is a risk that can be predicted and therefore factored in to a certain extent. However, it cannot be the same as SSP having the risk of a cost increase the company had no reason to believe it would have passed on to it.

The fact that it cannot have been assumed by the parties that SSP would have this risk is also confirmed by Rasmussen's position originally having been that SSP should receive coverage for its additional costs. If was only when Statoil entered the picture that Rasmussen found they had to take a different position. However, it is clear that the subsequent actions of both parties confirm that SSP’s understanding of the contract is correct.

“Industry practice” is asserted as independent grounds for compensation. SSP has submitted a number of examples of cost increases due to reduced work hours being compensated for in catering and housekeeping contracts. If these adjustment clauses were somewhat different to the clause in the contract in the present case, this must be of limited importance in this context. The massive amount of documentation that has been presented shows clear encouragement for increased salary costs to be compensated, including when the increased salary costs can be traced back to the fact that less work is provided for the same price. The defendant has not presented a single example of compensation having been denied.

Provided that the defendant’s understanding of the contract is fundamentally correct, there must be grounds for revising the contract pursuant to Section 36 of the Norwegian Contract Act. An unforeseen and significant change in the contractual assumptions has occurred. In reality, an increase in labour costs of 7.14% is very significant, not least when taking into consideration the extremely small profit margins in the agreement. Also of key importance in the assessment pursuant to Section 36 of the Norwegian Contracts Act must be that all reasonable assumptions would argue for compensation. For SSP it makes no difference whether more has to be paid per hour of work performed or whether less work is performed for the amount that was previously paid in salary.

As mentioned, SSP’s contractual party, Rasmussen, found the claim for compensation to be reasonable. The fact that Rasmussen has not paid such compensation is due to Statoil. However, Statoil is a member of the relevant employer organisations in connection with operations on the Norwegian continental shelf. These organisations have made statements that the companies will, of course, have increased costs due to the reduction in work hours since a reduction in staffing has not been possible due to increased productivity. Questions can be asked about whether or not Statoil is bound by the employer organisations in connection with this. In any event, it says something about the logic of this reasoning when Statoil acts contrary to its organisations.

The defendant's claim that SSP has not suffered any loss as a result of the reduced work hours is a logical fallacy. SSP has had to increase staffing levels that fully compensate for the reduction in work hours. In connection with this, it is sufficient to refer to the fact that, in the negotiations with the organisations, SSP was not granted the right to reduce the number of personnel on “POLYCASTLE”. SSP's claim for an adjustment must also apply irrespective of the company's specific additional costs.

Clause 9 in annex C lists 1 October and 1 April as being the adjustment dates. However, the dates were selected based on the relevant dates for the review of collective agreements. In this case, the changes occurred from 1 January 1987 and, based precisely on the reasons for selecting the adjustment dates, it must be correct to pay compensation already from 1 January 1987. In addition, taking into consideration the choice of adjustment date, reference can also be made to the grounds that have been asserted for being able to claim coverage for the increase in costs.

The plaintiff has submitted the following prayer for relief:

“1. K/S Rasmussen Offshore A/S is ordered to pay SAS Service Partner Offshore and Industrial Catering A/S NOK 2,076,485, in addition to statutory interest on overdue payments, from the due date for the individual elements of the claim until payment takes place, as well as compound interest on the principal amount and interest balance as of 31 December 1987 and 1988 in accordance with the statutory interest, until payment takes place.
2. SSP is awarded full costs.
3. Rasmussen is ordered to pay all costs relating to the arbitration.”

The defendant, K/S Rasmussen Offshore A/S, has principally asserted the following:

The agreement between the parties is a fixed price contract and is not based on a “Cost+” principle. The extent to which the payment may be adjusted is precisely stipulated in clause 9 of annex C to the contract.

The adjustment clause is a technical provision. It was formulated with the intention that there would not be any discussion about the right to or size of an adjustment in the payment.

Adjustment of the payment is directly linked to two indexes, the wholesale price index for foodstuffs in group B and the pay scales for the respective groups of the contractor’s personnel in accordance with agreements between NAF and NOPEF/CAF. The adjustment clause is based on average considerations. The cost of ingredients for foodstuffs was weighed up against labour costs. The consequence of the wording of the adjustment clause is that if, for example, food prices increase, this will result in an increase to the rates in annex C, without consideration to whether the individual rates are “food intensive” or “wage intensive”.

Since the adjustment clause is directly linked to these two indexes, SSP can incur increased costs that compensation cannot be claimed for. Practical examples can be mentioned, such as an increase in the employer’s national insurance contributions, change in sick leave arrangement etc. Such cost increases, which are not applicable to the adjustment clause, are something SSP carries the risk for. This is precisely the system in the contract. Cost increases that come under the adjustment clause are a risk borne by Rasmussen as long as the clause authorises coverage. Cost increases that fully or partly fall outside of this are a risk borne by SSP. When SSP claims in this case that it has "assumed the risk for” the cost increase associated with the reduction in work hours, this is an attempt to distance themselves from the principal point in the adjustment arrangement that was selected.

The reduction in work hours resulted in no changes to the pay scales, which are the basis for the adjustment. There is not only a formal reason, but also a very real reason for why the reduction in work hours was not included as a cost element in the pay scale. The intention of the organisations in connection with the reduction in work hours was that this would not, insofar as possible, result in increased costs for the employers, and would be balanced out through increased productivity. For some employers, the costs associated with the reduction in work hours could be minor, while for others it would perhaps not be possible to achieve any increase in productivity. However, in terms of this contract, it is not increases in SSP’s actual salary expenses that are grounds for making adjustments, but increases in the general pay scale. The clause is linked to the general and objective considerations, and is made independent of the actual expenses of the contractual parties.

The plaintiff has asserted that the contract presupposed that the “pay scales” were comparable. There may be some substance in this argument, but if it was to be relevant in this instance there had to have been major changes in the fundamental conditions for the salary calculation. This is not the case in this instance.

The defendant has invoked Rasmussen's position concerning an adjustment and made a point out of the fact that it is Statoil that has opposed adjusting the payment. To this it is noted that Rasmussen's position on this matter cannot be assigned weight. Pursuant to the contractual arrangement with Statoil, Rasmussen could have passed any additional costs onto this company. Therefore, Rasmussen did not in fact have any independent interest in opposing the adjustment

There is no industry practice whereby the reduction in work hours granted the right to increase the payment for the catering and housekeeping contract. The defendant has submitted some examples of such an increase. However, the content of the different contracts varies and also differs from the present contract. It also appears to be the case that in some instances there has been partial compensation for additional costs and some of the adjustments also appear to have occurred based on ex gratia positions.

Section 36 of the Norwegian Contracts Act cannot constitute grounds for revising the contract. In this instance, the maximum cost increase is 7.14%. The defendant has not submitted any accounting documentation or other documentation that shows the earnings situation before and after the reduction in work hours.

SSP has not documented that the company has suffered any loss. For certain periods the company had lower staffing levels on "POLYCASTLE" than it was obligated to provide in the agreement with Rasmussen. Rasmussen has not wanted to do anything about this. In reality, SSP has adapted to the reduction in work hours by reducing staffing levels.

If the Arbitral Tribunal should find in favour of SSP's claim for compensation, the company cannot be granted compensation from prior to 1 April 1987. The parties selected the specific adjustment dates with their eyes open and this must be decisive.

The defendant has submitted the following claim for relief:

"1. The Arbitral Tribunal finds in favour of and awards costs to K/S Rasmussen Offshore A.S.
2. SAS Service Partner Offshore and Industrial Catering A.S. shall pay the fees and expenses of the Arbitral Tribunal."

The Arbitral Tribunal has found that it cannot find in favour of SSP's claim for compensation for additional costs due to the reduction in work hours.

Pursuant to clause 9 in annex C of the contract, changes in the "pay scale" provide grounds for adjusting the contractual payment. The Tribunal considers the "pay scale" to be salary and employment conditions that, on a general basis, have specific financial consequences for the employers. As examples of such changes in the "pay scale", reference is made to the letter of 9 December 1987 from NOAF, cf. exhibit 25 to the writ of summons. Cost calculations have been carried out for a number of changes in the collective agreement, the financial effects of which can be quantified. With regard to the reduction in work hours, NOAF wrote the following to a number of companies, including SSP, on 27 February 1987:

"The intentions of the central organisations, cf. section F of the work hour supplement, are that the reduction in work hours shall be implemented with the least possible costs. Among other things, it presupposes initiatives in the individual companies for maintaining production, improving productivity and efficiently utilising work hours.

Therefore, the cost effect for the individual companies as a result of the reduction in work hours will depend on the effect of the above-mentioned initiatives and the extent to which the reduction in work hours will require increased manpower. The costs may therefore vary from company to company and possibly also within a company's different contractual areas. NOAF can therefore not specifically comment on the cost aspect for each company.

Section B of the work hour supplement includes provisions for providing compensation in the hourly pay rates for employees who are employed on hourly wages. This compensation provides full compensation for each employee for the reduction in work hours and can, in isolation, express the companies' costs if staffing is increased to exactly the same extent as the reduction in work hours.

However, we are aware that various initiatives have been implemented in the companies that will influence the final costs associated with the reduction in work hours."

It states here that nothing general can be said about the financial consequences of the reduction in work hours. These could be relatively minor if that the company achieves improvements in productivity, but the effects may also be greater, up to 7.14%. When the consequences are so variable, it is difficult to determine that there has been any change in the "pay scale". It is in itself support for this result that the employer organisations have not been able to quantify the change as a cost increase in the collective arrangement. In addition to this is the fact that the "pay scale" has clearly focussed on the employer organisations' quantifying of the financial

consequences of the operational changes. Based on how the adjustment clause is worded, it is clearly not SSP's actual expenses, but the general, collective wage costs that will form the basis for adjusting the payment.

To support its position, SSP has asserted the parties' preconditions, or what the parties can be assumed to bear the risk for. The Tribunal considers it probable that the parties selected an adjustment clause that would reasonably reflect the principal cost elements. However, on the other hand, a system has been selected (and this must have been done intentionally) for making adjustments that shall be independent of SSP's specific, actual costs. The Tribunal therefore cannot see that a potential requirement for SSP to be able to achieve coverage for the significant cost increases through the adjustment clause can warrant an increase in the contractual payment that has no coverage in the adjustment clause other than being based on a natural interpretation of this.

The plaintiff has asserted industry practice and, in connection with this, has made reference to several contractual arrangements in which, at least in part, compensation was paid for cost increases due to a reduction in work hours. The Tribunal notes that the asserted industry practice cannot in itself be legally binding. These cannot be considered customs or habits developed over a longer period that express the perception in the industry that existed when the contract was entered into. The asserted practice originates from the period when the current dispute was relevant.

However, the asserted practice could be of importance from a different viewpoint. The Tribunal understands the documented practice such that there must have been reasonably widespread encouragement in the industry for full or partial compensation for cost increases resulting from the reduction in work hours. It is correct that the adjustment clauses vary in the different contracts and none are worded in the same manner as in the present contract. However, the Tribunal considers it doubtful that the different linguistic formulations of these clauses can provide the explanation that SSP and also Christiania Dampkjøkken have achieved adjustments in these instances. The attitude in the industry that is expressed through this practice supports the defendant's assertions of what the parties' preconditions have been. However, the Tribunal finds that this cannot be decisive. As has been stated, the contract was worded such that adjustment must occur based on objective criteria and not based on SSP's actual expenses. It appears that it is precisely coverage of such actual expenses that has been accepted in the examples presented. However, it is difficult to consider this as being anything other than contrary to the actual system for adjustment that was selected. It is also difficult to disregard the fact that adjustment could, at least partly, have occurred based on reasonableness considerations.

It is the plaintiff's opinion that if the "pay scale" is to be interpreted as stated above it must be a contractual requirement that the "pay scale" is comparable. The Tribunal understands this reasoning such that if, when calculating the payment, this must be based on the difference between the previous and new pay scales, the assumption must be that the benefits achieved in accordance with the new pay scale are the same as for the previous pay scale. The Tribunal does not rule out that the basis for a pay scale may be changed to such an extent that this reasoning must be accepted. However, even though the reduction in work hours was not inconsiderable, the change is not greater than that an interpretation of the adjustment clause based on a natural linguistic understanding of this having to be decisive, without it being possible to include the type of reservation such as requirements that the basis for the pay scales has remained unchanged.

Section 36 of the Norwegian Contracts Act has been asserted. These grounds cannot be accepted. Firstly, a cost increase of 7.14% (if this is the actual cost increase for SSP) cannot in itself provide grounds for any revision of the agreement. The Tribunal makes reference to the fact that this is an agreement in a commercial arrangement. The Tribunal also finds that it does not have an accounting basis for being able to assess the relative effect the cost increase has had for, among other things, SSP's earnings from the agreement.

In the writ of summons, the plaintiff asserted that Statoil, whose position has been the deciding factor in Rasmussen's dismissal of the claim, is a member of "the relevant employer organisations". The Tribunal is in some doubt about what is behind this assertion. However, the Tribunal would note that it cannot see that the employer organisations have provided any statements that would indicate that the plaintiff's interpretation of the contract is correct. The employer organisations would also not be able to bind member company Statoil to a non-collective agreement such as the agreement between SSP and Rasmussen. It was asserted in the writ of summons that there would unlikely be any discussion of a rate adjustment if a "Gro day[1]" was introduced and that this supports the defendant's understanding of the contract. The Tribunal doubts whether the assertion has

[1] "Gro" refers to the former Norwegian Prime Minister Gro Harlem Brundtland. A "Gro day" is a commonly used expression to describe work days sandwiched between public holidays and weekends that many people take off (e.g. the Friday after Ascension Day).

been maintained, but will note that it does not assist in finding a solution to this dispute to speculate about the consequences of other forms of reductions in work hours. The Tribunal cannot see that any practice exists in connection with the introduction of a “Gro day” that would be of significance to the interpretation of the present agreement.

In accordance with this, the Tribunal finds that it must rule in favour of the defendant. It is not necessary for the Tribunal to address the loss SSP has suffered as a result of the reduction in work hours. It is also not necessary for the Tribunal to address the question of the dates from which compensation could have been claimed if there were grounds for increasing the payment.

With regard to costs and expenses to the Arbitral Tribunal, the following is noted:

The legal solution to the present dispute has included some doubt. The element that has principally created this doubt is the fact that, to a large extent, compensation appears to have been paid for the cost increases that the reduction in work hours entailed for the fulfilment of catering and housekeeping contracts. Among other things, this meant that it was reasonable that SSP wanted to have a legal examination of its claim.

In isolation, the doubt that has existed argues for applying the exemption provision in Section 172, paragraph two of the Norwegian Civil Procedure Act, to order each of the parties to cover their own costs. However, the Tribunal has found that, in addition to its own costs, the plaintiff must cover the costs for the defendant, as well as the expenses of the Arbitral Tribunal. The Tribunal has placed emphasis on the fact that in disputes between commercial parties, restraint should be exhibited when applying the exemption provision in Section 172, paragraph two of the Norwegian Civil Procedure Act. The clear starting point should be that when a party asserts a contractual interpretation that the Tribunal does not agree with, this party must bear the financial consequences of having commenced the dispute. The other party's costs are a natural part of this financial risk. The Tribunal has placed further emphasis on the fact that the present agreement was entered into as late as 17 March 1986, in other words on a date when it was a well-known fact that the labour organisations would demand that standard work hours be reduced in the collective wage agreement in 1986. In the view of the Tribunal, the plaintiff had particular reason to ensure that the contract stated that a reduction in work hours also provided grounds for adjusting the payment if this was SSP's pre-condition when entering into the agreement.

In accordance with this, the Arbitral Tribunal has found that the plaintiff must pay the defendant's costs, including the expenses of the arbitrator, expenses for writing etc. in connection with the arbitration award, and any other expenses for the Arbitral Tribunal.

The defendant submitted a statement of costs in the pleading of 14 September 1989. The statement of costs amounted to NOK 65,000. The defendant later submitted an additional pleading and the Court assumes that coverage of the costs of this pleading is also claimed. Based on this, costs for the defendant are set at NOK 67,000. Expenses for the Arbitral Tribunal, which thus must be covered by the plaintiff, are specified in a separate letter.

The arbitration award shall be sent to Oslo District Court for archiving, cf. Section 465, paragraph two of the Norwegian Civil Procedure Act. With regard to the selection of Oslo District Court and not Kristiansand District Court, reference is made to the fact that the parties agreed that the case shall be heard and decided in Oslo, cf. Section 36 of the Norwegian Civil Procedure Act.

Conclusion of ruling:

1. The Arbitral Tribunal finds in favour of K/S Rasmussen Offshore A/S.

2. SAS Service Partner Offshore and Industrial Catering A/S shall pay K/S Rasmussen Offshore A/S costs for the Arbitral Tribunal of NOK 67,000 within 2 weeks from the pronouncement of this arbitration award.

3. SAS Service Partner Offshore and Industrial Catering A/S shall pay the expenses for the Arbitral Tribunal in accordance with a separate statement.