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# Aspects of Ship Finance: The Market, Ship Mortgages and their Enforcement

*Professor Stephen Girvin\**

The ship finance market has, during the past decade, undergone profound changes. Compared with readily available ship finance in the boom years of the early noughties, the Global Financial Crisis (GFC) has seen many traditional ship finance banks exit the market. For those banks that have remained in shipping, there are now significantly tighter funding parameters, in line with the imposition of stricter controls over banks by the Basel Committee on Banking Supervision. Those seeking ship finance have, increasingly, had to rely on other sources of finance. Whatever the source of finance, the lender typically will want to secure that finance through the tried and trusted mechanism of a ship mortgage. Following an event of default on the mortgage, the lender may wish to enforce its rights by possession, sale, and arrest (followed by sale) of the ship. This paper analyses how these choices play out, particularly in the context of recent decisions of the English and Singapore courts.

Keywords: Ship finance; banks and other sources of funding; mortgages; mortgagees' remedies of possession, sale, and arrest; blockchain and ship finance

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## 1 Introduction

At the beginning of January 2018, the world commercial fleet comprised 94,171 ships, having a combined tonnage of 1.92 billion dwt.<sup>1</sup> Save for ships wholly financed by large public companies or wealthy private individuals,<sup>2</sup> a large proportion of this commercial fleet is financed by banks. For most bank lenders, the ship is the primary form of security, albeit a somewhat risky security,<sup>3</sup> as ships have a fluctuating and ultimately depreciating capital value, do not automatically generate income, and may incur heavy and inescapable running costs, whether operating or idle.<sup>4</sup>

The impact of economics on the financial portfolio of most shipping companies cannot be underestimated. The difficulties faced after the Global Financial Crisis (GFC) of 2008 should not, however, be viewed as a unique event affecting the shipping markets.<sup>5</sup> Nevertheless, the events which led to the failure of Lehmann Brothers in September 2008 underlined a number of significant issues affecting shipping, in particular an oversupply of ships, many of which were ordered during the preceding peak market. The imminent delivery of newly-built ships from shipyards, particularly in China and Korea, aggravated a growing imbalance between market demand and supply and led to the insolvency of a number of well-known shipping

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<sup>1</sup> *Review of Maritime Transport 2018* (UNCTAD) 23.

<sup>2</sup> Shipping still resonates with substantial empires built on the initiative of shipping magnates: see, eg, John Angelicoussis (Angelicoussis Shipping Group); John Frederiksen (Frederiksen Group); Rodolphe Saadé (CMA CGM); Diego Aponte (MSC); Eyal Ofer (Zodiac Maritime); George Propokiou (Dynacom/ Dynagas); Henning Oldendorff (Oldendorff Carriers); George Economou (DryShips); Teo Siong Seng (Pacific International Lines); Bertram Rickmers (Rickmers Group); Thomas Wilhelmsen (Wilhelmsen Group). See *Lloyd's List One Hundred* (8th edn, 2017) <<https://lloydslist.maritimeintelligence.informa.com/One-hundred-Edition-Eight/Digital-Edition>> accessed 19 July 2019.

<sup>3</sup> As many banks found out in the post-2007 credit crunch: see Nigel Lowry, "Broken" banking system leaves gap for new ship finance crowd', *Lloyd's List*, 9 March 2017.

<sup>4</sup> Alison Clarke, 'Ship Mortgages' in Norman Palmer and Ewan McKendrick (eds), *Interests in Goods* (2nd edn, LLP 1998) 663, 665.

<sup>5</sup> In recent history, the Arab-Israeli War of October 1973 and the oil embargo which followed it also created panic in the shipping and banking markets and that, in turn, led to significant problem loans, initially in the Norwegian banking market, which had underwritten substantial loans to tanker owners, and quickly spread throughout the market: see Peter Stokes, *Ship Finance: Credit Expansion and the Boom-Bust Cycle* (2nd edn, LLP 1997) chs 3, 4.

companies<sup>6</sup> and difficulties in the chartering markets, with charterers returning ships early<sup>7</sup> and, sometimes, late.<sup>8</sup> In November 2007, Clarksons<sup>9</sup> reported daily Capesize bulk carrier rates of US\$169,000<sup>10</sup> per day but by late 2008 this had dropped substantially to US\$20,000 per day.<sup>11</sup> At the time of writing, even the lowest rates available at the end of 2008<sup>12</sup> would now be considered eminently respectable.<sup>13</sup> Other shipping sectors have fared equally badly; for oil tankers, for example, the markets in 2018 were considered ‘horrific’<sup>14</sup> but the volatility of this sector of the market was also highlighted when a series of blasts occurred on the tankers, *Kokuka Courageous* and *Front Altair* in the Gulf of Oman in June 2019,<sup>15</sup> prompting significantly higher volumes in traded freight futures, the highest since 2014.<sup>16</sup>

The first part of this paper sets out some of the primary mechanisms by which ship finance is arranged. Such issues are rarely, if ever, considered in the standard legal texts but are an essential feature in the armoury of any knowledgeable ship finance lawyer.<sup>17</sup> The second part of this paper is concerned with some aspects of ship mortgage enforcement: what options

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<sup>6</sup> Notably, Hanjin Shipping Co Ltd. See, eg, Paul Slater, ‘Hanjin: Tip of the iceberg’ *Lloyd’s List* (London, 23 September 2016); Martin Davies, ‘Cross-Border insolvency and admiralty: A middle path of reciprocal comity’ (2018) 66 *AJCL* 101; M Tsimplis, ‘Modified universalism and cross border insolvency of shipping companies’ [2020] *JBL* (forthcoming). See also Xu Jingchen, ‘Maritime cross-border insolvency in China’, CML Law Working Paper Series 19/04 <<https://law.nus.edu.sg/cml/pdfs/wps/CML-WPS-1904.pdf>> accessed 19 August 2019.

<sup>7</sup> See, eg, *Golden Strait Corp v Nippon Yusen Kubishika Kaisha (The Golden Victory)* [2007] UKHL 12, [2007] 2 AC 353.

<sup>8</sup> See, eg, *Transfield Shipping Inc v Mercator Shipping Inc (The Achilles)* [2008] UKHL 48, [2009] 1 AC 61.

<sup>9</sup> See <<https://www.clarksons.com>> accessed 19 June 2019.

<sup>10</sup> Peter Illingworth, ‘Ship finance — the banker’s perspective’ in Julie Clegg and Jonathan Ward (eds), *Shipping Finance: A Practical Handbook* (4th edn, Globe Law and Business Ltd 2018) 17.

<sup>11</sup> See, eg, Jan-Henrik Hübner, ‘Shipping Markets and their Economic Drivers’ in Manolis G Kavussanos and Ilias D Visvikis, *The International Handbook of Shipping Finance* (Palgrave Macmillan 2016) 18.

<sup>12</sup> For a review of the rates 1945–2008, see Martin Stopford, *Maritime Economics* (3rd edn, Routledge 2009) 119.

<sup>13</sup> See, eg, Peter Sand, ‘Dry bulk shipping: Uncertainty mounts against a backdrop of weaker growth in Chinese imports’ <[https://www.bimco.org/news/market\\_analysis/2019/20190220\\_2019\\_01\\_drybulk\\_shipping](https://www.bimco.org/news/market_analysis/2019/20190220_2019_01_drybulk_shipping)> accessed 21 May 2019.

<sup>14</sup> *Ibid.*

<sup>15</sup> ‘Oil tankers “attacked” in Gulf of Oman’, *Lloyd’s List* (London, 13 June 2019); ‘Tanker attacks: Kokuka Courageous being towed to port’ *Lloyd’s List* (London, 14 June 2019).

<sup>16</sup> Michelle Wiese Bockmann, ‘“Monstrous” week for tanker freights pushes volumes to five-year high’, *Lloyd’s List* (London, 17 June 2019).

<sup>17</sup> This paper does not, however, set out to be a primer on ship finance. Detailed analysis may be found in the following texts, to which I am indebted: Clegg and Ward (n 10); Orestis Schinas, Carsten Grau and Max Johns (eds), *HSBA Handbook on Ship Finance* (Springer 2015); Stopford (n 12) ch 7; Kavussanos and Visvikis (n 11).

are available to a mortgagee bank when the shipowner (mortgagor) is in default?<sup>18</sup> It considers the underlying principles supporting the available mechanisms for enforcement and, in particular, recent cases on discrete areas of the law relating to ship mortgages. Finally, as a postscript, this paper considers how blockchain technology may (or may not) play a role in the ship finance market in the future.

## 2 Ship financing

### 2.1 Background

Over forty years ago, on 11 February 1975, the Liberian-flagged *Panglobal Friendship*,<sup>19</sup> a tanker, sank while on the course of a voyage from Curaçao to Trinidad. In the court proceedings that followed, Roskill LJ summarised the typical mechanism for securing finance over ships in the following way:<sup>20</sup>

For at least a quarter of a century, if not more, the method of obtaining finance for building ships (which was adopted in this case by finance obtained from ... Citibank) was widely adopted on both sides of the Atlantic. It may be summarised in these words. The bank advances to one or more owning companies a large sum of money. It of course requires security. It will take a mortgage on the ship for that security. It may take other mortgages on other ships for the same security. If the ship, as often happens, is about to be time chartered, then the bank will take an assignment of the time charter in order that the bank as assignee can benefit from the time charter in order to reduce the mortgage debt. In addition it will almost invariably in my experience take an assignment of insurance policies and P & I Club cover in order that in the event of total or partial loss of the ship the bank as the lender may be suitably secured. As a result, over the last quarter of a century when many ships similarly built and financed have been totally lost banks have found themselves completely

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<sup>18</sup> The standard work is David Osborne, Graeme Bowtle and Charles Buss, *The Law of Ship Mortgages* (2nd edn, Informa 2016). See, however, also Nigel Meeson and John A Kimbell, *Admiralty Jurisdiction and Practice* (5th edn, Informa 2018) ch 10.

<sup>19</sup> Built in 1967 at Smith's Dock Co in South Shields (IMO Number 6803272).

<sup>20</sup> The *Panglobal Friendship* was insured on the London market for S\$1.5m, the question for the Court of Appeal being whether Citibank, which had lent money on this and several other ships, was entitled to this money and whether the time charterers should be permitted to intervene in the proceedings.

protected in the events which have happened. The effect of all this is to ensure that the lending bank is completely secured against the insolvency of the borrower who intends that the bank shall obtain complete priority over the claims of other creditors against the borrower.<sup>21</sup>

Although much of what Roskill LJ said there is still true now, ship financing today is a world away from what it was then.<sup>22</sup> In the ship lending boom between 1967 and 1973,<sup>23</sup> mortgage-backed bank loans were the norm for the financing of newly-built ships, covering 70–75 per cent of the total capital invested; the new norm today, after the Global Financial Crisis (GFC),<sup>24</sup> is for bank debt to be around 50–60 per cent.<sup>25</sup> Indeed, a prominent feature of ship finance during the past decade has been the development of new finance structures and new sources of finance other than from banks, which has become increasingly sparse, for the reasons which are elaborated further below.

## 2.2 Bank finance

Bank finance has, for the longest time, been the principal source of finance for new ships,<sup>26</sup> with the ship as collateral, once delivered from the shipyard,<sup>27</sup> or bought and sold second-hand in the sale and purchase market, the latter considered to be ‘the bread and butter of a ship financier’s business’.<sup>28</sup> As individual banks may only advance a proportion of the required finance, loans may be syndicated among a group of banks, usually, in better times,<sup>29</sup> for a loan tenor between five and ten years<sup>30</sup> and with repayments in semi-annual or quarterly

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<sup>21</sup> *Citibank NA v Hobbs Savill & Co Ltd (The Panglobal Friendship)* [1978] 1 Lloyd’s Rep 368, 371.

<sup>22</sup> See Clarke (n 4) 665 fn 17.

<sup>23</sup> See Stokes (n 5) ch 2; Liana Miliotis, ‘All change ahead’ (2018) 32(1) MRI 16.

<sup>24</sup> This phrase typically refers to the period of extreme stress in global financial markets and banking systems between mid-2007 and early 2009. See, generally, Andrew Farlow, *Crash and Beyond: Causes and Consequences of the Global Financial Crisis* (Oxford University Press 2013) ch 4.

<sup>25</sup> F Giannakoulis, ‘Overview of ship finance’ in Kavussanos and Visvikis (n 11) ch 3; Illingworth (n 10) 33.

<sup>26</sup> See George Paleokrassas, ‘Debt financing in shipping’ in Kavussanos and Visvikis (n 11) ch 5.

<sup>27</sup> Financing prior to delivery cannot be mortgaged, there being no ship over which the mortgage can attach: see Charles R Cushing, ‘Shipbuilding finance’, in Kavussanos and Visvikis (n 11) 95; Giannakoulis (n 23) 80; Stopford (n 12) 29. For further, detailed, consideration, see Jonathan Ward and Danaö Hosek-Ugolini, ‘The financing of newbuildings’ in Schinas et al (n 17) 51.

<sup>28</sup> Dora Mace-Kokta and Danaö Hosek-Ugolini, ‘The financing of second-hand vessels’ in Clegg and Ward (n 10) 81.

<sup>29</sup> See Julian McQueen, ‘Syndicated loan market is dead’ *Lloyd’s List* (London, 21 June 2011). But cf ‘Deal go-ahead despite market’ (2008) 22(5) MRI 3.

<sup>30</sup> The latter period was described in 2012 as being like ‘winning the lottery’: see David Osler, ‘Landing a 10-year ship loan is “like winning the lottery”’ *Lloyd’s List* (London, 15 November 2012).

instalments, with a balloon payment<sup>31</sup> on maturity.<sup>32</sup> Ships may also be financed by more than one such loan, provided by a different lender, or group of lenders.<sup>33</sup> The terms of the proposed financing are usually set out in a term sheet,<sup>34</sup> such as BIMCO's SHIPTERM, developed in 2017 and intended for bilateral transactions between a single lender and one or more borrowers.<sup>35</sup>

Such finance used to be a major source of business for banks and, during the shipping boom in the noughties,<sup>36</sup> bank institutions lending to shipping had significant loan portfolios;<sup>37</sup> the estimated global shipping portfolio in 2010 was around US\$450 billion, but this fell to US\$355.25 billion in 2016 and to US\$345 billion in 2017.<sup>38</sup> Although viewed by banks as a favourable sector in which to do business, shipping has always been a volatile and cyclical business. The downturn in shipping exposed many banks heavily invested in shipping, particularly European banks,<sup>39</sup> to a toxic debt burden.

As a result the trend has been for many, especially European, banks<sup>40</sup> to reduce their exposure or, in a number of cases, to dispose entirely of their shipping loan portfolios.<sup>41</sup> One of the prime examples of the latter was Royal Bank of Scotland;<sup>42</sup> in the former, another UK-

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<sup>31</sup> ie a contractual payment of a specified amount added, usually, to the final instalment.

<sup>32</sup> For detailed terms, see Giannakoulis (n 25) 78; Kyriakos Spoullou, 'Key clauses of a shipping loan agreement' in Kavussanos and Visvikis (n 11) 213.

<sup>33</sup> Depending on the place of registration of the mortgage. Under English law and Singapore law, priority of the mortgagees is determined by the order in which the mortgages are registered: see, respectively, Merchant Shipping Act 1995, c 21, Sch 1, para 8(1); Merchant Shipping Act 1995, cap 179, s 28.

<sup>34</sup> See Illingworth (n 10) 11.

<sup>35</sup> See <<https://www.bimco.org/contracts-and-clauses/bimco-contracts/shipterm#>> accessed 19 June 2019.

<sup>36</sup> See particularly Hübner (n 11) 1, 13 for an overview of the different shipping market sectors and their performance.

<sup>37</sup> In 2007, for example, such loan portfolios ranged from \$1bn to \$20bn: *ibid*, 286.

<sup>38</sup> See 'Full steam ahead: Deleveraging report 2018 Q3' (Deloitte); 'Global Shipping Loan Portfolios' Drop to \$345 billion says Petrofin Bank Research' *Hellenic Shipping News* (Piraeus, 17 September 2018).

<sup>39</sup> In 2008, European banks held 90% of this risk, with German banks in the lead, with 45%, Scandinavian banks 20%, and British banks 11%: Giannakoulis (n 25) 75; Illingworth (n 10) 20.

<sup>40</sup> Not that difficulties have not been felt elsewhere, particularly Asia: see David Osler, 'Shipping downturn "has cost Asian banks hundreds of millions of dollars"' *Lloyd's List* (London, 10 September 2013).

<sup>41</sup> Lambros Papaeconomou, 'Inglorious end to a celebrated era by Royal Bank of Scotland', *Lloyd's List* (London, 21 September 2016). See also *Natwest Markets Plc (formerly known as the Royal Bank of Scotland plc) v Stallion Eight Shipping Co SA (The Alkyon)* (2 May 2019), below at text to n 256.

<sup>42</sup> Lambros Papaeconomou, 'Shipping commercial banks run for the door' *Lloyd's List* (London, 20 June 2017).

based bank, Lloyds Banking Group in 2012<sup>43</sup> disposed of US\$750 million from its US\$8 billion book to Oaktree Capital,<sup>44</sup> a private equity firm.<sup>45</sup>

German banks were particularly hard hit.<sup>46</sup> This was primarily because of the so-called 'KG'<sup>47</sup> market in shipping<sup>48</sup> which developed in a way which was to prove the undoing of many market-leading banks.<sup>49</sup> Commerzbank, formerly the world's number two ship finance bank, decided to exit shipping altogether in 2012<sup>50</sup> and by 2018 this had largely been achieved.<sup>51</sup> Nord/LB, another market leading bank, reduced its shipping portfolio in 2016 and aimed at further reductions, from €19 billion to €14 billion, in 2018<sup>52</sup> but these intentions were realised sooner, with a reduction to to €12.1 billion by early 2018 and a shift in focus from commercial shipping to ferries and cruises.<sup>53</sup> By the end of the first quarter of 2019, Nord/LB had reduced this loan book still further to \$5.5 billion, after a portfolio sale to the private equity investor, Cerberus Capital Management.<sup>54</sup> HSH Nordbank was particularly badly affected<sup>55</sup> and was eventually privatised in early 2018 by a sale to US-based equity firms, Cerberus and JC

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<sup>43</sup> Société Générale (SocGen) did this in 2011: see David Osler, 'Citibank takes \$2bn tranche of SocGen shipping book' *Lloyd's List* (London, 18 June 2012).

<sup>44</sup> See <<https://www.oaktreecapital.com/>> accessed 19 June 2019.

<sup>45</sup> David Osler, 'Other banks could follow Lloyds half-price ship loan sale' *Lloyd's List* (London, 1 October 2012). A further sale, to Davidson Kempner, took place in 2013: see David Osler, 'Davidson Kempner named buyer of Lloyds Bank shipping portfolio' *Lloyd's List* (London, 12 December 2013). Cf also Nigel Lowry, 'Piraeus Bank sells bad shipping loans to US fund' *Lloyd's List* (London, 11 June 2019).

<sup>46</sup> See B Barnard, 'Ship Finance on Life Support' *Journal of Commerce* (New York, 28 March 2013).

<sup>47</sup> Kommanditgesellschaft (Limited Liability Partnership).

<sup>48</sup> See Illingworth (n 10) 22; Stopford (n 12) 306. For detailed consideration, see Max Johns and Christoph Sturm, 'The German KG System' in Schinas et al (n 17), ch 4.

<sup>49</sup> See, eg, Patrick Hagen, 'KG model in crisis as ship values crash' *Lloyd's List* (London, 24 March 2009).

<sup>50</sup> Patrick Hagen, 'Commerzbank to exit ship financing' *Lloyd's List* (London, 27 June 2012); David Osler, 'Commerzbank accelerates its withdrawal from shipping' *Lloyd's List* (London, 13 February 2014); 'Commerzbank shipping book down to \$12.7bn as pullout continues' *Lloyd's List* (London, 12 March 2015).

<sup>51</sup> It confirmed in 2018 that the run-down had reached the point where its shipping book was down to 90% on its peak (\$1.2bn): James Baker, 'Commerzbank shipping book shrinks to €1bn' *Lloyd's List* (London, 7 August 2018).

<sup>52</sup> 'Nord/LB losses climb to \$2bn' *Lloyd's List* (London, 6 April 2017).

<sup>53</sup> Anastassios Adamopoulos, 'Nord/LB cuts shipping portfolio by \$5.8bn' *Lloyd's List* (London, 17 April 2018).

<sup>54</sup> See <<https://www.cerberus.com/>> accessed 18 May 2019. David Osler, 'NordLB to exit ship finance after "painful" losses' *Lloyd's List* (London, 4 April 2019); Anastassios Adamopoulos, 'NORD/LB sells \$2.9bn shipping loan portfolio' *Lloyd's List* (London, 10 April 2019).

<sup>55</sup> David Osler, 'HSH Nordbank to offload billions of dollars of toxic shipping debt' *Lloyd's List* (London, 20 October 2015); 'HSH Nordbank offloads \$5.6bn of bad shipping debt on taxpayers' *Lloyd's List* (London, 1 July 2016); 'HSH Nordbank writes off \$900m of shipping debt' *Lloyd's List* (London, 3 November 2016); 'HSH Nordbank to offload \$5bn toxic shipping debt at 60% discount' *Lloyd's List* (London, 1 May 2018).



Flowers, subsequently approved by the European Commission,<sup>56</sup> and now known as Hamburg Commercial Bank.<sup>57</sup> The meltdown continued with other banks, including Deutsche Bank<sup>58</sup> and DZ Bank, also experiencing difficulties.<sup>59</sup>

The availability of bank finance was not, by any means, the sole outcome of the GFC. There were also other factors at work, not the least of which was a significant oversupply of tonnage, significantly exacerbated by orders to shipyards which were ready for delivery and flooded an already oversupplied market.<sup>60</sup> The hiatus in the availability of finance from European-based banks, represented by a reduction in the European share of the global shipping book from 83 per cent to 62 per cent in the period between 2010 and 2015, has presented an opportunity for Asian-based banks, which have picked up some of the slack.<sup>61</sup> At the same time, not all European banks have left shipping altogether; some newer banks, such as Cyprus-based Hellenic Bank,<sup>62</sup> have entered the market.<sup>63</sup>

Notwithstanding the difficult conditions in the shipping sector, and the marked deceleration in the availability of bank debt finance, many continue to expect that bank debt will remain the industry's primary source of funding.<sup>64</sup>

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<sup>56</sup> See Anastassios Adamopoulos, 'HSH Nordbank sale gets EU approval' *Lloyd's List* (London, 26 November 2018). See also 'State aid: Commission approves aid-free privatisation of German HSH Nordbank', European Commission, IP/18/6561.

<sup>57</sup> See Grant Rowles, 'HSH Nordbank sale completed, becomes Hamburg Commercial Bank' *Splash 247* (Singapore, 29 November 2018). See also David Osler, 'Hamburg Commercial Bank still seeking industry deals, head of shipping insists' *Lloyd's List* (London, 21 May 2019) and <<https://www.hcobank.de/en/loesungen/shipping/shipping>> accessed 19 June 2019.

<sup>58</sup> See 'Deutsche Bank sells \$1bn ship loan portfolio' *Lloyd's List* (London, 18 June 2018); David Osler, 'Deutsche Bank makes further progress on 'derisking' shipping portfolio' *Lloyd's List* (London, 25 July 2018).

<sup>59</sup> Anastassios Adamopoulos, 'DZ Bank "considering all options" for DVB' *Lloyd's List* (London, 27 February 2018).

<sup>60</sup> See Richard Eglington, 'Turbulent waters for ship finance market' (2012) 26 MRI 10.

<sup>61</sup> See David Osler, 'Asian shipping banks move up top lenders league table' *Lloyd's List* (London, 2 December 2015).

<sup>62</sup> See <<https://www.hellenicbank.com>> accessed 19 August 2019.

<sup>63</sup> See Nigel Lowry, 'Hellenic Bank grows ship finance book with largest loan' *Lloyd's List* (London, 10 August 2018).

<sup>64</sup> Thus, 23% of responders thought so in a survey produced by the law firm, Norton Rose Fulbright in 2017: see *The Way Ahead: Transport Survey 2017*, downloadable from <<https://transportsurvey.nortonrosefulbright.online/publications/shipping>> accessed 10 July 2019.

## 2.3 Corporate loans

Apart from mortgage-backed loans, an aspect of bank finance available to large established companies is the corporate loan, typically unsecured and available to publicly-listed companies, such as (most) liner shipping companies, and giving the company a source of capital which is flexible.<sup>65</sup>

## 2.4 Capital markets

The capital markets are an accessible and attractive form of ship finance,<sup>66</sup> although only to larger shipping companies. This type of finance is typically available in two main forms, *public offers of shares*<sup>67</sup> and issues of *bonds*. Each of these is now considered.

A *listing or offer of shares* (equity) by a public company is not unique to shipping and can occur in any market sector. The difficulty, however, for most shipping companies is that they are simply too small to consider listing. That said, there are a significant number of public shipping companies which have listed their shares on the major stock exchanges of the world; these currently include Copenhagen,<sup>68</sup> Hong Kong,<sup>69</sup> New York,<sup>70</sup> Oslo,<sup>71</sup> Singapore,<sup>72</sup> Taipei,<sup>73</sup> and Tokyo,<sup>74</sup> although others, such as the London Stock Exchange, have also sought to enter this market.<sup>75</sup> The primary reason for listing is often the potential this gives to access a wider pool of finance, possibly also enhancing the company's public image, and, for existing shareholders, increasing the marketability of their shares. The disadvantage of listing is that flotation is demanding, involving legal, regulatory, financial and marketing aspects with

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<sup>65</sup> See Giannakoulis (n 25) 82; Stopford (n 12) 291.

<sup>66</sup> See Theodore C Syriopoulos, 'Shipping finance and international capital markets' in Costas Th Grammenos (ed), *The Handbook of Maritime Economics and Business* (2nd edn, Lloyd's List 2010) ch 28.

<sup>67</sup> Jeffrey Pribor and Cecilie Skajem Lind, 'Public and Private Equity Markets' in Kavussanos and Visvikis (n 11) 169, 170; Stopford (n 12) 297.

<sup>68</sup> AP Møller – Maersk A/S (Maersk) is the leading example.

<sup>69</sup> Stock Exchange of Hong Kong (SEHK): see, eg, China Cosco Holdings Co Ltd (China Cosco) and Orient Overseas (International) Ltd (OOIL) as prime examples.

<sup>70</sup> New York Stock Exchange (NYSE) and NASDAQ: see, eg, Costamare Inc, Diana Shipping Inc, Frontline Ltd, Navios Maritime Holdings, Teekay Shipping Corp, Tidewater Inc.

<sup>71</sup> The Oslo Børs (OB): see, eg, Odfjell SE.

<sup>72</sup> The Singapore Exchange (SGX): see, eg, Cosco International Singapore Co Ltd.

<sup>73</sup> Eg Hapag-Lloyd AG.

<sup>74</sup> The Tokyo Stock Exchange (TSE): see, eg, Kawasaki Kisen Kaisha Ltd (K Line), Mitsui OSK Lines, Nippon Yusen (NYK) Line.

<sup>75</sup> See, eg, Richard Meade, 'London Stock Exchange kicks off shipping charm offensive' *Lloyd's List* (London, 30 October 2012).

specialist professional advisors and, usually, services provided by an investment bank.<sup>76</sup> An IPO<sup>77</sup> is, therefore, a costly exercise and not one which is guaranteed to succeed.<sup>78</sup> As one leading writer has noted, having achieved listing, the corporate structures required by the markets can also slow decision-making and make the company subject to much greater scrutiny from shareholders, who are looking for a return on their investment.<sup>79</sup>

Another avenue for investment from public funds is the *bond* market,<sup>80</sup> a type of unsecured debenture offered by an issuer, a shipping company, to bondholders, financial institutions, for an agreed term,<sup>81</sup> with the payment of interest, the 'coupon', and gaining in popularity.<sup>82</sup> Such bonds may be characterised as investment grade, sub-investment grade, or convertible bonds (convertible into stock), but in shipping the bonds are 'high-yield', rated below investment grade,<sup>83</sup> and typically, for this reason, involving a relatively high coupon,<sup>84</sup> which may also be floating. At the end of the term, the capital is repaid to the bondholder. There are, inevitably, both advantages and disadvantages with this type of financing. An important advantage is that bonds are unsecured, with minimal covenants and no repayments during the life of the bond. The cashflow of shipping companies who enter this market is also protected as there is no need to make continuing payments to a bank. On the other hand, instead of a bilateral relationship between a single institution and the shipping company, albeit over a relatively short term, this type of security means that the shipping company is exposed to a debt which extends over a longer term, with the principal amount not repayable until the bond matures<sup>85</sup> rather than being gradually amortized. Although, in practice, there might be an expectation that the bond will eventually be refinanced, there may be the risk of

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<sup>76</sup> Pribor and Lind (n 67) 173.

<sup>77</sup> ie an 'Initial Public Offering' of shares.

<sup>78</sup> See, eg, Nigel Lowry, 'Why shipping is finding it tough to break IPO drought' *Lloyd's List* (London, 14 September 2018).

<sup>79</sup> Stopford (n 12) 299.

<sup>80</sup> Ibid, 300. For detailed treatment, see Basil M Karatzas, 'Public Debt Markets for Shipping' in Kavussanos and Visvikis (n 11) ch 6.

<sup>81</sup> Typically 10 years, but potentially longer (up to 15 years): *ibid*, 301.

<sup>82</sup> See, eg, Michelle Wiese Bockmann, 'High-yield bond market set for record boom' *Lloyd's List* (London, 26 January 2010); Janet Porter, 'CMA CGM raises \$741m through note offering' *Lloyd's List* (London, 9 July 2017); Abdul Hadhi, 'More shipping companies tapping bond market as available funds decline, Drewry says' *Lloyd's List* (London, 1 November 2017).

<sup>83</sup> These are usually rated below 'BBB-' by the major external credit rating agencies, namely, Standard & Poor's Financial Services LLC (S&P), Moody's Corp, and Fitch Ratings Inc, and are also known as speculative or junk bonds.

<sup>84</sup> See, eg, Giannakoulis (n 25) 85.

<sup>85</sup> Stopford (n 12) 301.

default on coupon payments, as occurred when some companies were forced into Chapter 11 proceedings<sup>86</sup> when they were unable to refinance their maturing bonds.<sup>87</sup>

## 2.5 Mezzanine financing

Falling somewhere between traditional debt finance from banks and financing from equity, mezzanine financing,<sup>88</sup> a type of hybrid financing between debt and equity, typically gives a lender the right to convert to an equity interest in the company in case of default but may also kick in<sup>89</sup> on maturity of the loan. Although hitherto not widely used,<sup>90</sup> there is some evidence of the availability of such financing from traditional shipping banks, private equity funds, or hedge firms,<sup>91</sup> particularly for smaller or medium-sized companies.<sup>92</sup> The debt may be secured by a second mortgage, but secured and unsecured loans, stock, junk bonds, subordinated loans, or preference shares are also common.<sup>93</sup> For shipping companies, the principal advantages are likely to be the availability of funding, not otherwise available, the provision of a more flexible repayment term, and spreading the dependence on debt financing across more than one source.<sup>94</sup> The main disadvantage for the shipowner, however, is cost, which will be higher than traditional secured debt.

## 2.6 Leasing and chartering

It may not always be attractive or practical to seek finance in one or other capital fund. Two other possibilities which have come to the fore are *operating leases* or *capital (financial) leases*.<sup>95</sup> In general terms, leases are attractive because they enable the shipping company, the lessee, to operate the ship without having ownership, which remains with the lessor. In

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<sup>86</sup> See, eg, 'Aegean Marine Petroleum files for Chapter 11 restructuring' *Lloyd's List* (London, 6 November 2018)

<sup>87</sup> See, eg, Inderpreet Walisa, 'Eagle Bulk completes \$256m refinancing' *Lloyd's List* (London, 12 December 2017).

<sup>88</sup> Giannakoulis (n 25) 81.

<sup>89</sup> A so-called 'equity kicker'.

<sup>90</sup> See Stopford (n 12) 296. Cf, eg, Lambros Papaeconomou, 'Shipping notes from Wall Street' *Lloyd's List* (21 January 2018); 'International Seaways ready for \$100m in mezzanine debt' *Lloyd's List* (London, 23 April 2018).

<sup>91</sup> Giannakoulis (n 25) 82.

<sup>92</sup> Miliotis (n 23) 17.

<sup>93</sup> See Cushing (n 27) 106; Paleokrassas (n 26) 139.

<sup>94</sup> *Ibid.*

<sup>95</sup> Philip Clausius, 'Ship Leasing' in Schinas et al (n 17) ch 14; Giannakoulis (n 25) 82; Stopford (n 12) 307.

the case of an operating lease, the ship is recorded only on the balance sheet of the lessor. Such leases have been heavily utilised by container shipowners.

In the case of a capital lease, the lessee has to record the leased asset in its books at the lower of the fair value of the asset or the present value of the minimum lease payments. Whether the lease is a capital lease essentially hinges on whether substantially all the risks and rewards of ownership have been transferred from the lessor to the lessee. In addition: (i) the agreement must contain a bargain purchase option price, which is at a significant discount to the reasonably expected price level; (ii) the fixed lease term should be equal to 75 per cent or more of the expected economic life of the asset; and (iii) the present value of the minimum lease payments must be equal to or greater than 90 per cent of the fair value of the asset.<sup>96</sup>

The structuring of a financial lease usually involves the creation of a so-called Special Purpose Company (SPC) by the lessor which arranges the building of the ship on a shipyard's standard terms, with financing provided by a bank, secured by a mortgage over the ship. The SPC leases the ship to the shipowner, provides a performance guarantee for all obligations and, during the course of the lease, makes payments pursuant to the relevant terms specified in the lease contract. Such leases are typically for much of or all of the operating life of the ship, unlike typical bank debt which is for a substantially shorter period.

For this reason, the lessor must be satisfied that the lessee will be able to meet its obligations under the lease.<sup>97</sup>

Such leases may also take the form of a sale and leaseback arrangement,<sup>98</sup> usually on a long-term bareboat charter basis, with an option (or obligation) to buy back the ship at the end of the lease.<sup>99</sup> With this type of arrangement, a ship already owned by the shipowner is sold to the leasing company, then chartered back.

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<sup>96</sup> Ioannis Alexopoulos and Nikos Stratis, 'Structured Finance in Shipping' in Kavussanos and Visvikis (n 11) 191, 203.

<sup>97</sup> For further consideration of the benefits and drawbacks, see *ibid.*

<sup>98</sup> For recent examples, see Anastassios Adamopoulos, 'Vitol in 11-tanker sale and leaseback deal with ICBC' *Lloyd's List* (London, 7 August 2018); 'Scorpio Bulkers announces sale and leaseback deal' *Lloyd's List* (London, 16 April 2019).

<sup>99</sup> Such an option is also available under the leading bareboat charterparty standard form, Barecon 2017 (and also under the earlier Barecon 2001 and Barecon 89 forms).

Another possibility is to structure the lease as a long-term time charterparty, paying a fixed amount of hire to the SPC which charters in the ship at a discounted rate to the spot market. The disadvantage, however, with a time charterparty, particularly one linked to the spot market, is that such markets are highly volatile and may make for a disproportionate burden to the lessee once spot freight rates drop below the level required to cover the lease payments and the cost of operating the ship.<sup>100</sup>

Although initially focused on container ships, such leasing arrangements have become increasingly attractive, particularly in light of the reduced availability of traditional bank finance and there has been an increase in the numbers and types of leases, covering all types of ships.<sup>101</sup>

## 2.7 Private equity

Another source of modern ship finance, particularly since the GFC, is private equity firms,<sup>102</sup> investment management companies that have more usually provided financial backing for startups or operating companies. Such investors were attracted to shipping by ships trading at historically low levels<sup>103</sup> and prominent examples of involvement in shipping have included acquisitions from asset sales by banks.<sup>104</sup> In some instances, joint ventures where both parties have contributed capital<sup>105</sup> have proved successful, but doubts have also been expressed as to whether shipping will attract significant investment from this sector.<sup>106</sup> Nevertheless, there is a degree of optimism that private equity will continue to be an important source of funding for shipping.<sup>107</sup>

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<sup>100</sup> See, eg, Giannakoulis (n 25) 83.

<sup>101</sup> See, eg, Lambros Papaeconomou, 'Five things to watch: ship finance' *Lloyd's List* (London, 19 April 2018).

<sup>102</sup> See, eg, Steve Matthews, 'Shipping still attractive to private equity funds' *Lloyd's List* (London, 24 February 2011); 'Owners must weigh up pros and cons of private equity' *Lloyd's List* (London, 10 March 2011).

<sup>103</sup> See, eg, Giannakoulis (n 25) 92; Pribor and Lind (n 67) 184.

<sup>104</sup> See above, text to n 26. See also James Baker, 'Gods of carnage' *Lloyd's List* (London, 22 November 2012).

<sup>105</sup> See, eg, Nicolaus Ascherfeld and Max Landshut, 'Joint ventures between private equity funds and shipping companies — current structures and exit scenarios' (2015) October/November *Marine Money* 14; Pribor and Lind (n 64) 185.

<sup>106</sup> See, eg, Liz McCarthy, 'Private equity cannot fill shortfall in ship finance' *Lloyd's List* (London, 28 September 2012); Nigel Lowry, 'Private equity steps back from shipping' *Lloyd's List* (London, 21 October 2014).

<sup>107</sup> Thus, 15% of responders thought so in a survey produced by the law firm, Norton Rose Fulbright in 2017: see *The Way Ahead: Transport Survey 2017*, <<https://transportsurvey.nortonrosefulbright.online/publications/shipping>> accessed 10 July 2019. See also Nigel Lowry, 'Private equity "is here to stay"' *Lloyd's List* (London, 13 October 2016).

## 2.8 Export credit agencies (ECAs)

Prior to the GFC, financing from export credit agencies in traditional shipbuilding countries was limited to around 10 per cent for shipping and off-shore financing.<sup>108</sup> This was because finance was widely available from banks. The post-GFC funding gap has, to some extent, been filled by the other financing mechanisms discussed earlier; nevertheless, for newbuilds in particular, ECAs provide a significant part of the required funding, either by extending direct funding to the shipowners or by issuing ECA guarantees/policies assigned to commercial banks.<sup>109</sup> Such funding is usually underpinned by the OECD's Sector Understanding on Export Credits for Ships (SSU) 2008,<sup>110</sup> which provides a set of non-binding guidelines for government-supported export credits for ships. ECA financing is available in countries<sup>111</sup> as diverse as China,<sup>112</sup> South Korea,<sup>113</sup> Germany,<sup>114</sup> Norway,<sup>115</sup> Italy,<sup>116</sup> Finland,<sup>117</sup> and France,<sup>118</sup> but there has been a marked escalation in the availability of export credit finance in the Far East, particularly China,<sup>119</sup> as a result of China's Belt and Road Initiative.<sup>120</sup> This type of finance has proved attractive when commercial financing is hard to come by. However, the loan tenor

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<sup>108</sup> By 2016 this had increased to more than 33%: see 'Shipping industry financing difficulties and alternative financing' (KPMG, 6 June 2016) <<https://home.kpmg/gr/en/home/insights/2016/06/funding-shipping-industry-obstacles-alternatives.html>> accessed 15 July 2019.

<sup>109</sup> See Alexopoulos and Stratis (n 96) 193.

<sup>110</sup> <<https://www.oecd.org/sti/ind/40198054.pdf>> accessed 15 July 2019. The participants are Australia, the EU, Japan, Korea, New Zealand, and Norway.

<sup>111</sup> See, generally, Ward and Hosek-Ugolini (n 27) 65.

<sup>112</sup> The Export-Import Bank of China (CEXIM) <<http://english.eximbank.gov.cn/>> accessed 15 July 2019; China Export & Credit Insurance Corp (Sinasure) <<http://www.sinasure.com.cn/en/>> accessed 15 July 2019.

<sup>113</sup> The Export-Import Bank of Korea (Korea Eximbank) <<https://www.koreaexim.go.kr/site/main/index002>> accessed 15 July 2019.

<sup>114</sup> Euler Hermes Deutschland AG (Hermes) <[https://www.eulerhermes.com/en\\_global.html](https://www.eulerhermes.com/en_global.html)> accessed 15 July 2019; KfW Bankengruppe <<https://www.kfw.de/kfw.de-2.html>> accessed 15 July 2019.

<sup>115</sup> Norwegian Export Credit Guarantee Agency (GIEK) <<https://www.giek.no/frontpage/>> accessed 15 July 2019; Eksportkreditt Norge AS (Export Credit Norway) <<https://www.eksportkreditt.no/en/>> accessed 15 July 2019.

<sup>116</sup> Istituto per I Servizi Assicurativi del Credito all'Esportazione (SACE); SIMEST <<https://www.sacesimest.it/en/about-us>> accessed 15 July 2019.

<sup>117</sup> Finnvera <<https://www.finnvera.fi/eng/>> accessed 15 July 2019.

<sup>118</sup> Compagnie Française d'Assurance pour le Commerce Extérieur (COFACE) <<https://www.coface.com/>> accessed 15 July 2019.

<sup>119</sup> See Cichen Shen, 'Cexim becomes world's largest shipping lender' *Lloyd's List* (London, 19 June 2018).

<sup>120</sup> Miliotis (n 20) 17.

is also generally longer than that provided by banks and the LTV amount can be 70 or 80 per cent of the value.<sup>121</sup>

## 2.9 Ship finance: the future?

As the preceding outline demonstrates, ship finance has undergone profound changes during the past decade. The dominating influence of traditional ship finance banks has gradually been worn down by exposure to toxic debt generated during the GFC. Meanwhile, the crisis in the banking sector generally, led to the Basel III and IV frameworks,<sup>122</sup> developed by the Basel Committee on Banking Supervision,<sup>123</sup> which sought to enhance the soundness and stability of the banking system by aligning minimum regulatory capital requirements more closely to the risks that banks face, and encouraging improvements in banks' risk management. The changes introduced were not directed specifically at banks offering shipping finance, but have significantly impacted this type of business.<sup>124</sup>

A further impact is the IMO regulations to reduce sulphur oxides (SOx) emissions from ships. Under Annex VI of the MARPOL Convention, these will from 1 January 2020 impose mandatory limits – a 0.50 per cent m/m (mass by mass) – for sulphur in fuel oil used on board ships operating outside designated emission control areas.<sup>125</sup>

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<sup>121</sup> See Kevin Oates, 'Ship Finance in Asia' <[https://globalmaritimehub.com/wp-content/uploads/attach\\_535.pdf](https://globalmaritimehub.com/wp-content/uploads/attach_535.pdf)> accessed 15 July 2019.

<sup>122</sup> There is some debate as to whether Basel IV is an additional framework or a completion of the Basel III accords. See, however, 'High-level summary of Basel III reforms' (Basel Committee on Banking Supervision, December 2017) <[https://www.bis.org/bcbs/publ/d424\\_hlsummary.pdf](https://www.bis.org/bcbs/publ/d424_hlsummary.pdf)> accessed 15 July 2019.

<sup>123</sup> This is a group of central banks and bank supervisory authorities in the G10 countries: see <<https://www.bis.org/bcbs/>> accessed 19 June 2019.

<sup>124</sup> See Steve Matthews, 'Access to finance is becoming increasingly difficult for shipping' *Lloyd's List* (London, 12 May 2010). Emily Lee, 'Basel III: post-financial crisis international financial regulatory reform' (2013) 28 *JIBLR* 433-447; 'Basel III and Its New Capital Requirements, as Distinguished from Basel II' (2014) 131 *Banking LJ* 27.

<sup>125</sup> MARPOL Reg 14.1. See also '2019 Guidelines for Consistent Implementation of the 0.50% Sulphur Limit under MARPOL Annex VI', Resolution MEPC.320(74), <<http://www.imo.org/en/OurWork/Environment/PollutionPrevention/Documents/Resolution%20MEPC.320%2874%29.pdf>> accessed 15 July 2019.



Taking a lead from this, the Poseidon Principles<sup>126</sup> have been developed in an effort spearheaded by certain global shipping banks<sup>127</sup> collaborating with leading industry players<sup>128</sup> and which are intended to be applicable to lenders, relevant lessors, and financial guarantors including export credit agencies. The Principles apply to all credit products secured by ship mortgages or finance leases secured by title over ships and where ships fall under the purview of the IMO.<sup>129</sup> In effect the Principles require signatories to measure and report the climate alignment of their individual shipping portfolios and will integrate climate considerations into lending decisions to incentivise maritime shipping's decarbonisation.<sup>130</sup> Whether this will have traction and impact on financing from banks remains to be seen. One leading commentator has argued that the world of ship finance should restrict its decisions to examination of the credit rating of the company soliciting finance and ensuring that there is a reasonable chance of the terms being fulfilled and the money being paid back on time.<sup>131</sup>

### 3 Mortgages and the law

#### 3.1 Registration and the effect of registration

This is not the place for a detailed review of the procedures required to register ship mortgages.<sup>132</sup> Suffice to say that there are differences between registers, particularly between common law and civil countries. In most common law countries, including Singapore

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<sup>126</sup> 'The Poseidon Principles: A global framework for responsible ship finance' (June 2019) <[https://www.poseidonprinciples.org/wp-content/uploads/2019/07/Poseidon\\_Principles.pdf](https://www.poseidonprinciples.org/wp-content/uploads/2019/07/Poseidon_Principles.pdf)> accessed 15 July 2019.

<sup>127</sup> Citi, Société Generale, and DNB. For the current signatories, see <<https://www.poseidonprinciples.org/signatories/>> accessed 15 July 2019. See Paul Taylor, 'Banks act to secure a future for shipping that's bright — and green' *Lloyd's List* (London, 18 June 2019); Jason Jiang 'Banks with a combined \$100bn shipping portfolio stimulate green change' *Splash247.com* (Singapore, 18 June 2019) <<https://splash247.com/eleven-shipping-banks-join-framework-to-promote-green-shipping/>> accessed 15 July 2019.

<sup>128</sup> AP Møller Mærsk, Cargill, Euronav, Gram Car Carriers, Lloyd's Register, and Watson Farley & Williams.

<sup>129</sup> Poseidon Principles (n 126) 1.

<sup>130</sup> See, eg, Richard Meade, 'Can banking's Poseidon adventure rewrite the script for shipping's decarbonisation disaster?' *Lloyd's List* (London, 17 June 2019).

<sup>131</sup> See Michael Grey, 'Viewpoint: Virtuous lending' *Lloyd's List* (London, 20 June 2019).

<sup>132</sup> For the registration procedures under different ship registers, see eg, Clegg and Ward (n 10) 313; Edward Watt, *Ship Registration: Law and Practice* (3rd edn, Informa 2019) chs 7-25.

and the UK,<sup>133</sup> ship mortgages are regulated by statute,<sup>134</sup> whereas in most civil law countries, including the top three ship registers, Panama, the Marshall Islands, and Liberia,<sup>135</sup> registration is not statutory<sup>136</sup> but contractual.

The Singapore Merchant Shipping Act 1995 provides that the

instrument creating the security ... shall be in the prescribed form or as near thereto as circumstances permit, and on production of that instrument the Registrar shall record it in the register.<sup>137</sup>

At first sight, the classic view of the ship mortgage is that the mortgage deed transfers ownership of the ship to the mortgagee, notwithstanding that the mortgagor, the shipowner, remains registered as 'owner' of the ship.<sup>138</sup> However, s 29 of the Merchant Shipping Act provides that:

Except as may be necessary for making a mortgaged ship or any share therein available as a security for the mortgage debt, the mortgagee shall not, by reason of the mortgage, be deemed to be the owner of the ship or share, nor shall the mortgagor be deemed to have ceased to be the owner thereof.<sup>139</sup>

On one view, s 29 should be read as providing that, although the mortgagee and not the mortgagor is owner, the mortgagor is to be treated as owner 'except as may be necessary for making a mortgaged ship ... available as security for the mortgage debt ...'. This approach certainly tallies with the view that the statutory mortgage provisions are better viewed as a sui generis statutory security. As a result, any security created and registered in accordance with the provisions of the statute will not, by virtue of registration, make the mortgagee

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<sup>133</sup> And most other common law jurisdictions, notably those in the Bahamas, Bermuda, Cyprus, and Hong Kong: see Julie Clegg, 'The ship mortgage — introduction' in Clegg and Ward (n 10) 151, 152.

<sup>134</sup> For Singapore, see the Merchant Shipping Act 1995, cap 179, Part II (for ships on the Singapore Registry); for the UK, see the Merchant Shipping Act 1995, c 21, Sch 1 (for UK-registered ships).

<sup>135</sup> Respectively, the current top three shipping registers worldwide: see *Review of Maritime Transport 2018* (UNCTAD) 35.

<sup>136</sup> Clegg (n 133) 152.

<sup>137</sup> S 25(1). Similar provision is made in the UK: see Sch 1, para 7(2), of the UK Merchant Shipping Act 1995.

<sup>138</sup> *Keith v Burrows* (1876) 1 CPD 722, 733. But cf *Ex parte North Brisbane Finance & Insurances Pty Ltd* [1983] 2 Qd R 684, 688.

<sup>139</sup> Cf Sch 1, para 10 of the UK Merchant Shipping Act 1995.

owner of the ship, but only give the mortgagee a *ius in re aliena*,<sup>140</sup> leaving intact the legal standing of the mortgagor as owner of the ship.<sup>141</sup>

Whatever view is taken of s 29, the statute is clear on the priority effect of statutory registration, namely that:

If there are more mortgages than one registered in respect of the same ship or share, the mortgagees shall, notwithstanding any express, implied or constructive notice, be entitled in priority one over the other, according to the date and time of the record of each mortgage in the register and not according to the date of each mortgage itself.<sup>142</sup>

In the event of non-registration of a mortgage,<sup>143</sup> it is clear that such an unregistered mortgage will fall behind a registered mortgage even if created before the statutory mortgage was registered and even if the registered mortgage had notice of the earlier mortgage.<sup>144</sup> This is subject to the rule that the registered mortgagee will not have priority where it has notice of the earlier mortgage and is in bad faith<sup>145</sup> or if the earlier interest was not, in fact, not registerable.<sup>146</sup> As between unregistered mortgages inter se and between unregistered mortgages and other equitable interests, priority is determined by the general equitable rules, such that that first in time interests will be prioritised, subject to postponement for inequitable conduct.<sup>147</sup> There is accordingly every incentive for the mortgagee and the mortgagor to ensure that registration is effected as soon as the loan is in place.

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<sup>140</sup> See, for this argument, George L Gretton, 'Ships as a branch of property law' in Andrew R C Simpson, Scott Crichton Styles, Euan West and Adelyn L M Wilson (eds), *Continuity, Change and Pragmatism in the Law: Essays in Memory of Professor Angelo Forte* (Aberdeen University Press, 2016) 367, 395.

<sup>141</sup> See particularly the arguments of Clarke (n 4) 681–4; Meeson and Kimbell (n 18) para 10.47.

<sup>142</sup> S 28. Cf Sch 1, para 8(1) of the UK Merchant Shipping Act 1995.

<sup>143</sup> An unregistered mortgage of a registered ship is equitable: see, eg, *The Shizelle* [1992] 2 Lloyd's Rep 444, 448 (legal unregistered mortgage of a ship not required to be registered). Cf also DC Jackson, *Enforcement of Maritime Claims* (4th edn, LLP 2005) para 23.38.

<sup>144</sup> *Black v Williams* [1895] 1 Ch 408, 421.

<sup>145</sup> See *Lombard North Central Ltd v Lord Advocate* 1983 SLT 361 (OH), 367.

<sup>146</sup> See, eg, *Household Financial Services Ltd v Island and River Trading Pty Ltd (The Sea Horse)* (NSW, 15 February 1993).

<sup>147</sup> Clarke (n 4) 684.

### 3.2 Deed of covenants

In practice, both in common law and civil law jurisdictions, the shipowner mortgagor and the mortgagee bank enter into a collateral agreement, the deed of covenants.<sup>148</sup> The deed invariably provides that it is supplemental to the statutory form of mortgage<sup>149</sup> and sets out the detailed contractual terms agreed between the parties. The deed of covenants is, typically, a substantial document which among other clauses will include assignments in favour of the mortgagee bank of earnings, insurances and involuntary disposition compensation<sup>150</sup> or separate deeds of assignment of insurances and of earnings.<sup>151</sup> Such deeds of covenants are essentially private contractual documents<sup>152</sup> and, for this reason, there are no standard forms as such, with each lender, or consortium of lenders, having its own preferences and standard terms and reflecting the terms on which finance has been offered.

### 3.3 Powers of the mortgagee

Mortgagees interests are typically protected at common law in three principal forms: possession of the ship; sale of the ship; arrest (and eventually, sale) of the ship. Each of these specific interests is now considered.

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<sup>148</sup> For examples, see the documents readily available online from two leading Singapore Banks, OCBC (<[http://www.ocbc.com/download/legal%20documents/20\\_ship%20loan%20financing/20.4\\_deed%20of%20covenants.doc](http://www.ocbc.com/download/legal%20documents/20_ship%20loan%20financing/20.4_deed%20of%20covenants.doc)> accessed 15 July 2019) and UOB (<[https://www.uobgroup.com/extranet/legal\\_docs\\_forms/Deed-Of-Covenants\\_Shipfinancing-032014.doc](https://www.uobgroup.com/extranet/legal_docs_forms/Deed-Of-Covenants_Shipfinancing-032014.doc)> accessed 15 July 2019). See also the deed in Osborne et al (n 18) App 3.

<sup>149</sup> In the form of mortgage required in common law countries: see the Preamble, UOB Deed of Covenants.

<sup>150</sup> See, eg, cl 4 of the deed in Osborne et al (n 18) 555. For detailed consideration, see Ian Mace, 'The assignment of insurances, earnings, charter rights and requisition compensation' in Clegg and Ward (n 10) 275.

<sup>151</sup> See, eg, UOB Deed of Assignment of Insurances; UOB Deed of Assignment of Earnings. As to the latter, see, eg, *SGB Finance SA v The owners and all persons claiming an interest in the MV 'Connoisseur'* [2018] IEHC 699, [2019] 1 Lloyd's Rep Plus 11.

<sup>152</sup> See *The Maule* [1997] 1 WLR 528 (PC), 532. Also reported as *Banque Worms v Owners of the Ship or Vessel 'Maule'* [1997] 1 Lloyd's Rep 419.

### 3.3.1 Possession

The mortgagee has no inherent right to take possession of the ship<sup>153</sup> or to intercept freight until possession is taken<sup>154</sup> and the statutory provisions on ship mortgages make no such provision. There are, however, two circumstances when such a right might arise at common law: (i) when ‘the money secured by the mortgage is due’;<sup>155</sup> or (ii) where the mortgagee’s security over the mortgaged ship has been impaired.<sup>156</sup> The possessory remedy is, however, rarely resorted to, primarily because of the statutory remedies available under both the Singapore and UK Merchant Shipping Acts, but also because support for the existence of such a right of possession has waned.<sup>157</sup>

### 3.3.2 Sale

The Singapore and UK Merchant Shipping Acts make express provision for a self-help remedy for the enforcement of the mortgagee’s interest in the ship. This remedy, a ‘self-help’ remedy, distinguishes mortgages in many common law jurisdictions from mortgages of ships registered in most civil legal systems,<sup>158</sup> which do not have an equivalent doctrine of self-help and require enforcement to be conducted exclusively through the courts. The Singapore provision states that:

Every registered mortgagee shall have power absolutely to dispose of the ship or share in respect of which he is registered, and to give effectual receipts for the purchase money; but where there are more persons than one registered as mortgagees of the same ship or share, a subsequent mortgagee shall not, except under the order of the High Court, sell the ship or share without the concurrence of every prior mortgagee.<sup>159</sup>

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<sup>153</sup> But cf *Collins v Lamport* (1864) 4 De G J & S 500, 504; *Wilson v Wilson* (1872) LR 14 Eq 32, 40; *Keith v Burrows* [1877] AC 636, 645.

<sup>154</sup> *Gardner v Cazenove* (1856) 1 H & N 423; *Brown v Tanner* (1868) LR 3 Ch App 597; *Liverpool Marine Credit Co v Wilson* (1872) LR 7 Ch 507; *Beynon v Godden* (1878) LR 3 Ex D 263; *Shillito v Biggart* [1903] 1 KB 683.

<sup>155</sup> See, eg, *The Cathcart* (1867) LR 1 A & E 314; *The Blanche* (1887) 6 Asp MLC 272.

<sup>156</sup> *Collins v Lamport* (1864) 4 De G J & S 500; *The Heather Bell* [1901] P 272; *The Manor* [1907] P 339.

<sup>157</sup> See Clarke (n 4) 688. Cf, however, *Latitude Fisheries Pty Ltd v The Ship ‘South Passage’* [2014] FCA 186 [13] where the view expressed in *The Heather Bell* (n 155) was accepted.

<sup>158</sup> There are, however, some notable exceptions, particularly among those civil law countries which have ties with the USA, such as Liberia, the Marshall Islands, and Panama: see Charles Buss, ‘Ship mortgagees: enforcement and remedies’ in Barış Soyer and Andrew Tettenborn (eds), *Shipbuilding, Sale and Finance* (Informa Law from Routledge 2016) 149, 151.

<sup>159</sup> Merchant Shipping Act 1995, s 30(1).

The wording in the equivalent UK legislation is different, providing that

every registered mortgagee shall have power, *if the mortgage money or any part of it is due*, to sell the ship or share in respect of which he is registered, and to give effectual receipts for the purchase money.<sup>160</sup>

While the wording of the Singapore legislation does not appear to require any pre-conditions for the exercise of the rights of sale, it appears unlikely that the power could be exercised without some indication of default, as is the case in the UK provision. Nevertheless, the parties may prefer to set out any express right of sale in the deed of covenants, as was the case in *The Maule*.<sup>161</sup>

In that case there were no instalments outstanding under a loan agreement, cl 7 of the loan agreement providing that:

Upon the procedure of any of the Events of Default specified in the Loan Agreement, then and in each and every such event the Mortgagee shall become forthwith entitled as and when it may see fit to put into force and to exercise all the powers possessed by it as Mortgagee and Chargee of the ship and in particular ... (e) to sell the ship or any share therein with or without prior notice to the owner ...

The Privy Council noted that, in the case of ship mortgages, the rights and duties of the parties were 'overwhelmingly dominated by contract'; accordingly, if the contract was clear enough, an express power of sale could be exercised even though there was nothing due under the loan.<sup>162</sup> Reversing the Hong Kong Court of Appeal,<sup>163</sup> the Privy Council held that there was nothing in the first part of the clause, under which the mortgagee was entitled 'to put into force and to exercise' the power of sale, which suggested that the exercise of the power was to be dependent on anything other than an event of default. Further, there was no room for any implied requirement or condition that money should first have become due under the

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<sup>160</sup> Sch 1, para 9(1) of the Merchant Shipping Act 1995. Emphasis supplied.

<sup>161</sup> [1997] 1 WLR 528 (PC), 532.

<sup>162</sup> At 533.

<sup>163</sup> [1995] HKEC 864.

loan agreement and nor could any such requirement be extracted from the words ‘all the powers possessed by it as Mortgagee’.<sup>164</sup>

In ordinary terms it is trite law that the mortgagor’s equity of redemption cannot be gratuitously overridden without some form of notice to the mortgagor, permitting it to redeem the ship.<sup>165</sup> If the mortgagor were then to make full payment of all outstanding sums, such a sale would be wrongful and the mortgagor would be entitled to damages.<sup>166</sup> In relation to cl 7(e) of *The Maule*, the Privy Council held that

the mere presence of a power to sell without notice does not render the whole power invalid. If, as in the present case, the borrowers are aware of the proposed sale, they can give seven days’ notice to repay ... and thereby redeem the ship. The mere possibility that the power of sale could be exercised in an unlawful manner without notice does not invalidate the power of sale in circumstances where the borrowers have a full opportunity to redeem.<sup>167</sup>

The recent case of *The Ocean Wind 8 of Hartlepool*<sup>168</sup> has highlighted the mortgagee’s rights on sale of a ship. A shipowner mortgaged *The Ocean Wind 8 of Hartlepool*, a British-registered wind farm support ship, to a bank in order to secure a loan of €2.247 million, the second defendant<sup>169</sup> acting as guarantor. When the shipowner fell into arrears on the mortgage, the bank took possession of the *Ocean Wind 8 of Hartlepool* and, through the services of an independent broker, sold the ship for £1.7 million. The proceeds of the sale were, however, insufficient to discharge the amount outstanding under the loan agreement and the bank brought proceedings to recover the shortfall of £220,000. After the shipowner was placed in compulsory liquidation, proceedings against it were stayed, whereupon the guarantor was

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<sup>164</sup> [1997] 1 WLR 528 (PC), 533. For fuller discussion, see Clarke [1997] LMCLQ 329.

<sup>165</sup> See *Miller v Cook* (1870) LR 10 Eq 641, 647 (Sir John Stuart V-C): ‘In the present case, besides the other objections to the contract, the terms of the power of sale are oppressive, and put the plaintiff completely at the mercy of the defendant. The power to sell without any notice to the plaintiff enabled the defendant at any moment to extinguish the right of redemption.’

<sup>166</sup> See *Fletcher & Campbell v City Marine Finance Ltd* [1968] 2 Lloyd’s Rep 520, 538.

<sup>167</sup> [1997] 1 WLR 528 (PC), 533.

<sup>168</sup> *Close Brothers Ltd v AIS (Marine) 2 Ltd (The Ocean Wind 8 of Hartlepool)* [2018] EWHC B14 (Admlty), [2019] 1 Lloyd’s Rep 510.

<sup>169</sup> Paul Simon Chandler.

sued. The guarantor submitted that no further money was owed because the bank had sold the ship at an undervalue in breach of its duty to obtain the best price reasonably obtainable.

The case was heard by Mr Jervis Kay QC, the Admiralty Registrar,<sup>170</sup> who provided the following outline of the relevant legal principles:<sup>171</sup>

- that the mortgagee of a ship owed the same duty of care in relation to the sale as any other mortgagee owed<sup>172</sup>
- that the mortgagee owed a non-delegable duty in equity to take reasonable care to obtain the best price reasonably obtainable at the time<sup>173</sup>
- that, absent cases of real urgency, the property had to be properly exposed to the market<sup>174</sup>
- that a true market value could have an acceptable margin of error<sup>175</sup>
- that a mortgagee must behave as a reasonable man would behave in the realisation of his own property, so that the mortgagor may receive credit for the fair value of the property sold<sup>176</sup>
- that the mortgagee must act fairly towards the mortgagor; he could protect his own interests but he was not entitled to conduct himself in a way which unfairly prejudiced the mortgagor and must take reasonable care to maximise his return from the property<sup>177</sup>
- that the mortgagee's duty to take care to sell for the best price was not delegable, for example by appointing a reputable agent to conduct the sale<sup>178</sup>

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<sup>170</sup> He possesses all the powers of the Admiralty Judge: see Meeson and Kimbell (n 18) ch 9; John A Kimbell, 'The Admiralty Registrar: past, present, and future' [2018] LMCLQ 414.

<sup>171</sup> [2018] EWHC B14 (Admlty) [12]. The principles also applied in respect of the mortgagee's duty to a guarantor: see *Standard Chartered Bank Ltd v Walker* [1982] 1 WLR 1410; *China & South Sea Bank Ltd v Tan* [1990] 1 AC 536 (PC).

<sup>172</sup> *Gulf & Fraser Fishermen's Union v Calm C Fish Ltd (The Calm C)* [1975] 1 Lloyd's Rep 188 (Can).

<sup>173</sup> *Tse Kwong Lam v Wong Chit Sen* [1983] 1 WLR 1349; *Raja v Austin Gray (A Firm)* [2002] EWCA Civ 1965, [2003] Lloyd's Rep PN 126.

<sup>174</sup> *Silven Properties Ltd v Royal Bank of Scotland Plc* [2003] EWCA Civ 1409, [2004] 1 WLR 997.

<sup>175</sup> *Michael v Miller* [2004] EWCA Civ 282.

<sup>176</sup> *McHugh v Union Bank of Canada* [1913] AC 299 (PC).

<sup>177</sup> *Palk v Mortgage Services Funding Plc* [1993] Ch 330.

<sup>178</sup> *Raja v Austin Gray (A Firm)* [2002] EWCA Civ 1965, [2003] Lloyd's Rep PN 126 [34].



- that a mortgagee was not entitled to unfairly prejudice the mortgagor by selling hastily at a knock-down price sufficient to pay off the debt<sup>179</sup>
- that a sale at just above the sum required to discharge the mortgage may be looked at carefully by the court, although there might well be occasions when that was the proper price or true market value
- that the mortgagee could not sell to himself, either alone or with others, or to a trustee for himself, nor to anyone employed by him to conduct the sale unless the sale was ordered by the court and he had obtained permission to bid<sup>180</sup>
- that where the mortgage sold to a ‘connected’ person the burden of proof was reversed and mortgagee had to prove that he took reasonable care to obtain the best price<sup>181</sup>
- that the reason for considering whether the mortgagee and the purchaser were or might be ‘connected’ was the need to guard against unconscious bias as well as the risk of other forms of skulduggery<sup>182</sup>

Having set out these principles in the context of a ship mortgage, the main issue then turned upon whether the ship had, in fact, been sold at an undervalue. The Admiralty Registrar noted that ship valuations were difficult and required a wide knowledge of the relevant markets. These were known to fluctuate rapidly and opinions might differ markedly between brokers.<sup>183</sup> The best guidance on the true value of a ship at a given time was to be obtained from actual sales of similar ships or, in the absence of such data, from any information available regarding similar ships.<sup>184</sup> Accordingly, although ‘on the low side’, the Admiralty Registrar considered that the price was in the appropriate bracket for the *Ocean Wind 8 of Hartlepool* when the sale took place. Moreover, given the state of the market at the relevant time, it was unlikely that a higher price could have been achieved.<sup>185</sup>

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<sup>179</sup> *Silven Properties Ltd v Royal Bank of Scotland Plc* [2003] EWCA Civ 1409, [2004] 1 WLR 997.

<sup>180</sup> *Farrar v Farrars Ltd* (1888) 40 ChD 395, 409.

<sup>181</sup> *Saltri III Ltd v MD Mezzanine SA Sicar* [2012] EWHC 3025 (Comm), [2013] 1 All ER (Comm) 661.

<sup>182</sup> *Australia & New Zealand Banking Group Ltd v Bangadilly Pastoral Co Pty Ltd* (1978) 139 CLR 195, 201 (cited with approval in *Alpstream AG v PK AirFinance SARL* [2013] EWHC 2370 (Comm), [2014] 1 All ER (Comm) 441).

<sup>183</sup> [2018] EWHC B14 (Admlty) [19].

<sup>184</sup> *Ibid.*

<sup>185</sup> *Ibid* [22].

The Admiralty Registrar noted that it was not surprising that a mortgagee, such as a lending bank wishing to repossess and sell a ship, would employ a broker<sup>186</sup> to perform that duty and to give advice. Appointment of a broker could not be regarded as acting in breach of an obligation to the mortgagor or guarantor.<sup>187</sup> Nevertheless, the Admiralty Registrar cautioned that the mere appointment of a broker could not diminish the duties of the mortgagee itself which was liable for any failings by its broker as the broker was acting as the mortgagee's selling agent rather than as an independent contractor.<sup>188</sup> Although the broker had been criticised for not advertising the *Ocean Wind 8 of Hartlepool*, it had sent the particulars to over 300 recipients but, given the restricted nature of the market and the number of operators involved, such marketing efforts were more than adequate.<sup>189</sup> The only offer made that had exceeded the sale price was based on borrowing conditions that would have meant that the bank was wholly or almost wholly financing the deal but no reasonable bank could have been expected to accept such conditions.<sup>190</sup> There was no evidence that the bank had suggested to its broker that the ship should be deliberately sold at an undervalue.<sup>191</sup> The Admiralty Registrar also rejected the argument that the ship was apparently sold in haste. Ships were wasting assets which cost money to moor and maintain and a mortgagee was justified in obtaining a sale at the earliest date to recover as much of the capital as possible.<sup>192</sup> The bank was, therefore, entitled to a sum to be assessed after considering the appropriate deductions that should be made from the sale price to account for the sale costs.<sup>193</sup>

The case will undoubtedly prove useful for a number of reasons. Among these is the Admiralty Registrar's careful summary of the principles generally applicable when a mortgagee chooses to exercise its rights of sale. Users of the Admiralty court will, however, wish to pay particular attention to the Admiralty Registrar's scrutiny of ship valuations, which seldom attract such specific and detailed scrutiny. In particular, the judgment underlines the duties of brokers in this context and the overriding duty of the mortgagee. While no two ship valuations will ever be conducted in the same way, given the ship-specific nature of the exercise, the general

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<sup>186</sup> Braemar.

<sup>187</sup> Ibid [23].

<sup>188</sup> Ibid.

<sup>189</sup> Ibid.

<sup>190</sup> Ibid.

<sup>191</sup> Ibid.

<sup>192</sup> Ibid.

<sup>193</sup> Ibid [26].

guidance provided will be useful for mortgagees when contemplating the sale of a ship in the future.

### 3.3.3 Arrest and sale of the ship

The statutory power of extra-judicial sale is, in reality, seldom used for ships, because such an extra-judicial sale rarely fetches a good price and, unlike a judicial sale of the ship,<sup>194</sup> will not give purchasers clean title.<sup>195</sup> For this reason, mortgagees more often than not rely on the statutory wording that:

Every registered mortgagee shall be entitled to enforce his mortgage by an action in rem in admiralty whenever any sum secured by the mortgage is unpaid when due or otherwise in accordance with the terms of any deed or instrument collateral to the mortgage.<sup>196</sup>

This wording is reinforced in the admiralty jurisdiction statute in Singapore, the High Court (Admiralty Jurisdiction) Act,<sup>197</sup> which absorbs the admiralty jurisdiction provisions of the Administration of Justice Act 1956,<sup>198</sup> was passed to reformulate into English law the provisions of the Arrest Convention 1952.<sup>199</sup> Section 3(1)(c)<sup>200</sup> of the High Court (Admiralty Jurisdiction) Act<sup>201</sup> therefore recognises that the admiralty jurisdiction of the High Court includes ‘any claim in respect of a mortgage of or charge on a ship or any share therein’.<sup>202</sup> Such claims are enforceable in rem and the admiralty jurisdiction of the High Court may be invoked against the ‘ship or property in question’.<sup>203</sup> A warrant for the arrest of the ship may

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<sup>194</sup> *The Tremont* (1841) 1 Wm Rob 163; *The Cerro Colorado* [1993] 1 Lloyd’s Rep 58, 61.

<sup>195</sup> For the effect of private sales, see *The Turtle Bay* [2013] SGHC 165, [2013] 4 SLR 615; *The M/V Union Gold*, *The MV Union Silver*, *The M/V Union Emerald*, *The M/V Union Pluto* [2013] EWHC 1696 (Admlty), [2014] 1 Lloyd’s Rep 53; *The Sea Urchin* [2014] SGHC 24; [2014] 2 SLR 646. See also Buss (n 158) 153; Paul Myburgh, “‘Satisfactory for its own purposes’”: Private direct arrangements and judicial ship sales’ (2016) 22 JIML 355.

<sup>196</sup> Section 30(2). For recent examples, see, eg, *Latitude Fisheries Pty Ltd v The Ship ‘South Passage’* [2014] FCA 186; *The Swiber Concorde* [2018] SGHC 197, [2018] 5 SLR 1283, [2019] 1 Lloyd’s Rep 2.

<sup>197</sup> 1961 (rev ed 2001), cap 123.

<sup>198</sup> 4 & 5 Eliz II, c 46, ss 1-8.

<sup>199</sup> This was not wholly successful and further revisions were made in the Senior Courts Act 1981, c 54, ss 20-27: see DC Jackson, ‘Admiralty jurisdiction — the Supreme Court Act 1981’ [1982] LMCLQ 236.

<sup>200</sup> See also the UK Senior Courts Act 1981, s 20(2)(c).

<sup>201</sup> Rev ed 2001, cap 123. Singapore is not a contracting state to the Arrest Convention 1952.

<sup>202</sup> See also s 3(4)(c) (and s 20(7)(c) of the UK Senior Courts Act 1981). The origins of the provision may be found in the Supreme Court of Judicature (Consolidation) Act 1925, 15 & 16 Geo V, c 49, s 22(1)(a)(ix).

<sup>203</sup> S 4(2). See also s 21(2) of the UK Senior Courts Act 1981.

be halted, subject to court approval,<sup>204</sup> if security is provided for the release of the ship.<sup>205</sup> If no security is provided, the creditors of the ship, including any mortgagees, can apply to the court for an order for sale of the ship and the court may make an order for a sale before judgment,<sup>206</sup> *pendente lite*, for good reason.<sup>207</sup> The mortgagee bank will also be permitted to make a bid or offer and participate in the sale by the court.<sup>208</sup>

#### 4 Material impairment of security and events of default

The trigger for action by mortgagees is, in practice, whenever the lender finds that there is a threat or material impairment to its security. In *Collins v Lamport*,<sup>209</sup> Lord Westbury LC suggested that

so long ... as the dealings of the mortgagor with the ship are consistent with, and do not materially prejudice and detract from, or impair the sufficiency of the mortgagee's security, the mortgagor has ... authority to enter into all contracts touching the disposition of her necessary to assure to him the full value and benefit of his property. But whenever a mortgagee can show that the act of the mortgagor prejudices or injures his security ... he can claim the full benefit of and exercise the rights given to him by his mortgage.<sup>210</sup>

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<sup>204</sup> See the provisions for release of the ship in Singapore: O 70, r 12 (for the UK, see the CPR, Pt 61, Rule 61.8(4)). This was recently considered by the English Court of Appeal in *Natwest Markets Plc (formerly known as the Royal Bank of Scotland plc) v Stallion Eight Shipping Co SA (The Alkyon)* [2018] EWCA Civ 2760, [2019] 1 Lloyd's Rep 406.

<sup>205</sup> See Paul Myburgh, 'P & I Club letters of undertaking and admiralty arrests' (2018) 24 JIML 201.

<sup>206</sup> This possibility is not available in many civil law countries, which require the mortgagee to have obtained judgment or 'executory title' before the court will order a sale of the ship: see Buss (n 158) 152.

<sup>207</sup> See *The Myrto* [1977] 2 Lloyd's Rep 243; *Deutsche Bank Trust Co Americas v The owners of the motor ship 'Sertao'* [2018] EWHC 1013 (Admlty). See D Rhidian Thomas, 'Admiralty sales *pendente lite*' (1998) 17 CJQ 409; Paul Myburgh, 'Admiralty sales *pendente lite*: reserve prices and broker appointments' (2018) 24 JIML 369.

<sup>208</sup> See *Norddeutsche Landesbank Girozentrale v The ship 'Beluga Notification' (No 2)* [2011] FCA 665 [33]–[34].

<sup>209</sup> (1864) 4 De G J & S 500, 503-504. See also *The Heather Bell* [1901] P 272, 280; *The Manor* [1907] P 339, 358.

<sup>210</sup> On the facts, the court held that the mortgagor had made a charterparty which was not prejudicial to the sufficiency of the security and that the mortgagees were bound by it. The court granted an injunction to restrain the mortgagees from dealing with the ship in any manner inconsistent with, or which might interfere with or prevent, the execution of the charterparty.

Whether or not there is what amounts to a threat to the mortgagee's security will be a question of fact<sup>211</sup> with the burden of proof falling on the mortgagee.<sup>212</sup> The mortgagee will often be assisted by one or more events of default<sup>213</sup> specified in the deed of covenants. In the absence of such a default or a degree of threat to the mortgagee's security, such as an actual or threatened fall in the net value of the ship, the mortgagor can restrain interference by the mortgagee. But this need not mean that the shipowner is under a duty to operate the ship; indeed, as the case of *Keith v Burrows*<sup>214</sup> illustrates, it may well choose to lay-up the ship, so long as in so doing the ship does not deteriorate or its value decline.

Depending on the wording of the default clause, one or more of the specified events may entitle the bank to accelerate the loan<sup>215</sup> and enforce its security. It is important to recognise, however, that this may not necessarily be the first (or preferred) step that the lender will take.<sup>216</sup> Where, as is often the case, the reason for the default is financial distress, it may be sensible to attempt to address this by a consensual restructuring of the underlying loan. If, however, this proves unworkable because the borrower is refusing to co-operate because it believes that a market recovery is imminent, the mortgagee will need to take steps to enforce its security. Before doing so, however, it may be prudent to consider a number of discrete questions:<sup>217</sup>

- where is the ship physically located?
- how favourable is the relevant jurisdiction where the ship is located for arrest and enforcement procedures?
- is there an existing charterparty commitment which may be prejudiced by the arrest?
- are there any trade creditors with claims against the ship that may rank ahead of the mortgage in that jurisdiction?

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<sup>211</sup> *The Myrto* [1977] 2 Lloyd's Rep 243, 254.

<sup>212</sup> *The Fanchon* (1880) 5 PD 173, 177.

<sup>213</sup> In *Doe v Roper* (1798) 1 Bos & P 250, 258, Eyre CJ stated that he did 'not know a larger or looser word than "default"'.

<sup>214</sup> [1877] AC 636, 645. See also *Collins v Lamport* (1864) 4 De G J & S 500, 504; *Wilson v Wilson* (1872) LR 14 Eq 32, 40.

<sup>215</sup> Ie cancel any outstanding lending commitment and declare all amounts owed to the bank to be immediately due and payable or payable on demand. This can only occur, however, if an acceleration clause is included in the agreement.

<sup>216</sup> See Buss (n 158) 149.

<sup>217</sup> See Spoulllos (n 32) 213, 225.

- will the ship's trade creditors be co-operative?
- will the borrower co-operate?
- who is the manager of the ship and could the manager be changed in case of a lack of co-operation?
- what are the costs of enforcement?
- are there prospective buyers for the ship?
- are there any foreign exchange rules in the jurisdiction where the ship is to be arrested which could prevent or delay any remittance of sale proceeds?

What amounts to a default must depend on what the relevant default clause says. The UOB Deed of Covenants clause<sup>218</sup> contains a list of 22 specified types of default, each of which is stated to be an 'event of default'. The latter is defined as

any event, state of affairs or circumstance specified as such in Clause 9 (*Events of Default*), including any event which would, with the passing of time, the giving of notice, the satisfaction or non-satisfaction of any condition, upon the Mortgage making a definition under any Facility Letter or Security Document or in any combination of the foregoing, constitute such an event ...<sup>219</sup>

Taking *non-payment* first,<sup>220</sup> typically the mortgagor will not have made a payment on one or more contractual payment dates.<sup>221</sup> Although non-payment per se is not mentioned, this would be embraced by the following wording:

**Other Default:** if the Mortgagor defaults in the discharge of any liabilities or indebtedness incurred in relation to the Ship or the employment thereof and such default may, in the opinion of the Mortgagee, have a material adverse effect ...<sup>222</sup>

Other defaults will arise in relation to the ship, such as if the registration of the ship is 'suspended, cancelled or revoked or (without the prior written consent of the Mortgagee)

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<sup>218</sup> Cl 9.

<sup>219</sup> Cl 1.1.

<sup>220</sup> See Osborne et al (n 18) para 11.3. See, eg, *Close Brothers Ltd v AIS (Marine) 2 Ltd (The Ocean Wind 8 of Hartlepool)* [2018] EWHC B14 (Admlty); [2019] 1 Lloyd's Rep 510, above at text to n 168.

<sup>221</sup> If more than one payment default has occurred, it may be necessary to consider whether the default has been waived or time for payment is no longer of the essence.

<sup>222</sup> UOB, cl 9.1(n).

changed ...'<sup>223</sup> or if the classification of the ship is likewise 'suspended, cancelled, discontinued or withdrawn or if any recommendations of the Classification Society<sup>224</sup> in relation to the ship is not complied with when due'.<sup>225</sup> Further defaults will occur where:

- the ship is disposed of (or there is an attempt to do so) without the prior written consent of the mortgagee<sup>226</sup>
- where the mortgagee, without prior written consent, creates or permits to arise or subsist any security interest,<sup>227</sup> other than those permitted<sup>228</sup>
- where the ship is or is likely to be libelled, arrested, detained or levied upon or taken into custody or seized<sup>229</sup>
- where any execution proceedings, attachment or other court processes are issued or brought against the ship<sup>230</sup>
- where the ship is compulsorily requisitioned or acquired<sup>231</sup>
- where the ship is laid-up without the prior written consent of the mortgagee or is the ship is laid up for more than 30 days<sup>232</sup>
- if the ship becomes a total loss<sup>233</sup>
- if the mortgagor abandons the ship<sup>234</sup>
- if the mortgagor breaches any security document<sup>235</sup> or if any security document is terminated<sup>236</sup>
- if it becomes impossible or illegal for the mortgagor to perform or fulfil the terms of any security document and this may, in the opinion of the mortgagee, have a 'material adverse effect'<sup>237</sup>

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<sup>223</sup> Cl 9.1(b).

<sup>224</sup> Defined in cl 1.1.

<sup>225</sup> Cl 9.1(c).

<sup>226</sup> Cl 9.1(d).

<sup>227</sup> See the definition in cl 1.1.

<sup>228</sup> Cl 9.1(e).

<sup>229</sup> Cl 9.1(f).

<sup>230</sup> Cl 9.1(g).

<sup>231</sup> Cl 9.1(h).

<sup>232</sup> Cl 9.1(i).

<sup>233</sup> Cl 9.1(j). See the definition in cl 1.1.

<sup>234</sup> Cl 9.1(k)

<sup>235</sup> Cl 9.1(l)

<sup>236</sup> Cl 9.1(m).

<sup>237</sup> Cl 9.1(o).

- if there is non-compliance with laws and regulations, such as ISM Code, ISPS Code, and MARPOL Protocol<sup>238</sup>
- if the terms of any environmental approvals<sup>239</sup> are not complied with or any environmental claim<sup>240</sup> is made<sup>241</sup>
- if any environmental incident<sup>242</sup> or any accident or major conformity, as defined in the ISM Code, occurs<sup>243</sup>
- if the ship is or is likely to be involved in any court or arbitral proceedings and this is likely to exceed an amount equivalent to 10 per cent of the insured value of the ship<sup>244</sup>
- if the mortgagor fails to maintain the required insurance coverage<sup>245</sup>
- if the ship is or is likely to be arrested, detained, or if any requisition of the ship for hire occurs<sup>246</sup>
- if the ship is involved in any incident required repairs which is likely to exceed an amount equivalent to 10 per cent of the insured value of the ship<sup>247</sup>

Default may also occur when there has been a so-called '*status*' default,<sup>248</sup> when an event occurs which affects the legal or financial standing of the mortgagor, such as a default under some other financial instrument,<sup>249</sup> or where an administration or winding up order is made against the mortgagor. Another type of default involves a *material adverse change* (MAC) in financial condition or a *material adverse effect* (MAE)<sup>250</sup> on the mortgagor's ability to perform its obligations. Such defaults are usually carefully scrutinised and a mortgagee seeking to rely on an MAC or MAE default will need to be confident that the applicable event or circumstance has occurred.<sup>251</sup>

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<sup>238</sup> Cl 9.1(p). These are all defined in cl 1.1.

<sup>239</sup> Defined in cl 1.1.

<sup>240</sup> Ibid.

<sup>241</sup> Cl 9.1(q).

<sup>242</sup> Defined in cl 1.1.

<sup>243</sup> Cl 9.1(r).

<sup>244</sup> Cl.9.1(s).

<sup>245</sup> Cl 9.1(t).

<sup>246</sup> Cl 9.1(u).

<sup>247</sup> Cl 9.1(v).

<sup>248</sup> Osborne et al (n 18) para 11.4.1.

<sup>249</sup> A so-called 'cross-default'.

<sup>250</sup> Osborne et al (n 18) para 11.4.2.

<sup>251</sup> See, further, Osborne et al (n 18) 222.



The difficulties which an impecunious borrower might face were highlighted in *The Alkyon*.<sup>252</sup> The claimants, Natwest Markets plc<sup>253</sup> and Royal Bank of Scotland plc, arrested the ship, a bulk carrier, at the port of Tyne<sup>254</sup> and sought an order for the sale of the ship so as to recover US\$12.8m together with interest. Natwest was the mortgagee of the ship under a First Preferred Marshall Islands mortgage dated 2 February 2015 but on 19 February 2018 Natwest advised the borrower that it had agreed to terms to ‘sub-participate’ its economic interest in the loan with Bank of America Merrill Lynch (BAML). The underlying issue was whether there was an event of default in consequence of the borrower’s<sup>255</sup> failure to comply with a notice under cl 17.15 of the loan agreement:

17.15. Additional security. If at any time the aggregate of the Market Value of the Ship and the value of any additional security ... determined conclusively by appropriate advisers appointed by the Agent ... for the time being provided to the Security Agent under this Clause 17.15 is less than one hundred and twenty five per cent (125%) of the aggregate of the amount of the Loan then outstanding and the amount certified by the Swap Provider to be the amount which would be payable by the Borrower to the Swap Provider under the Master Agreement if an Early Termination Date were to occur at that time (the ‘VTL Coverage’), the Borrower shall, within thirty (30) days of the Agent’s request, at the Borrower’s option:

17.15.1 pay the Security Agent or to its nominee a cash deposit in the amount of the shortfall to be secured in favour of the Security Agent as additional security for the payment of the Indebtedness; or

17.15.2 give to the Security Agent other additional security in amount and form acceptable to the Security Agent in its discretion; or

17.15.3 prepay the Loan in the amount of the shortfall.

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<sup>252</sup> *Natwest Markets Plc (formerly known as the Royal Bank of Scotland plc) v Stallion Eight Shipping Co SA (The Alkyon)* (2 May 2019). See also the earlier proceedings between the parties: *Natwest Markets Plc (formerly known as the Royal Bank of Scotland plc) v Stallion Eight Shipping Co SA (The Alkyon)* [2018] EWCA Civ 2760, [2019] 1 Lloyd’s Rep 406 (upholding [2018] EWHC 2033 (Admlty), [2018] 2 Lloyd’s Rep 601); Tettenborn [2019] LMCLQ 168.

<sup>253</sup> Formerly Royal Bank of Scotland plc.

<sup>254</sup> ie pursuant to its powers of arrest under the UK Senior Courts Act 1981: see above at text to n 194.

<sup>255</sup> The borrower was not represented in the proceedings, save for a letter from its sole director.

Under the VTL notice the borrower was required to provide additional security of US\$1.75 million or repay the loan in the amount of US\$1.4 million. On 22 March 2018, the claimant notified the borrower that the market value of the ship was US\$15.25 million, 112 per cent of the aggregate of the amount of the loan then outstanding, and requested the borrower within 30 days to pay a cash deposit as additional security, to provide other security, or to prepay the loan. The borrower disputed the valuation provided by BRS<sup>256</sup> and provided valuations from Clarksons,<sup>257</sup> Braemar ACM Valuations Ltd,<sup>258</sup> Maersk Broker K/S,<sup>259</sup> and BRS,<sup>260</sup> all of which were higher than the initial BRS valuation.

On 25 April 2018 the claimant notified the borrower that an event of default had occurred and reserved the rights of the finance parties. By a notice dated 15 June 2018 ('the First Acceleration Notice'), the claimant notified the borrower that the total commitments were cancelled and that the loan together with accrued interest was immediately due and payable, and it demanded that the borrower immediately repay the loan. By a notice dated 20 July 2018 ('the Second Acceleration Notice'), the claimant notified the borrower that if it was the agent and the First Acceleration Notice was not valid or effective, then the total commitments were cancelled and the loan together with accrued interest was immediately due and payable, and it demanded that the borrower immediately repay the loan.

These issues in the case crystallised around cl 17.15 of the loan agreement. The first issue was whether the original valuation by BRS was outside the range of values which could have been determined by a reputable, independent, and first class firm of shipbrokers acting honestly, in good faith and rationally, and using a conventional valuation procedure or methodology. The judge, however, found that while the original BRS valuation was lower than the valuations later provided by the borrower, this was not outside the conventional range and had not been provided otherwise than in accordance with the market valuation term of the loan agreement. A related issue was whether, in choosing a valuer, the claimant had acted in a way which was arbitrary, capricious, or for an improper purpose, or otherwise than in pursuit

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<sup>256</sup> US\$15.25m (on 21 March).

<sup>257</sup> US\$17.5m (on 28 March).

<sup>258</sup> US\$17.25m (on 16 April).

<sup>259</sup> US\$17m–US\$18m (on 17 April).

<sup>260</sup> US\$16.5m (on 20 April).

of its legitimate commercial interests and thereby in breach of the appointment term. The judge found that this was not the case.

The final issue was whether the claimant was in breach of the loan agreement in purporting to cancel the total commitments and accelerate the loan. In the light of the conclusions he had already reached, the judge was satisfied that there was no breach on the part of the claimant, which he noted went

to the commercial heart of the matter and the answer at the commercial heart of the matter is whether the commercial parties have or have not acted in accordance with the commercial arrangements that they agreed between themselves. It is clear from what I have already found that the claimants have acted within the envelope of that commercial arrangement.<sup>261</sup>

While it was clear on the facts that the disposal of the economic interest on the loan<sup>262</sup> had altered the commercial dynamic in a way which was not favourable to the borrower — which its director in his letter to the court described as a ‘readily discernible change of position’ and allegedly made it harder to engage with those at the helm economically than had been the case before the disposal of the economic interest — the judge was not sympathetic. He noted, in particular, that the channel of communication when a matter was in dispute or when there was a difficulty in a channel of communication was through the solicitors involved. He found that there was nothing to indicate that the claimants’ solicitors were not prepared to receive dialogue or engagement, regardless of the disposal of the economic interest.<sup>263</sup>

The proceedings in this second hearing involving the *Alkyon* were notable because of the absence of any legal representation on the part of the borrower, which it could not afford.<sup>264</sup> Other points to note from the court’s decision are its scrutiny of the terms of the loan agreement and, in particular, the mechanism for the assessment of the market value of the ship and which, once activated, amounted to an event of default under the agreement.

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<sup>261</sup> Transcript, p 10.

<sup>262</sup> *le to BAML*.

<sup>263</sup> *Ibid*.

<sup>264</sup> Emphasised by the fact that its solicitors had ‘recently come off the record’: transcript, p 2. This may be contrasted with the earlier proceedings where the borrower was represented by a leading shipping QC and junior counsel: see *The Alkyon* (n 252).

## 5 Mortgage enforcement and priorities

Creditors involved in shipping disputes frequently face a formidable hurdle: following the sale of the ship there are insufficient assets to satisfy all the outstanding claims against the ship.<sup>265</sup> In such circumstances, it becomes paramount to determine the relative standing, or priority, of each claim vis-à-vis other, different, types of claim and also similar claims inter se.<sup>266</sup> For less well-secured creditors,<sup>267</sup> the risk is that the claim by the mortgagee will eviscerate the fund realised from the sale of the ship. In Singapore, as with many countries in the British commonwealth, the backdrop is English law.<sup>268</sup> While there is no Convention factor in Singapore,<sup>269</sup> as is also the case in the UK and most other commonwealth countries, there is also no codified hierarchy of admiralty priorities. The fundamental principle in relation to claims by mortgagees is that while these fall behind<sup>270</sup> maritime liens,<sup>271</sup> whether arising before or after the mortgage,<sup>272</sup> they enjoy priority over all other statutory in rem claims,<sup>273</sup> which includes the providers of necessaries to the ship.<sup>274</sup>

The basis for any variation to the established ranking of claims has long been recognised as flexible, by reference to considerations of equity,<sup>275</sup> public policy, commercial expediency,

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<sup>265</sup> See, eg, *The Ruta* [2000] 1 WLR 2068, 2070.

<sup>266</sup> For a classic treatment of priorities, see D R Thomas, *Maritime Liens* (Stevens & Sons, 1980), ch 9. See also Jackson (n 143) ch 23; Meeson and Kimbell (n 18) ch 6.

<sup>267</sup> Notably those creditors having a statutory right of action in rem against the ship: see the High Court (Admiralty Jurisdiction) Act, cap 123, s 3(1)(d)–(q) and the UK Senior Courts Act 1981 s 20(2)(e)–(r).

<sup>268</sup> In Singapore, the category of Sheriff's expenses is read more widely, notably in respect of port dues (see, eg, *The Felicie* [1991] SGHC 138, [1991] 2 SLR(R) 550; *Planmarine AG v Maritime and Port Authority of Singapore* [1999] SGCA 16, [1999] 1 SLR(R) 669) and crew wages (see, eg, *Keppel Corp Ltd v Chemical Bank* [1994] SGCA 3, [1994] 1 SLR(R) 54). But the same is not true of agency expenses: see *The 'Makassar Caraka Jaya Niaga III-39'* [2012] SGHC 175. More generally, see Toh Kian Sing, *Admiralty Law and Practice* (3rd edn, LexisNexis 2017) 366.

<sup>269</sup> Neither Singapore nor the UK has ratified the Maritime Liens and Mortgages Convention 1993 (in force 5 September 2004).

<sup>270</sup> See art 5.1 of the Maritime Liens and Mortgages Convention 1993. Cf, however, the South African Admiralty Jurisdiction Regulation Act 1983, Act No 105 of 1983 (as amended), s 11, discussed in Gys Hofmeyr, *Admiralty Jurisdiction: Law and Practice in South Africa* (2nd edn, Juta & Co Ltd 2017) 291.

<sup>271</sup> In Singapore, as elsewhere in the commonwealth, these are limited to damage done by a ship, salvage, the master and crew's wages, and master's disbursements: see, eg, Thomas (n 266) chs 4-7. The maritime lien for bottomry (and respondentia) is now redundant: *ibid*, ch 8. See also the Australian Admiralty Act 1988 (Cth), s 15(2).

<sup>272</sup> See *The Royal Arch* (1857) Swa 269.

<sup>273</sup> *Johnson v Black (The Two Ellens)* (1872) LR 4 PC 161, 170.

<sup>274</sup> As illustrated by the deeply flawed reasoning of the majority in *Bankers Trust International Ltd v Todd Shipyards Corp (The Halcyon Isle)* [1981] AC 221 (PC).

<sup>275</sup> *The Leoborg (No 2)* [1964] 1 Lloyd's Rep 380, 383.

and justice.<sup>276</sup> The proposition that the established order of priorities may be altered if the equities in any particular case demand it, is widely recognised among commonwealth countries, including Singapore,<sup>277</sup> which again follows English law in this regard.<sup>278</sup> Other jurisdictions, such as Australia,<sup>279</sup> New Zealand,<sup>280</sup> Canada,<sup>281</sup> and Hong Kong,<sup>282</sup> have also generally adopted the English position.<sup>283</sup> The bottom line is that the courts insist that the established order of priorities should only be disturbed if there is a ‘powerful reason’ to do so, one which is truly exceptional or special, and when departure from the established order is essential to prevent an obvious injustice.<sup>284</sup> The bar is high, some would say appropriately so, given the need for certainty and predictability in an area of law which is not governed by statute but by precedent of long-standing.

A Singapore case, *The Posidon*,<sup>285</sup> has recently provided detailed consideration of the criteria required to disturb the Admiralty order of priorities in which mortgagees are preferred over other statutory in rem claimants. The case concerned a loan facility agreement, secured by mortgages for two ships, the *Posidon*<sup>286</sup> and the *Pegasus*.<sup>287</sup> The loan agreement was complicated, providing for the capitalisation of any unpaid interest, which would be added to

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<sup>276</sup> Thomas (n 266) para 418.

<sup>277</sup> *The Eastern Lotus* [1980] SGCA 1, [1979-1980] SLR(R) 389, [7].

<sup>278</sup> [2016] SGHC 138, [2017] 2 Lloyd’s Rep 390 [14].

<sup>279</sup> *Patrick Stevedores No 2 Pty Ltd v The Proceeds of Sale of the Ship MV ‘Skulptor Konenkov’* [1997] FCA 361, (1997) 75 FCR 47, 50; *Reiter Petroleum Inc v The Ship ‘Sam Hawk’* [2016] FCAFC 26, [2016] 2 Lloyd’s Rep 639, [79].

<sup>280</sup> *ABC Shipbrokers v The Ship ‘Offi Gloria’* [1993] 3 NZLR 576, 582; *Fournier v The Ship ‘Margaret Z’* [1999] 3 NZLR 111, 117.

<sup>281</sup> *Comeau’s Sea Foods v The Frank and Troy* [1971] FC 556 [17]–[19]; *Todd Shipyards Corp v Altema Compania Maritima (The Ioannis Daskalelis)* [1974] 1 Lloyd’s 174, 179; *Tito G Llido v The ship ‘Lowell Thomas Explorer’* [1980] 1 FC 339 [11]; *Fraser Shipyard & Industrial Centre Ltd v Expedient Maritime Co* (1999) 170 FTR 1; *Bank of Scotland v Nel* [2001] 1 FC 408, 419–20.

<sup>282</sup> *Hua Chiao Commercial Bank Ltd v The Fortune Founder* [1987] HKLR 156, 160.

<sup>283</sup> See also Toh (n 268) 394.

<sup>284</sup> *The Pickaninny* [1960] 1 Lloyd’s Rep 533, 537; *The Lyrma (No 2)* [1978] 2 Lloyd’s Rep 30, 33; *Scott Steel Ltd v The Ship ‘Alarissa’* 125 FTR 284, [15]; *Fournier v The Ship ‘Margaret Z’* [1999] 3 NZLR 111, 117; *Royal Bank of Scotland plc v The Golden Trinity* [2004] FCJ No 992, 254 FTR 1 [118].

<sup>285</sup> [2017] SGHC 138, [2018] 3 SLR 372, [2017] 2 Lloyd’s Rep 390. Some shipowners have a liking for Greek gods when naming ships, such as the famous, but now sadly defunct, Blue Funnel Line (owned by Alfred Holt and Co of Liverpool), all of whose ships were named after major figures of classical Greek history. See also the earlier discussion of the Poseidon Principles at text to n 126.

<sup>286</sup> In Greek mythology Posidon — or, more correctly, Poseidon — was the god of the sea, of earthquakes, and horses, credited with the power of gathering clouds, raising and calming the sea, letting loose storms, and granting safe voyages. He is often depicted riding a four-horse chariot and wielding a trident: see, eg, *The Oxford Classical Dictionary* (4th edn, Oxford University Press 2012).

<sup>287</sup> Pegasus is the mythical winged horse said to have sprung from the severed neck of the gorgon, Medusa, when pregnant by Poseidon, and renowned as the carrier of the thunder and lightning of Zeus: *ibid*.

the principal amount of the loan. Non-payment of interest during the first 24 months of the loan (the so-called 'grace period') was not considered to be an event of default but when the owner defaulted on an interest payment some months after the grace period, the bank treated this as an event of default. The bank duly communicated this to the registered owner and warrants of arrest were issued against them the ships in Singapore. The proceedings arose following an application by a bank for the determination of the order of priorities against the proceeds of sale.

The bank sought payment out of the balance of sale proceeds in partial satisfaction of in rem judgments which it had obtained in its favour, but the application was opposed by the interveners,<sup>288</sup> three bunker suppliers<sup>289</sup> who had supplied bunkers to the ships.<sup>290</sup> The bunker suppliers obtained judgment in default of appearance,<sup>291</sup> pursuant to a maritime claim arising under s 3(1)(l) of the Singapore legislation.<sup>292</sup> The question now was whether the bank or the bunker suppliers had priority. The bunker suppliers argued that they had priority ahead of the bank because the bank had allegedly authorised and approved the bunker purchases. Alternatively, they argued that the bank had, with knowledge of the shipowners' insolvency, acquiesced in the procurement of bunkers knowing that it would benefit from them.

The bunker suppliers' main argument was a classic one in the circumstances. They argued that the order of priorities was not immutable because the distribution of the sale proceeds by the court was a matter of procedure and practice that took into account considerations of equity. They further argued that the equities of the case justified an alteration of the order of

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<sup>288</sup> As to interveners, see O 70, r 16 of the Singapore Rules of Court (CPR Part 61.8(7) of the Civil Procedure Rules in England). In *The Dowthorpe* (1843) 2 W Rob 73, 77, Dr Lushington explained that 'if a person may be injured by a decree in a suit, he has a right to be heard as against the decree although it may eventually turn out that he can derive no pecuniary benefit from the result of the suit itself'. See further *The Long Bright* [2018] SGHC 216, [2018] 5 SLR 1397, [2019] 1 Lloyd's Rep Plus 19.

<sup>289</sup> World Fuel Services (Singapore) Pte Ltd, World Fuel Services Europe Ltd, and World Fuel Services Trading DMCC.

<sup>290</sup> By long-standing Admiralty usage, such claimants are often referred to as 'necessaries men', in deference to s 6 of the Admiralty Court Act 1840, 3 & 4 Vict, c 65, which gave such jurisdiction to the then High Court of Admiralty in England.

<sup>291</sup> See O 70, r 20 of the Singapore Rules of Court (CPR Part 61.9 of the Civil Procedure Rules in England).

<sup>292</sup> See s 20(2)(m) of the UK Senior Courts Act 1981. This head of claim is widely framed as 'any claim in respect of goods or materials supplied to a ship for her operation or maintenance'. See also art 1(k) of the Arrest Convention 1952.

priorities such that their various bunker claims would rank ahead of the bank's mortgage claims.

The judge found that there were three main factors which cumulatively went to the equities of the particular case and warranted a departure from the established order of priorities such that a mortgagee's claim was ordered to rank behind that of a supplier of bunkers. First, knowledge that the mortgagor was insolvent has to be shown; next, the mortgagee must be fully aware, in advance, of the nature and extent of the expenditure incurred by the competing claimant; and finally, any such expenditure must bring about some benefit to the mortgagee.<sup>293</sup> Ultimately, the overarching consideration was the justice of the case that called for an alteration to the order of priorities.<sup>294</sup>

Having identified the relevant principles, the judge held that the interveners had not shown that any benefit accrued to the bank and/or its security because of the supply of bunkers.<sup>295</sup> The fact that the bunkers gave the ships motive power so as to generate earnings benefited the borrowers, not the bank.<sup>296</sup> It was also the borrowers, not the bank, which had the use of the operating account in the relevant period.<sup>297</sup> There was, moreover, no evidence that the borrowers were insolvent prior to the event of default and up to that date the bank had no reason to believe that the borrowers were unable to pay their debts as they fell due.<sup>298</sup> From the perspective of the bank, the borrowers were merely facing a short-term cash flow difficulty pending receipt of freight/hire, and it had taken a commercial decision to extend a bridging loan 'to a good customer'.<sup>299</sup>

The judge emphasised that the order of priorities would only be recalibrated if the mortgagee was fully aware in advance of the arrangements made by the bunker suppliers.<sup>300</sup> It was not sufficient to say that, since all ships required bunker fuel to have motive power, the

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<sup>293</sup> These three factors were not listed in order of importance: [2017] SGHC 138 [27].

<sup>294</sup> Ibid.

<sup>295</sup> Ibid [34].

<sup>296</sup> Ibid [86].

<sup>297</sup> Ibid [69].

<sup>298</sup> Ibid [84].

<sup>299</sup> Ibid [81].

<sup>300</sup> See *ibid* [86], relying on *Canadian Imperial Bank of Commerce (CIBC) v The 'Orion Expedito'* [1990] FCJ No 1160, 43 FTR 284.

mortgagee must be taken to have knowledge of the fuel supplies being procured.<sup>301</sup> In the present case the bank did not have knowledge of the bunker supplies. Accordingly, the bunker suppliers had not shown the existence of special circumstances to justify a departure from the established order of priorities so as to enable their claims to rank ahead of the bank's mortgage claims.<sup>302</sup>

The case therefore endorses the status quo, which has long favoured the claims of mortgagee banks over other types of admiralty claimants, save for maritime lienees. It provides important guidance on the steps that will need to be taken by claimants, particularly the providers of necessaries who might wish to make a case to a court disturbing the established order which favours mortgagee banks over other statutory claimants. Although a Singapore case and hence not binding outside the jurisdiction, the case is likely to provide authoritative and helpful guidance in other jurisdictions.

## **6 Postscript: ship finance and new technology**

There is considerable interest in the shipping industry in the possibilities of blockchain, the 'distributed ledger technology' which enables information and transactions to be managed collectively across an entire network using a chain of blocks of data. Initially the technology behind the popular cryptocurrency Bitcoin, blockchain, as a secured, decentralised, and encrypted public ledger, is now being explored by various industries as a means of revolutionising the way trades, transactions, and payments are performed.<sup>303</sup>

The initial push in the shipping industry has seen large operators collaborating with technology companies to gauge how blockchain technology may assist them in the future.<sup>304</sup> In addition to this, maritime hubs, including Singapore, are actively exploring the possibility

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<sup>301</sup> Ibid.

<sup>302</sup> Ibid, [90].

<sup>303</sup> See Elson Ong, 'Blockchain bills of lading', CML Law Working Paper Series 18/07 <<https://law.nus.edu.sg.cml/pdfs/wps/CML-WPS-1807.pdf>> accessed 18 March 2019.

<sup>304</sup> See 'Blockchain Series — No 1 Blockchain and Shipping March 2018' <<http://www.wfw.com/wp-content/uploads/2018/03/WFWBriefing-Blockchain-and-Shipping.pdf>> accessed 18 March 2019.



of digitalising trade and maritime documentation, such as bills of lading.<sup>305</sup> All of this is being done in the hope that blockchain technology will create a platform not anchored down by endless paperwork and complex transactions, but instead fully digitalised, reducing costs. In Singapore, Cargill and Rio Tinto have completed a test run of a blockchain-based letter of credit and electronic bill of lading; in Rotterdam, ABN Amro and Samsung have teamed up in an effort to reduce paperwork.<sup>306</sup>

Whether some of this could yet spill over to the ship finance context is still speculative. It has been argued that this could be possible,<sup>307</sup> and there is some evidence of this in the market, with the establishment of shipowner.io,<sup>308</sup> a start-up which intends to democratize investment in merchant ships by offering a blockchain-based trading platform, and claims to have US\$200 million in listed assets and services.<sup>309</sup> Using tokens, it is said that investors will be able to buy into assets and services on the marketplace platform and in this way enable small investors to buy into the business of ship finance, with shipowners benefitting from greater liquidity, better price transparency, lower costs, and more secure transactions. The arrival of such start-ups must, nevertheless, be approached with some caution.<sup>310</sup> While ship registers already actively promoted the use of digital technology for communicating with their registered members, whether financial institutions will want to allow highly confidential and client-specific financial information to be recorded using blockchain technology remains to be seen.

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<sup>305</sup> While there is considerable uncertainty concerning the legal value of blockchain bills of lading, as with other electronic bills of lading, Singapore has announced that it is pushing ahead with a pilot of its blockchain-based maritime trade platform, TradeTrust: see, eg, 'Eliminating paper documents, S\$300m research fund top-up among MCI's 2019 plans' <<https://www.channelnewsasia.com/news/singapore/eliminating-paper-documents-s-300m-research-fund-top-up-among-11308722>> accessed 18 March 2019.

<sup>306</sup> See James Baker, 'Blockchain trials turn to finance', *Lloyd's List*, 9 November 2018.

<sup>307</sup> 'Ship registry, mortgages and liens in electronic form': see <<https://www.oxtonlaw.com/ship-registry-mortgages-and-liens>> accessed 18 March 2019.

<sup>308</sup> See <<https://shipowner.io>> accessed 21 August 2019.

<sup>309</sup> See 'Blockchain arrives for ship finance' *The Maritime Executive* (5 February 2018), <<https://www.maritime-executive.com/article/blockchain-arrives-for-ship-finance>> accessed 21 August 2019.

<sup>310</sup> See Max Tingyao Lin, 'Cryptos can succeed in shipping, but investors need to be careful' *Lloyd's List* (London, 26 February 2018).

## 7 Conclusion

This paper has sought to draw together a number of strands rarely found in any one particular dimension in the existing literature. The first part of the paper demonstrates how the upheaval in the ship finance market has provided an opportunity for the development of a new range of ship finance products, mainly as a response to the withdrawal of some of the major banks. There are now formidable limitations exercised by those banks which continue to maintain a shipping loan book and a range of imaginative and, in some instances, tried and tested solutions available.

The financial crunch has also seen a number of well-known shipping companies go to the wall. On the one hand, this has brought to the fore the complex relationship between insolvency and admiralty.<sup>311</sup> On the other hand, this has also resulted, in a number of instances, in a renewed focus by some banks in enforcing mortgages, against which much bank finance was formerly readily offered and secured, albeit in better days. The mechanism for taking action against recalcitrant borrowers has never appeared as formidable as is currently the case, with many lenders actively taking steps against borrowers whose financial difficulties have brought them within the terms of the events of default so assiduously drafted in many deeds of covenants and considered recently in *The Alkyon*.<sup>312</sup> In such circumstances, the interests of other maritime creditors may also come to the fore, as was the case in *The Posidon*.<sup>313</sup> Other parties, such as guarantors caught up in the fray, may be more willing to challenge the steps taken by the enforcing bank, as was the case in *The Ocean Wind & of Hartlepool*,<sup>314</sup> although in the particular circumstances they were unable to persuade the court that bank had sold the ship at an undervalue.

Shipping is, famously, a cyclical business remarkable for the peaks and troughs which frequently occur,<sup>315</sup> often provoked by factors outside shipping. The GFC has been no exception and has brought about a prolonged slump in shipping and, not least, shipping finance. This has had a profound effect on the way in which shipping is financed and, as this

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<sup>311</sup> See above at n 6.

<sup>312</sup> Above at text to n 252.

<sup>313</sup> Above at text to n 285.

<sup>314</sup> Above at text to n 168.

<sup>315</sup> See especially Stopford (n 12) ch 3.

paper has sought to show, the way in which banks have sought to recoup their losses from borrowers.