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## Admiralty— The Package Doctrine of COGSA §4(5)— Second Circuit Abandons the “Functional Economics” Test

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# Admiralty– The Package Doctrine of COGSA §4(5)– Second Circuit Abandons the “Functional Economics” Test

Lisa Filloramo

## **Abstract**

In *Mitsui & Co. v. American Export Lines, Inc.*, the Court of Appeals for the Second Circuit rejected the “functional economics” test which it had developed in an earlier case as a standard for interpreting section 4(5) of the Carriage of Goods by Sea Act (COGSA). Part One of this Recent Development will discuss the historical development of the problem of carrier liability. Part Two will examine the case law as it has evolved in the Second Circuit since the late 1960’s. Part Three will then analyze the Mitsui decision and the impact it has had on the law in this area.

## RECENT DEVELOPMENTS

ADMIRALTY—THE PACKAGE DOCTRINE OF COGSA § 4(5)—SECOND CIRCUIT ABANDONS THE “FUNCTIONAL ECONOMICS” TEST—*Mitsui & Co. v. American Export Lines, Inc.*, Nos. 80-7095/7085 (2d Cir. Jan. 16, 1981).

In *Mitsui & Co. v. American Export Lines, Inc.*<sup>1</sup> the Court of Appeals for the Second Circuit<sup>2</sup> rejected the “functional economics” test which it had developed in an earlier case<sup>3</sup> as a standard for interpreting section 4(5) of the Carriage of Goods by Sea Act (COGSA).<sup>4</sup> That section provides in pertinent part:

Neither the carrier nor the ship shall in any event be or become liable for any loss or damage to or in connection with the transportation of goods in an amount exceeding \$500 per package lawful money of the United States, or in case of goods not shipped in packages, per customary freight unit . . . unless the nature and value of such goods have been declared by the shipper before shipment and inserted in the bill of lading.<sup>5</sup>

Since the passage of the act in 1936,<sup>6</sup> there has been heated debate as to the precise definition of a “package” for purposes of this section.<sup>7</sup> This debate reached a new intensity with the advent of containerization in the 1960's.<sup>8</sup> With carriers now providing

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1. Nos. 80-7095/7085, slip op. at 1093 (2d Cir. Jan. 16, 1981).

2. The case was heard before Chief Judge Feinberg, Circuit Judge Oakes, and Circuit Judge Friendly, who delivered the opinion of the court. *Id.* at 1066-67.

3. *Royal Typewriter Co. v. M/V Kulmerland*, 483 F.2d 645 (2d Cir. 1973). The functional economics test was so named because of the emphasis it placed on the functional character of export packaging in determining carrier liability. See notes 52-56 *infra* and accompanying text.

4. 46 U.S.C. § 1304(5) (1976).

5. *Id.*

6. Carriage of Goods by Sea Act, Pub. L. No. 521, ch. 229, 49 Stat. 1207 (1936).

7. For examples of early cases on this point, see *Gulf Italia Co. v. American Export Lines, Inc.*, 263 F.2d 135 (2d Cir.), *cert. denied*, 360 U.S. 902 (1959) (partially wrapped but not fully enclosed tractor is not a package); *Mitsubishi Int'l Corp. v. S.S. Palmetto State*, 311 F.2d 382 (2d Cir. 1962), *cert. denied*, 373 U.S. 922 (1963) (three fully enclosed rolls of steel are a package).

8. Containerization became popular in the 1960's as an economic means of shipping cargo. It allows shippers to load their goods directly at their plants into reusable metal containers. The most common size of these containers is 40 feet by 8

large reusable containers which the shippers could load themselves at inland points, the courts had to determine whether the container or some unit within the container as loaded was the "package" for determining liability.<sup>9</sup> As might have been expected, the definitions arrived at were numerous and varied.<sup>10</sup> The functional economics test developed by the Second Circuit became the touchstone of discussion on the issue, both in those courts which accepted it and in those which refused to follow it. The criticism engendered by the test<sup>11</sup> and its inconsistency with prior law<sup>12</sup> have finally brought the Second Circuit to reconsider the problems raised by containerization. Recognizing the inadequacy of the functional economics test, the court has now adopted a far more pragmatic approach.

Part One of this Recent Development will discuss the historical development of the problem of carrier liability. Part Two will examine the case law as it has evolved in the Second Circuit since

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feet by 8 feet. The goods are then transported in the container to the ship, where they can be stowed more efficiently for passage. G. GILMORE & C. BLACK, *THE LAW OF ADMIRALTY* 14 (2d ed. 1975); Bissell, *The Operational Realities of Containerization and Their Effect on the "Package" Limitation and the "On-Deck" Prohibition: Review and Suggestions*, 45 *TUL. L. REV.* 902 (1971); Calamari, *The Container Revolution and the \$500 Package Limitation—Conflicting Approaches and Unrealistic Solutions: A Proposed Alternative*, 51 *ST. JOHN'S L. REV.* 687, 688 n.4 (1977).

9. COGSA does provide that the liability of the carrier may exceed \$500 per package when the shipper declares a higher value for the goods. See note 5 *supra* and accompanying text. The shipper might then have to pay a higher freight charge to compensate for the increased cost of liability insurance of the carrier. Although the carrier may argue that a shipper who fails to declare a higher value in the bill of lading should be estopped from making this claim after the loss has occurred, this argument merely begs the question of how the shipper could have assessed the potential liability of the carrier prior to shipment. The shipper must first be able to determine what will be considered a package under the act before he is able to decide whether it is necessary to declare a higher value for the cargo. See *Standard Electrica, S.A. v. Hamburg Sudamerikanische Dampfschiffahrts-Gesellschaft*, 375 F.2d 943, 948 (2d Cir. 1967) (Feinberg, J., dissenting).

10. See Bissell, *supra* note 8, at 905-06; De Orchis, *The Container and the Package Limitation—The Search for Predictability*, 5 *J. MAR. L. & COM.* 251 (1974); Simon, *The Law of Shipping Containers*, 5 *J. MAR. L. & COM.* 507, 515-17 (1974); van Wageningen, *Interpreting COGSA: The Meaning of "Package"*, 30 *U. MIAMI L. REV.* 169 (1975).

11. See, e.g., Simon, *supra* note 10, at 520-30; Simon, *More on the Law of Shipping Containers*, 6 *J. MAR. L. & COM.* 603, 611-18 (1975); Note, *Containers and the Problem of Interpretation Under COGSA Section 4(5)*, 35 *WASH. & LEE L. REV.* 301, 307-08 (1978) [hereinafter cited as *Problem of Interpretation*].

12. See text accompanying notes 100-05 *infra*.

the late 1960's. Part Three will then analyze the *Mitsui* decision and the impact it has had on the law in this area.

### I. THE PROBLEMS AT COMMON LAW AND THE STATUTORY SOLUTIONS

At common law, the extent to which a carrier could be held liable for loss or damage to cargo steadily decreased as the shipping industry grew. Under general maritime law, carrier liability was almost absolute.<sup>13</sup> During the nineteenth century, the burden of loss shifted to the point where carriers could contract away almost all their liability in the bill of lading.<sup>14</sup> This change was possible because of the serious inequality in bargaining position between the carrier and the shipper.<sup>15</sup>

COGSA was not the first statutory solution to the problem of carrier liability. In 1893, Congress attempted to strike a compromise between the interests of the shippers and carriers in the Harter Act.<sup>16</sup> Sections 1 and 2 of the act favor the shipper by forbidding certain stipulations from being asserted into the bill of lading, such as exemptions from liability for carrier negligence,<sup>17</sup> failure to use due care with respect to the cargo,<sup>18</sup> or failure to use due diligence in furnishing a seaworthy vessel.<sup>19</sup> Section 3 acts as a balance to these prohibitions by limiting carrier liability for errors of navigation, dangers of the sea, and acts of God.<sup>20</sup> In 1921, this compromise became incorporated into the Hague Rules,<sup>21</sup> the

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13. G. GILMORE & C. BLACK, *supra* note 8, at 139-40. Even when liability was virtually absolute, there were exceptions which absolved the carrier of responsibility if the loss was caused by an act of God or public enemy, the inherent vice of the goods, or the fault of the shipper.

14. *Id.* at 142. With the introduction of the bill of lading (the contract between the carrier and the shipper), carriers began inserting many more exemptions from liability into the contract. The list of exceptions became long and fairly standardized. *Id.* at 140. See *Legislative Note*, 23 VA. L. REV. 590, 595 (1937).

15. See *Recupero, The Shipper's Right to Recover Under COGSA for Damage to Containerized Cargo*, 15 B.C. INDUS. & COM. L. REV. 51, 52 (1973).

16. 46 U.S.C. §§ 190-196 (1976).

17. *Id.* § 190.

18. *Id.*

19. *Id.* § 191.

20. *Id.* § 192.

21. 51 Stat. 233 (1924). The Hague Rules were promulgated to provide some uniformity in the law governing international carriage of goods by sea. They provide in part:

Neither the carrier nor the ship shall in any event be or become liable for any loss or damage to or in connection with goods in an amount exceeding

leading international agreement in this area. The Hague Rules in turn became the basis for COGSA.<sup>22</sup>

COGSA was enacted to give primacy in domestic law to the United States' adherence to the Hague Rules.<sup>23</sup> Although the legis-

100 pounds sterling per package or unit or the equivalent of that sum in other currency unless the nature and value of such goods have been declared by the shipper before shipment and inserted in the bill of lading.

*Id.* at 252. These Rules were first drafted as clauses which could be voluntarily inserted into bills of lading. In 1924, they took the form of a convention, to which the United States adhered subject to a number of reservations. G. GILMORE & C. BLACK, *supra* note 8, at 143-44. The convention was ratified by 12 nations and adhered to by 30 others, making it one of the most widely ratified private law conventions.

The Hague Rules were revised by the 1968 Protocol adopted in Brussels, also known as the Visby Amendments. Protocol to Amend the International Convention for the Unification of Certain Rules of Law Relating to Bills of Lading, Feb. 23, 1968, 1 TRANSPORT LAWS OF THE WORLD, I/E/15 (1977). The section which deals with the package limitation now provides: "Where a container, pallet or similar article of transport is used to consolidate goods, the number of packages or units enumerated in the Bill of Lading as packed in such article of Transport shall be deemed the number of packages or units for the purpose of this paragraph." *Id.* at 4. The Protocol came into force in 1977. There are now 15 nations party to it. The United States has not ratified the Protocol, and Professors Gilmore and Black note that since ratification has been slow, one should proceed for now on the assumption that COGSA will continue to be the law. G. GILMORE & C. BLACK, *supra* note 8, at 144. For an extensive discussion of the container clause as it appears in the Protocol, see DeGurse, *The "Container Clause" in Article 4(5) of the 1968 Protocol to the Hague Rules*, 2 J. MAR. L. & COM. 131 (1970).

The most recent international formulation on the issue is found in the 1978 Convention on the Carriage of Goods by Sea, commonly known as the Hamburg Rules. U.N. Doc. A/CONF. 89/13 (1978). The United States is signatory to the Hamburg Rules along with 25 other nations, but has not ratified the Rules. For a discussion of the changes and solutions provided by the Rules, see THE HAMBURG RULES ON THE CARRIAGE OF GOODS BY SEA (S. Mankabady ed. 1978).

22. The language of the Hague Rules and COGSA are very similar. Compare note 21 *supra* with text accompanying note 5 *supra*. There is, however, one important difference between the two:

[T]he Hague Rules limit carrier liability to \$500 per package or unit, in contrast to COGSA's per package or customary freight unit limitation. Under the Hague Rules, it apparently makes little difference whether an item is considered a package or an unpackaged unit since the terms have been construed to have essentially the same meaning. Conversely, under COGSA there is a significant difference between a package and a customary freight unit.

Calamari, *supra* note 8, at 691 (footnotes omitted).

23. See 79 CONG. REC. 13,340-41 (1935) (remarks of Sen. White). An Understanding to the ratification of the Hague Rules provides that where COGSA and the Hague Rules conflict, COGSA will prevail. Second Understanding to the United States' Ratification of the Hague Rules, May 6, 1937, reprinted in A. KNAUTH, THE AMERICAN LAW OF OCEAN BILLS OF LADING 77 (4th ed. 1953).

lative history is unclear,<sup>24</sup> it would appear that sponsors of COGSA were again trying to effect some kind of compromise between the interests of the carrier and shipper. This is evidenced by the setting of the \$500 package limitation. As a minimum liability which cannot be contracted away,<sup>25</sup> it ensures that shippers will be at least partially compensated for the loss of their cargo. The same \$500 amount also acts as a ceiling which limits the carrier's potential liability.<sup>26</sup>

Today, COGSA governs the export and import of goods in foreign trade,<sup>27</sup> but the Harter Act remains in effect with respect to domestic shipping,<sup>28</sup> with the stipulation that a bill of lading for domestic transport may by its terms bring itself within the provisions of COGSA.<sup>29</sup> The most important difference between the two is the absence of a provision in the Harter Act regarding a package limitation on liability.<sup>30</sup> In addition, COGSA allows for greater freedom of contract to the extent that carrier liability may be increased, but not decreased, by agreement of the parties.<sup>31</sup>

## II. THE FUNCTIONAL ECONOMICS TEST OF THE SECOND CIRCUIT

### A. *The Evolution of the Test*

As previously noted, the functional economics test was only one solution of many which emerged from the courts in response to the container revolution.<sup>32</sup> In fact, it was not the first interpretation to be proffered by the Second Circuit. Prior to *Mitsui*, the court had already decided a line of cases which were reconcilable only on very tenuous grounds.

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24. Differing interpretations have been offered as to the congressional intent behind COGSA. See, e.g., *Mitsui & Co. v. American Export Lines, Inc.*, Nos. 80-7095/7085, slip op. at 1077-78; *Leather's Best, Inc. v. S.S. Mormaclynx*, 451 F.2d 800, 815 (2d Cir. 1971); *Problem of Interpretation*, supra note 11, at 303-04 & n.16.

25. 46 U.S.C. § 1304(5) (1976).

26. See *id.*

27. 46 U.S.C. § 1300 (1976). The status of COGSA is subject to whatever revisions may be ratified by the United States in the future under the 1968 Protocol and the Hamburg Rules. See note 21 *supra*.

28. G. GILMORE & C. BLACK, supra note 8, at 147.

29. 46 U.S.C. § 1312 (1976); see Edelman, *Cargo Claims, Limitation of Liability on a Container*, N.Y.L.J., June 5, 1980, at 1, col. 1.

30. 46 U.S.C. §§ 190-196 (1976). See also Calamari, supra note 8, at 690.

31. G. GILMORE & C. BLACK, supra note 8, at 145.

32. See notes 67-74 *infra* and accompanying text.

The first of these cases was *Standard Electrica, S.A. v. Hamburg Sudamerikanische Dampfschiffahrts-Gesellschaft*.<sup>33</sup> Although the case involved palletized<sup>34</sup> rather than containerized cargo, it is still instructive in terms of the criteria used by the court in determining the meaning of "package" in light of technological changes in the shipping industry. Holding the pallets, rather than the individual cartons which they supported, to be the COGSA package,<sup>35</sup> the court seemed particularly concerned with the intent of the parties as evidenced in the shipping documents<sup>36</sup> and the fact that the shipper had himself chosen to utilize the pallets.<sup>37</sup> In a strong dissent, Judge Feinberg criticized the majority opinion as having disregarded the intent of Congress in enacting section 4(5), which he felt should be construed in close cases such as this so as to protect the cargo interest as against the carrier.<sup>38</sup> Subsequently, other members of the court were willing to express their concurrence with the *Standard Electrica* majority rationale.<sup>39</sup>

Within the next four years, the court's position changed dras-

33. 375 F.2d 943 (2d Cir. 1967).

34. Six cartons, each containing forty television tuners, were stacked on a wooden platform or pallet in three tiers. A second wooden deck was placed on top of the cartons, and everything was held together by metal straps. *Id.* at 944.

35. *Id.*

36. The shipping documents referred to a quantity of nine, indicating the nine pallets on which the cartons were stacked. No further description of the contents was given. *Id.* at 946.

37. *Id.*

38. *Id.* at 947 (Feinberg, J., dissenting). Judge Feinberg also addressed and disposed of the major arguments advanced by the majority. First, he said that the intent of the parties was at best ambiguous, and not as clear-cut as the majority's reference to the shipping documents alone suggested. *Id.* at 948. Second, he found the majority's point that it was in fact the shipper who chose to palletize the cargo to be irrelevant. *Id.* Third, he noted that the opportunity to declare a higher value simply begged the question of how to define "package" for purposes of § 4(5). *Id.* See also note 9 *supra*.

39. Of particular interest has been Judge Hays' dissenting opinion in *Encyclopedia Britannica, Inc. v. S.S. Hong Kong Producer*, 422 F.2d 7, 19-20 (2d Cir. 1969) (Hays, J., dissenting). Although the majority in that case did not consider the question of the package limitation, Judge Hays dissented to show his support for the *Standard Electrica* view that the container could in fact be the COGSA package. There was, however, a distinction between *Standard Electrica* and *Encyclopedia Britannica* which Judge Hays did not consider. While the shipping documents in *Standard Electrica* described only nine pallets with no further explanation of their contents, the bill of lading in *Encyclopedia Britannica* described "one container s.t.c. [said to contain] 536 cartons of bound books." This distinction could be crucial under the approaches adopted in later cases. See notes 45, 103 *infra* and accompanying text.

tically. In *Leather's Best, Inc. v. S.S. Mormaclynx*,<sup>40</sup> the court held that a provision in the bill of lading limiting the carrier's liability to \$500 with respect to the contents of each container<sup>41</sup> was invalid under COGSA.<sup>42</sup> The bill of lading described the goods as "1 container s.t.c. [said to contain] 99 bales of leather."<sup>43</sup> Although *Standard Electrica* was distinguished on its facts,<sup>44</sup> the court espoused a new rationale which threw the entire *Standard Electrica* reasoning into doubt. Returning to the importance of congressional intent, Judge Friendly stated:

Still we cannot escape the belief that the purpose of § 4(5) of COGSA was to set a reasonable figure below which the carrier should not be permitted to limit his liability and that "package" is thus more sensibly related to the unit in which the shipper packed the goods and described them than to a large metal object, functionally a part of the ship, in which the carrier caused them to be "contained."<sup>45</sup>

At the very least, the *Leather's Best* holding would seem to say that if goods are shipped in what would ordinarily be considered a package, within a container furnished by the carrier, and the number of such packages is disclosed in the bill of lading, then those packages, rather than the container, would be the COGSA package.<sup>46</sup> Admittedly, these criteria might not have changed the result in *Standard Electrica*, primarily because the contents of the pallets in that case were not disclosed in the bill of lading.<sup>47</sup> This question, however, was left open by the *Leather's Best* court. Of primary importance was the new emphasis on the common, ordinary meaning of the word "package," and the sense of sympathy for the shipper evident in the court's interpretation of COGSA and the legislative intent behind the act.

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40. 451 F.2d 800 (2d Cir. 1971).

41. *Id.* at 804.

42. *Id.* at 816.

43. *Id.* at 804.

44. *Id.* at 815. *Standard Electrica* involved pallets instead of containers, admittedly a somewhat different proposition. Also, the pallets in *Standard Electrica* had been made up by the shipper and the shipping documents seemed to indicate that the parties regarded the pallets to be the packages. *Id.*

45. *Id.* at 815 (footnote omitted) (emphasis added). The Supreme Court, in a longshoreman's personal injury case, has characterized a container as "a modern substitute for the hold of the vessel." *Northeast Marine Terminal Co. v. Caputo*, 432 U.S. 249, 270 (1977).

46. 451 F.2d at 804, 815-16.

47. 375 F.2d at 946; see note 44 *supra*.

The holding in *Leather's Best* was reinterpreted by the Second Circuit in *Royal Typewriter Co. v. M/V Kulmerland*<sup>48</sup> so that it would comport with the new standard being enunciated in that case, the functional economics test.<sup>49</sup> In *Kulmerland* the court was faced with the situation which *Leather's Best* had left open, specifically, the case in which the shipper furnished the container and failed to disclose the contents to the carrier.<sup>50</sup> In an attempt to achieve uniformity in these decisions, the test of functional packaging was created as a " 'common sense test' under which all parties concerned can allocate responsibility for loss at the time of contract, purchase additional insurance if necessary, and thus 'avoid the pains of litigation.' "<sup>51</sup>

The functional economics test allocates the burden of proof between carrier and shipper for showing whether the container or the individual units within the container are the COGSA packages.<sup>52</sup> The primary consideration is the actual packaging of the goods as it affects their suitability for breakbulk shipment.<sup>53</sup> If the goods could have been shipped in the individual cartons in which the shipper packed them, then the presumption arises that the carton is the package, and the burden of proof is on the carrier to show that the parties intended otherwise.<sup>54</sup> Conversely, if the actual packaging would not be suitable for breakbulk shipment, then the presumption is that the container is the package, and this presumption must be rebutted by the shipper with evidence that the parties actually intended the cartons to be the COGSA package.<sup>55</sup> Factors such as trade usage, custom, and characterization of the cargo in this shipping documents are only relevant in rebutting the presumption which is created by law.<sup>56</sup>

Using this test the court found that the goods in question could not have been shipped as they were packaged, and therefore

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48. 483 F.2d 645 (2d Cir. 1973).

49. *Id.* at 648. The test was later applied and explicated in *Cameco, Inc. v. S.S. American Legion*, 514 F.2d 1291 (2d Cir. 1974).

50. 483 F.2d at 646.

51. *Id.* at 649 (quoting *Standard Electrica*, 375 F.2d at 945).

52. *Id.* at 649; *Cameco, Inc. v. S.S. American Legion*, 514 F.2d at 1298.

53. 483 F.2d at 648. Breakbulk refers to the method of shipping whereby individual barrels, boxes, bales, bags, cartons, and drums are stowed in the hold of the vessel, as opposed to being placed in containers. *Calamari, supra* note 8, at 692 n.24.

54. 483 F.2d at 649.

55. *Id.*

56. *Calamari, supra* note 8, at 703.

the container was the package unless the shipper could prove that the parties intended otherwise.<sup>57</sup> The court went on to say that the underlying concept in *Leather's Best* was that the bales of leather could have been shipped breakbulk as they were packaged, and therefore constituted the COGSA package.<sup>58</sup> In fact, the court found the entire functional economics test to be implicit in the holding of *Leather's Best*.<sup>59</sup>

### B. Criticism of the Functional Economics Test

The functional economics test has brought severe criticism from courts<sup>60</sup> and commentators alike.<sup>61</sup> The *Mitsui* court itself provides a comprehensive analysis of the test's weaknesses.<sup>62</sup> First, there is the issue of economic waste. The functional economics test requires the shipper to go to the unnecessary expense of packaging his goods for overseas shipment, even though they will be stored in a container, in order to hold the carrier liable for \$500 per unit.<sup>63</sup> Second, there is the issue of uncertainty. The shipper has little basis for predicting whether his packaging will in fact pass the *Kulmerland* test.<sup>64</sup> Similarly, if the shipper has loaded the container at an inland point, the carrier cannot know what type of packaging has been used and consequently cannot assess his potential liability.<sup>65</sup> This prevalent uncertainty makes it impossible for both the carrier and shipper to make informed decisions regarding the purchase of additional insurance.<sup>66</sup>

One decision which has received a great deal of attention for its criticism of the functional economics test is *Matsushita Electric Corp. v. S.S. Aegis Spirit*,<sup>67</sup> decided in the Western District of Washington. Written by Judge Beeks, "an experienced admiralty

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57. 483 F.2d at 649.

58. *Id.*

59. *Id.*

60. For a discussion of the cases prior to *Mitsui* which were critical of the functional economics test, see notes 67-74 *infra* and accompanying text.

61. See note 11 *supra*.

62. Nos. 80-7095/7085, slip op. at 1088.

63. See Simon, *supra* note 10, at 523.

64. See Nos. 80-7095/7085, slip op. at 1088; *Problem of Interpretation*, *supra* note 11, at 307.

65. See Nos. 80-7095/7085, slip op. at 1088; *Problem of Interpretation*, *supra* note 11, at 308.

66. The problem is analogous to that of the shipper predicting the necessity of declaring a higher value in the bill of lading. See note 9 *supra*.

67. 414 F. Supp. 894 (W.D. Wash. 1976).

lawyer before his appointment to the bench,"<sup>68</sup> *Matsushita* is the only law on the subject to date within the important Ninth Circuit.<sup>69</sup> Judge Beeks focused his attention on the intent of Congress in enacting COGSA.<sup>70</sup> He noted that the only distinction made in the statute is between those goods which are shipped in packages and those which are not. The line between goods shipped in sturdy packaging and those shipped in lesser packaging is one which is simply not drawn under the act.<sup>71</sup> Furthermore, overemphasizing the intent of the parties makes the intent of Congress in establishing a minimum liability "illusory and negotiable."<sup>72</sup> In other words, if the parties are allowed to change the plain meaning of the word "package" as it is used in the statute, then the \$500 limitation becomes meaningless.<sup>73</sup>

Other courts have followed *Matsushita*, advanced their own criticism, and proposed their own solutions.<sup>74</sup> As the *Mitsui* court

68. Nos. 80-7095/7085, slip op. at 1089.

69. The Ninth Circuit, like the Second Circuit, is important in the area of admiralty law because it has jurisdiction over large coastal areas. Although *Matsushita* was a case of first impression within the Ninth Circuit, it is worth noting the remarks made by the Ninth Circuit Court of Appeals in *Hartford Fire Ins. Co. v. Pacific Far East Lines, Inc.*, 491 F.2d 960 (9th Cir. 1974), which appear to support a *Leather's* best type of reasoning. See the discussion in *Matsushita*, 414 F. Supp. at 903.

70. 414 F. Supp. at 904.

71. *Id.*

72. *Id.* at 905.

73. *Id.* It should be noted that victims of adhesion contracts have by definition not been able to express an intent. Simon, *supra* note 11, at 615.

74. See, e.g., *Yeramex Int'l v. S.S. Tendo*, 55 A.M.C. 1807 (E.D. Va. 1977), *rev'd*, 595 F.2d 943 (4th Cir. 1979); *Commonwealth Petrochemicals, Inc. v. S.S. Puerto Rico*, 455 F. Supp. 310 (D. Md. 1978), *rev'd*, 607 F.2d 322 (4th Cir. 1979). An example of how complex the solutions can become is provided by *In re Norfolk, Baltimore and Carolina Line, Inc.*, 478 F. Supp. 383 (E.D. Va. 1979) where the court expounded twelve criteria for determining what constitutes the COGSA package:

(1) Whether the carrier actually possesses superior bargaining strength sufficient to coerce the shipper's agreement to adhesion contract; (2) Whether the parties treated the container as a single unit in their negotiations, on the documents of contract, and in determining the shipping rate; (3) Whether the shipper, or at least one other than the carrier, chose to ship the goods in container; (4) Whether the shipper or carrier procured the container; (5) Whether the goods were delivered to the carrier previously loaded into the container; (6) Whether the goods were loaded by the shipper or by the carrier; (7) Whether the carrier actually observed the contents of the container before it was sealed for shipment; (8) Whether the container was loaded with the shipper's goods only, and not those of any other shipper; (9) Whether the markings on the containers provided a complete and accurate indication of the contents and their value; (10) Whether the bill of lading contained any declaration of the nature of the container's contents and their

noted, these decisions "indicate that the likelihood of general acceptance of the functional economics test is small."<sup>75</sup> The district court in *Matsushita*, faced with the dichotomy created by the Second Circuit in the *Standard Electrical/Leather's Best* line of cases, noted that "[o]ne might well conclude that the Second Circuit is still in the process of refining an appropriate legal standard to resolve the limitation question."<sup>76</sup> The Second Circuit has grasped another opportunity to do just that in *Mitsui*.

### III. *MITSUI & CO. v. AMERICAN EXPORT LINES, INC.*

The *Mitsui* decision involved two plaintiffs, both of whom suffered loss of or damage to their cargo which was being carried by defendant American Export Lines (AEL) aboard the S.S. Red Jacket.<sup>77</sup> Plaintiffs Mitsui & Co. and Ataka & Co. (Mitsui) were consignees of 1834 tin ingots. Plaintiffs Armstrong Cork Canada, Ltd. and Armstrong Cork Co. (Armstrong) were the shippers of 1705 rolls of floor covering. On January 10, 1974, a storm caused a stow of 50 containers to collapse, sending 43 containers overboard and damaging the rest.<sup>78</sup> American Export Lines was found to be liable for the loss in an earlier case,<sup>79</sup> and all that remained in *Mitsui* was the settlement of these two damage claims.

The tin ingots had been piled into 124 stacks and shipped in five containers.<sup>80</sup> The stacks were referred to as bundles and were designated as such in the bills of lading.<sup>81</sup> The ingots were not strapped together or secured into these bundles in any way.<sup>82</sup> AEL claimed that the ingots were shipped in five packages, referring to the five containers in which the ingots were stowed, which would

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value; (11) Whether the bill of lading provided the shipper with an adequate opportunity to declare the value of the container and its contents, and to obtain financial protection for any excess value; (12) Whether the shipper took advantage of this opportunity.

*Id.* at 392.

75. Nos. 80-7095/7085, slip op. at 1089.

76. 414 F. Supp. at 903.

77. Nos. 80-7095/7085, slip op. at 1068-69.

78. *Id.*

79. *Houldew & Co. v. S.S. Red Jacket*, 55 A.M.C. 1382 (S.D.N.Y. 1977), *aff'd by order*, 582 F.2d 1271 (2d Cir. 1978), *cert. denied sub nom.* Am. Export Lines, Inc. v. Metal Traders, Inc., 439 U.S. 1128 (1979).

80. Nos. 80-7095/7085, slip op. at 1069.

81. *Id.* at 1072.

82. *Id.* at 1070-71.

limit its liability to \$2500.<sup>83</sup> Mitsui, on the other hand, claimed that the ingots were not shipped in packages at all, and that the carrier's liability was therefore \$500 per ingot under a clause in the bill of lading which fixed liability at \$500 per package *or* per shipping unit.<sup>84</sup>

The floor covering rolls were wrapped by the shipper, who had inserted fibre discs at the top and bottom to protect the rolls, and wrapped the bottom in burlap to hold the discs in place.<sup>85</sup> The bills of lading described a specific number of rolls said to be contained within the carrier's thirteen containers.<sup>86</sup> AEL again contended that its liability was limited to \$500 per container, or \$6500. Armstrong considered each roll to be a package, and asked that liability be determined accordingly.<sup>87</sup>

Judge Motley in the district court applied the functional economics test to these facts.<sup>88</sup> She found that prior to containerization, ingots had been shipped in bundles, and each bundle was therefore the COGSA package. She disregarded the fact that the bundles were not strapped or tied, apparently because the stacking itself was useful in the loading process.<sup>89</sup> Both AEL and the Mitsui plaintiffs appealed. As to the Armstrong plaintiffs, each roll of floor covering was found to be a package. Since the figure of \$500 per roll exceeded the actual value of the goods, the actual value was awarded.<sup>90</sup> AEL appealed.

Writing for the Court of Appeals, Judge Friendly engaged in an extensive analysis of the law as it had developed in the Second Circuit, and considered at length the various lines of criticism which had evolved in response to the functional economics test of *Kumberland*.<sup>91</sup> Judge Friendly seemed to accept the *Standard Electrica* interpretation of congressional intent in COGSA when he wrote:

Although the legislative history of COGSA does not make clear why Congress created a ceiling on liability, the drafters of § 4(5)

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83. *Id.* at 1069.

84. *Id.*

85. *Id.* at 1073.

86. *Id.* at 1069, 1074.

87. *Id.* at 1069.

88. *Armstrong Cork Can., Ltd. v. S.S. Red Jacket*, 74 Civ. 2770, slip. op. at 4-5 (S.D.N.Y. Dec. 21, 1979).

89. *Id.* at 7, 9.

90. Nos. 80-7095/7085, slip op. at 1075.

91. *Id.* at 1088-93.

must have contemplated that a fixed limit on liability . . . would permit the parties to 'ascertain at the time of contract when additional coverage was needed, place the risk of additional loss upon one or the other, and thus avoid the pains of litigation.'<sup>92</sup>

In addition, Judge Friendly acknowledged that Congress probably had the superior bargaining position of the carrier in mind when it prohibited the reduction of liability below the \$500 limit.<sup>93</sup> In a later footnote, he pointed out that the result in *Kulmerland* was directly opposed to this two-fold rationale.<sup>94</sup> The total value of the adding machines in that case was \$29,000, yet recovery was limited to \$500 under the functional economics test, and would have remained so even if the bill of lading had disclosed the number of cartons and described the goods.<sup>95</sup> "This limitation would be reminiscent of the precise evil which . . . COGSA [was] designed to remedy."<sup>96</sup>

Although the criticism of *Kulmerland* was extensive and the congressional purpose had not been served by the functional economics test, the court did not base its decision in *Mitsui* on these considerations alone.<sup>97</sup> In fact, Judge Friendly was particularly careful to point out that the court would be bound by *Kulmerland*, in spite of all its difficulties, unless it proved to be inconsistent with previous case law.<sup>98</sup> Finding that *Kulmerland* was in fact inconsistent with the holding in *Leather's Best*, the court overruled *Kulmerland* and thereby abandoned the functional economics test.<sup>99</sup>

The *Kulmerland* court had claimed that the critical consideration under the functional economics test, *i.e.*, whether or not the goods were packaged for breakbulk shipment, was implicit in the *Leather's Best* holding.<sup>100</sup> Judge Friendly pointed out, however, that the question of whether or not the bales of leather could have been shipped breakbulk was never considered in *Leather's Best*. No evidence was introduced on the point, and the argument was never

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92. *Id.* at 1077-78 (quoting *Standard Electrica*, 375 F.2d at 945). See also note 51 *supra* and accompanying text.

93. Nos. 80-7095/7085, slip op. at 1078.

94. *Id.* at 1085 n.11.

95. *Id.*

96. *Id.*

97. See *id.* at 1085.

98. *Id.*

99. *Id.* at 1086. See generally *Simon*, *supra* note 10, at 527-29.

100. See 483 F.2d at 649.

advanced.<sup>101</sup> Not only was there no basis in fact for this primary assertion in *Kulmerland*, but the results in the two cases were found to be inconsistent as well.<sup>102</sup> Under *Leather's Best*, if the container is furnished by the carrier and the contents are disclosed, then the container is *not* the COGSA package.<sup>103</sup> Application of the functional economics test changes this result if the contents are not suitably packaged for export shipment.<sup>104</sup> The inconsistency is clear. In *Mitsui* the contents of a carrier furnished container were disclosed. The court found, therefore, that they "must apply the square holding of *Leather's Best* . . . and not the inconsistent test announced in *Kulmerland*."<sup>105</sup>

Where does this leave *Kulmerland*? The *Mitsui* court accepted the first part of the functional economics test, wherein packages suitable for breakbulk shipment are considered the COGSA packages.<sup>106</sup> The second part of the test, however, which presumes the container to be the package if the units within are not suitable for export shipment, did not stand.<sup>107</sup> The *Mitsui* court acknowledged that such a test may in fact show that the units are not packages, but it does not necessarily follow that the container is the package simply because the units are not.<sup>108</sup> What of the more likely conclusion, proposed by Judge Friendly, that the goods were *not shipped in packages at all*, in which case liability would be assessed at \$500 per customary freight unit (as opposed to per package) under the specific provision of 4(5)?<sup>109</sup>

With this far more pragmatic rationale in mind, the court proceeded upon the facts before it. With respect to the Armstrong plaintiffs, the court found each roll of floor covering to be a package within the plain, ordinary meaning of the word, noting that each had been wrapped sufficiently so as to conform to such meaning.<sup>110</sup> The issue of whether or not that wrapping was suitable for breakbulk shipment, which would have been decisive under the functional economics test, was found to be immaterial.<sup>111</sup>

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101. Nos. 80-7095/7085, slip op. at 1086.

102. *Id.*

103. *Id.*; see text accompanying notes 40-46 *supra*.

104. Nos. 80-7095/7085, slip op. at 1086.

105. *Id.*

106. *Id.* at 1086-87.

107. *Id.* at 1087.

108. *Id.*

109. *Id.*; see text accompanying note 5 *supra*.

110. Nos. 80-7095/7085, slip op. at 1094.

111. *Id.*

The affirmance in the case of the *Mitsui* plaintiffs was somewhat more involved. The court disagreed with Judge Motley's conclusion that each bundle was a package.<sup>112</sup> Whereas Judge Motley had considered the way in which ingots had been shipped breakbulk prior to containerization,<sup>113</sup> the Second Circuit considered the ordinary meaning of the word package and found that stacks of ingots which were not tied or held together in any way could not be considered a package.<sup>114</sup>

Applying its new reasoning, the court went on to say that although the bundles were not the packages, it did not necessarily follow that the container was the package, and in fact held that it was not.<sup>115</sup> The court made it clear that in the absence of extenuating circumstances, this case would be resolved by assessing liability at \$500 per customary freight unit, which would be the long ton.<sup>116</sup> Language was found in the bill of lading, however, which would have increased the carrier's liability to \$500 per ingot as opposed to \$500 per long ton.<sup>117</sup> Any increase in liability effected by agreement between the parties is expressly permitted under § 4(5).<sup>118</sup> The situation was further complicated by another clause in the bill of lading which prohibited any increase in the carrier's liability above that provided for in the act.<sup>119</sup> The court decided that the ambiguity thus created in the bill of lading should be resolved in favor of the shipper.<sup>120</sup> This should have meant that Mitsui would receive \$500 per ingot.<sup>121</sup> Instead, the court ultimately relied on other language in the bill of lading in which the shipper described the contents of the container as "bundles," even

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112. *Id.*

113. *Armstrong Cork Can., Ltd. v. S.S. Red Jacket*, 74 Civ. 2770, slip. op. at 5 (S.D.N.Y. Dec. 21, 1979).

114. Nos. 80-7095/7085, slip op. at 1094.

115. *Id.*

116. *Id.* at 1094-95.

117. The bill of lading provided that for those goods not shipped in packages, liability would be assessed at \$500 per shipping unit. The contract defined shipping unit as "each physical unit or piece of cargo not shipped in a package, including articles or things of any description whatsoever . . ." *Id.* at 1095-96. This would mean that if the ingots were not shipped in packages, each individual ingot would be considered a shipping unit, thereby increasing the carrier's liability to \$500 per ingot.

118. *Id.* at 1096. See also note 31 *supra* and accompanying text.

119. Nos. 80-7095/7085, slip op. at 1096.

120. *Id.*

121. *Id.* at 1097. Of course, the shipper will never receive more than his actual loss. 46 U.S.C. § 1304(5). Since Mitsui's actual loss was less than \$500 multiplied by 1,834 ingots, they would have received the former amount. Nos. 80-7095/7085, slip op. at 1097.

though the ingots were not by definition properly bundled.<sup>122</sup> Since the carrier had no way of knowing that such representation was false, liability was limited to \$500 per bundle, thereby affirming the district court.<sup>123</sup>

### CONCLUSION

Judge Oakes, who had written the majority opinion in the *Kulmerland* case, filed a separate concurring opinion in *Mitsui*. Conceding the difficulty of the problem involved, he concluded:

[J]udge Friendly's most perceptive opinion in this case, coupled with that of Judge Beeks in *Matsushita* . . . , referred to and quoted at length by Judge Friendly, have persuaded me that the "functional economics" test of *Kulmerland* does not function well and had better be abandoned. In the realm of container shipping, where the bill of lading specifies the contents, the ship's container should not be deemed a package—even presumptively only—irrespective of how the goods within it are packed. I therefore am joining in the abandonment of the *Kulmerland-Cameco* test, noting only that the results of neither case would be changed by virtue of today's decision.<sup>124</sup>

The *Mitsui* decision does not answer all the questions raised by the need to reinterpret COGSA's package limitation in light of technological changes in the shipping industry. For example, it is still not certain how a case such as *Standard Electrica*, where the contents of a shipper-furnished container are not disclosed to the carrier, might be decided today. It is certain, however, that a standard such as the functional economics test is not useful in passing upon these questions of liability. The more practical approach of *Leather's Best* and *Mitsui* should be employed in the interim until Congress decides to revise COGSA in accordance with the 1968 Visby Amendments or the 1978 Hamburg Rules.<sup>125</sup>

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122. Nos. 80-7095/7085, slip op. at 1097.

123. *Id.*

124. *Id.* at 1103 (Oakes, J., concurring) (citation omitted).

125. See note 21 *supra*.