

SECURITY FOR SHIP FINANCING IN SINGAPORE — A CASE STUDY

In 1961 the United Nations Industrial Survey Mission¹ mapped out a maritime future for Singapore and recommended, *inter alia*, that the then nascent shipbuilding industry be given an impetus. Today shipbuilding is one of the leading sectors of the economy in Singapore.²

It is proposed to consider the security arrangements in respect of the purchase of a new ship to be constructed and registered in Singapore from a case study which represents the paradigm, at least for most major shipbuilders.

The financing that is required by the shipowner for the purchase of the ship is met by the shipbuilder who is prepared to finance up to eighty per cent of the purchase price. The balance of twenty per cent is to be paid by the shipowner before delivery of the vessel. The terms of the deferred payment are therefore twenty per cent "down payment" to be paid in four instalments of five per cent each at various stages during the course of construction and, on completion of the vessel, half-yearly payments spread over a period of eight years, the first payment to commence six months from the date of delivery.

A sale of a ship which has not come into existence is a sale of future goods under the English Sale of Goods Act, 1893,³ the contract being an agreement to sell. Although generally no property in the ship passes until it is completed, it is possible to draft a contract giving the shipowner "the property in those parts which, when they are put together, make the complete ship".⁴ But in the case under study there is no such term as the shipowner is required to pay only twenty per cent of the purchase price up to delivery of the completed ship. From the view point of the shipbuilder the twenty per cent payment is insufficient to justify the passing of property in the uncompleted ship.

The shipbuilder does not alone carry the burden of financing and looks to a financier — a banker — for loan and banking facilities. The

1. The Mission, led by Dr. A. Winsemius, submitted a report dated 13 June 1961 to the Government of Singapore, on "An Industrialization Programme for Singapore."
2. Noted by the Minister for Labour, *New Nation*, 26 November 1974.
3. 56 & 57 Vict., c. 71. The Act is applicable if an issue relates to a "mercantile" one under s. 5(1) of the Civil Law Act, Cap. 30, Singapore Statutes, Rev. Ed., 1970.
4. *Sir James Laing and Sons v. Barclay, Curie and Co. Ltd.* [1908] A.C. 35 at p. 43 (*per* Lord Halsbury).

security arrangements must therefore be considered between (i) the shipowner and the shipbuilder and (ii) the shipbuilder and the banker.

A. SECURITY ARRANGEMENTS BETWEEN SHIPOWNER AND SHIPBUILDER

The property in the completed vessel passes to the shipowner on delivery and the purchase on deferred payment is secured by a series of promissory notes and a mortgage of the ship at the time of delivery, accompanied by a deed of covenants.

PROMISSORY NOTES

The shipowner makes and delivers to the shipbuilder a series of sixteen promissory notes each in the principal sum equal to five per cent of the purchase price. The notes carry interest at the agreed rate from the delivery date down to the date of payment. They mature successively at half-yearly intervals.

It is noteworthy that each note contains a provision that “the parties are entitled to the benefits of the deed of covenants which contains, among other things, provision for *acceleration of the maturity* upon the happening of certain stated events and also for prepayments on account of the principal sum prior to the maturity upon the terms and condition therein specified”.⁵

Does a provision importing a condition as to acceleration of the maturity date take the instrument out of the definition of a promissory note? A promissory note is defined in section 88(1) of the Bills of Exchange Act⁶ as:

...an unconditional promise in writing made by one person to another signed by the maker, engaging to pay, on demand or *at a fixed or determinable future time*, a sum certain in money, to, or to the order of a specified person or to bearer.⁷

Where the promise is to pay on a maturity date, it is clear that there is an engagement “to pay...at a fixed...future time.” Where the time for payment is determined by the occurrence of an event then whether or not it satisfies the requirement of “determinable future time” would depend on whether or not the event is certain or uncertain. If the event is one which may never occur, then the time is indeterminate and hence outside the ambit of section 88(1). Thus in the English case of *Beardesley v. Baldwin*,⁸ it was held that a promissory note to pay money within so many days after the defendant should marry was not a negotiable note under the English Bills of Exchange Act, which is in *pari materia* with the local Act. Again, in the English

5. Emphasis added.

6. Cap. 28, Singapore Statutes, Rev. Ed., 1970.

7. Emphasis added.

8. (1941) 2 Stra. 1151.

case of *Palmer v. Pratt*,⁹ it was held that an order to pay at thirty days after the arrival of the ship "Paragon" at Calcutta was not a promissory note as the ship may never arrive.

In the case of the acceleration clause under study, there are two alternative times for payment: it is fixed in so far as any of the stated events contained in the deed of covenants do not occur. However, should any of those events occur, the acceleration clause advances the maturity date to the happening of the event. This is to be distinguished from those cases where there is only one method of payment—and it is dependent on some contingency.

Be that as it may, the definition speaks of, *inter alia*, "a fixed or determinable future time," so that the time must be a fixed or a determinable future time; it cannot be both "fixed" and "determinable". Does the acceleration clause alter the fixed time to one which is determinable? Comparison may be drawn from section 9(1)(c) of the Act which provides:

The sum payable by a bill is a *sum certain* within the meaning of this Act, although it is required to be paid—by stated instalments, *with a provision that upon default in payment of any instalment the whole shall become due*.¹⁰

The analogy of section 9(1)(c) should apply: it is submitted that the acceleration clause does not alter the fixed time to one which is "determinable at a future time" even though it may advance the time of payment.

MORTGAGE OF THE SHIP

1. The Merchant Shipping Act

It is pertinent to give some background to the present position relating to registration of Singapore ships and registered mortgages under the Merchant Shipping Act (hereinafter referred to as the Act).¹¹

Registration of Ships

Before 2nd September 1966, Singapore was a port of British registry. In 1966,¹² an independent registry for Singapore ships was established and the law was amended in 1968¹³ to provide for an open registry of ships offering a flag of convenience to any shipowner in Singapore. The ownership of Singapore ships is not restricted in any way to Singapore citizens or corporations incorporated in Singapore. A ship is defined in section 2 as including "every description of vessel

9. (1924) 2 Bing. 185.

10. Emphasis added.

11. Cap. 172, Singapore Statutes, Rev. Ed., 1970.

12. The Merchant Shipping (Amendment) Act, No. 26 of 1966, made provision for the establishment of a register of Singapore ships.

13. The Merchant Shipping (Amendment) Act, No. 44 of 1968 (now ss. 396 to 415 and 417 to 524 of the Act, Cap. 172).

used in navigation not propelled by oars.” A “vessel” is in turn defined as including “any ship or boat or any other description of vessel used in navigation”. Under section 397 of the Act, the following ships are not required to be registered:

- (a) any ship not exceeding fifteen tons;
- (b) any native sailing ship;
- (c) any boat licensed under section 350 of the Act;
- (d) any fishing vessel licensed under the Fisheries Act.

However this does not mean that all other ships must be registered as section 396(1) simply provides:

Any ship over fifteen tons wherever built and whether owned by a citizen of Singapore or a body corporate established or registered in Singapore or by a citizen or national of any foreign country or a body corporate established or registered outside Singapore, *may* be registered as a Singapore ship.¹⁴

However, under section 616(1) only a “Singapore ship or a share therein”¹⁵ may be the subject of a registered mortgage under the Act. A “Singapore ship” is defined in section 2 as “a ship registered under Part XIII of this Act.” Hence, before a mortgage can be registered, the ship itself must first be registered in the port of registry in Singapore.

Registered Mortgages

Before the Merchant Shipping (Amendment No. 2) Act, 1970,¹⁶ sections 31-46 of the United Kingdom Merchant Shipping Act, 1894¹⁷ applied to mortgages of Singapore ships. Section 416 has now been repealed and specific provisions are made in regard to mortgages of Singapore ships without reference to the United Kingdom Merchant Shipping Act. However, except for a few technical points, these provisions are in *pari materia* with those in the United Kingdom Act.

The new section 416(1) makes provision for the registration of a mortgage of a Singapore ship or a share therein as security for a loan: the instrument creating the security must be “in the prescribed form or as near thereto as circumstances permit”. The main particulars contained in the prescribed form are the official number and name of the ship, its number year and port of registry, the acknowledgment of the loan by the mortgagor, the covenants for the loan and interest. There is also a statement that a mortgage is created in the ship “above particularly described and in her boats, guns, ammunition, small arms, and appurtenances.” The form must be signed by the shipowner and if it is a corporation, its seal must be affixed.

14. Emphasis added.

15. A ship is divided into sixty-four shares and the title of each owner is distinct and indivisible. The shares may be owned by one or more persons but the number must not exceed sixty-four.

16. No. 56 of 1970. It came into force on 26 February 1971.

17. 57 & 58 Vict. c. 60.

Only a completed vessel can be the subject of a registered mortgage. Under the Act, a vessel under construction is not capable of being registered as a ship. Although an equitable mortgage can be created on a ship under construction, the question does not arise in the case under study since under the shipbuilding contract, as noted earlier, the property in the uncompleted vessel is not to pass to the shipowner. It may be noted that even where property is to pass before completion, the shipbuilder's possessory lien or unpaid vendor's lien,¹⁸ as the case may be, on the uncompleted vessel, is sufficient security.

Registration of mortgages is not compulsory. But the shipbuilder would be well advised to register the mortgage. For a mortgage which is not registered will rank subsequent to one which is registered even though the registered mortgagee has notice of the prior unregistered mortgage.

In the English case of *Black v. Williams*,¹⁹ Vaughan Williams J. held that although equitable interests in ships are recognized, a legal mortgage of a ship, in statutory form and registered, has priority over an equitable charge previously given, even where the legal mortgagee has notice of the charge.

As between registered mortgages, section 416C which was introduced by the 1970 Amendment Act provides:

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 book and not according to the date of each mortgage itself.²⁰

2. The Mortgage

The above account shows that all the shipowner needs to do to effect a mortgage on the vessel is to execute an instrument in the prescribed form or as near as circumstances permit (for the prescribed form, see next page). The instrument is then recorded in the register book.

As the shipowner under study is a company incorporated in Singapore, particulars of the mortgage are registered in the Registry of Companies as required under the Companies Act:²¹ failure to register would render the mortgage so far as the security thereby created is concerned void as against the liquidator and any creditor of the company.

18. Sale of Goods Act 1893, s. 41.

19. [1895] 1 Ch. 408.

20. Emphasis added.

21. Cap. 185, Singapore Statutes, Rev. Ed., 1970, s. 108(1).

FORM VIII

REPUBLIC OF SINGAPORE

MORTGAGE (TO SECURE PRINCIPAL SUM AND INTEREST)
(Body Corporate)

Official No.	Name of Ship	No., Year and Port of Registry	Whether a Sailing, Steam or Motor Ship
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Length.....	•Feet/Metres	Tenths	Horse Power of Engines (if any)
Breadth.....			Tonnage
Depth.....			Gross.....
			Register.....

and as described in more detail in the Certificate of the Surveyor and the Register Book

We.....in consideration of.....
 (\$.....) this day lent to us by.....do hereby for ourselves and our successors
 covenant with the said.....and.....assigns firstly That we or our successors
 will pay to the said.....or.....assigns the said sum of.....
 together with interest thereon at the rate of.....per cent per annum on the.....day of.....
 next, and secondly, that if the said principal sum is not paid on the said day, we or our successors
 will, during such time as the same or any part thereof remains unpaid, pay to the said.....
 or.....assigns interest on the whole of such part thereof as may for the time being remain
 unpaid, at the rate of.....per cent per annum by equal half-yearly payments on the.....
 day of.....and.....day of.....in every year; and for better securing to
 the said.....the repayment in manner aforesaid of the principal sum and interest
 we hereby mortgage to the said.....shares, of which we are the Owners in
 the Ship above particularly described, and in her boats, guns, ammunition, small arms, and appurtenances.
 Lastly, we for ourselves and our successors covenant with the said.....and.....
 assigns that we have power to mortgage in manner aforesaid the above-mentioned shares, and that
 the same are free from encumbrances.....

In witness whereof we have hereunto affixed our common seal this.....day of.....
 One thousand nine hundred and.....

The Common Seal of the

 was affixed hereunto in the presence of.....



Notes:

1. The prompt registration of a Mortgage Deed at the Port of Registry of the Ship is essential to the security of the Mortgagee, as a Mortgage takes its priority from the date of production for registration, not from the date of the instrument.

2. Registered Owners or Mortgagees are reminded of the importance of keeping the Registrar of Singapore Ships informed of any change of residence on their part.

*Delete as necessary

DEED OF COVENANTS

Under the system of registration in Singapore, unlike, for example, that in Panama or the United States, only the mortgage in the prescribed form is registered. This form contains brief particulars in regard to the shipowner (mortgagor), the ship, the mortgagee, the principal sum and interest. It is therefore not possible to register the terms and conditions pertaining to the mortgage. To overcome the deficiencies in the prescribed form of mortgage, a deed of covenants is executed to supplement the mortgage but it is a separate document and is not registrable.

The deed of covenants under consideration contains the following: covenant for payment and interest, description of indebtedness, scope of security, the statement that the mortgage is subject to the deed, covenants of the shipowner, insurance and renewals thereof, events of default and remedies and sundry provisions.

The main terms are summarised below:

1. Covenant for payment—the shipowner acknowledges the debt and covenants to pay the principal sum and interest thereon by the instalments at the times and in the manner as stipulated in or evidenced by the promissory notes.
2. Scope of security—the shipbuilder (mortgagee) is given a continuing security for the payment of all moneys due and payable by the shipowner (mortgagor). The security so created is not to be satisfied by any immediate payment or satisfaction of any part of the amount secured.
3. The shipowner covenants for itself, its successors and assigns and agrees with the mortgagee, its successors and assigns that the vessel and all the appurtenances, and all improvements and replacements, which may thereafter be made, are to be held by the mortgagee.
4. Covenants of the shipowner—the shipowner covenants that it will not cause or permit the vessel to be operated in any manner contrary to law, will not engage in any unlawful trade or violate any law or carry any cargo that will expose the vessel to penalty, forfeiture or capture and will not do, or suffer or permit to be done, anything which can or may injuriously affect the registration or enrolment of the vessel under the laws and regulations of the Republic of Singapore and will keep the vessel duly documented.
5. The shipowner will pay and discharge all taxes, assessments, governmental charges, fines and penalties lawfully imposed on the vessel or any income therefrom.
6. Except for the crew's wages or salvages, no other lien is to be created by the shipowner, charterer or master of the vessel.

7. The shipowner is required to have in the vessel, a certified copy of the mortgage and the deed so that they can be shown on request to all persons having business with the vessel which might give rise to any lien thereon other than liens for crew's wages and salvages. The shipowner is also required to place and keep prominently displayed, in the chart room and in the master's cabin of the vessel, a framed printed notice in plain type of such size that the paragraph of reading matter shall cover a space not less than six inches wide by nine inches high, reading as follows:

“Notice of Mortgage”

“This vessel is covered by a first statutory ship mortgage and deed of covenants collateral to such mortgage under the laws of the Republic of Singapore. Under the terms of said mortgage and deed of covenants neither the shipowner, any charterer, nor the master of the vessel nor any other person has any right, power or authority to create, incur or permit to be imposed upon this vessel any lien whatsoever other than for crew's wages and/or salvage.”

8. The shipowner undertakes to keep the vessel in good running order and repair; also, the shipowner will not make or permit to be made, any substantial change in the structure, type or speed of the vessel without the consent of the mortgagee.
9. During the period of the mortgage and the deed of covenants the shipowner is prohibited from selling, hypothecating, transferring, demising, chartering or abandoning the vessel without the written consent of the mortgagee.
10. The shipowner is required to insure the vessel in the joint names of the shipowner and the mortgagee for the full insurable value of the vessel and not less than 130% of the total balance of the mortgage debt remaining unpaid and interest. The insurance covers the following: marine perils; risks of war and fire by hull; machinery policies; port risk.
11. The shipowner will at its own expense have the vessel fully entered in a Protection and Indemnity Association or Club in good standing in both protection and indemnity clauses, or keep the vessel insured against protection and indemnity risks and liabilities by policies or certificates.
12. The interest of the mortgagee as mortgagee shall be duly endorsed or noted upon all ship's cover notes policies certificates of entry or other instruments of insurance issued in connection with such insurance or entry and each and every policy covered by these provisions shall contain a Loss Payable clause whereby any moneys due in respect of claims under the policy shall be payable to the mortgagee.
13. The proceeds of insurance for all losses, except for actual or constructive total loss, are to be paid to the shipowner unless

the shipowner is in default under the mortgage or the deed of covenants and the mortgagee has notified the insurer. In such a case the mortgagee is entitled to the insurance moneys and shall apply the proceeds according to clause 20 of the deed of covenants or at the option of the mortgagee to the payment of repairs, salvage or other charges.

14. In the event of an actual or constructive total loss of the vessel, the insurance proceeds is to be paid to the mortgagee or its assigns up to the total sums due under all of the promissory notes then outstanding and such other sums due to the mortgagee under the terms of the mortgage and the deed of covenants, together with accrued interest.
15. The shipowner undertakes to reimburse the mortgagee with interest, for any expenditure which the mortgagee may expend in providing such protection in respect to insurance, discharge of liens, taxes, dues, assessments, governmental charges, fines and penalties lawfully imposed, repairs, attorneys' fees and other matters as the shipowner is obligated but fails to provide.
16. Events of default and remedies — in the event of certain events such as default in payment of the loan, observance and performance of any of the covenants, or of the winding up of the shipowner, or where the shipowner ceases or threatens to cease to carry on business, arrest of the ship, appointment of trustee, liquidator or receiver, forfeiture of the vessel or any share therein, the mortgagee will have the following right to —
 - (a) immediate payment of all the outstanding promissory notes;
 - (b) exercise all the rights and remedies in foreclosure;
 - (c) bring suit at law, in equity or in admiralty, to recover judgment for any and all amounts due under the promissory notes or the mortgage;
 - (d) take possession of the vessel without the legal process and without being responsible for loss or damage;
 - (e) sell the vessel by public auction or private contract at any place and at such time as the mortgagee may specify.
17. A sale of the vessel made in pursuance of the mortgage or the deed of covenants whether under the power of sale or any judicial proceedings will operate to divest all right, title and interest of any nature of the shipowner. The shipowner, its successors and assigns lose all claims to the vessel. No purchaser is bound to inquire whether notice has been given, whether any default has occurred, as to the propriety of the sale or as to the application of the proceeds. The holder of the promissory notes may bid for and purchase such property, and upon compliance with the terms of sale may hold, retain and dispose of such property without further accountability.
18. If any legal proceedings are taken to enforce any right under the mortgage and the deed of covenants, the mortgagee will be

entitled as of right to the appointment of a receiver of the vessel and the freights, hire, earning, issues, revenues, income and profits due from the operation.

19. The shipowner covenants that, as and when all the promissory notes shall become due and payable and remain unpaid for 14 days, then the shipowner will pay to the mortgagee the whole amount due and payable on the promissory notes, for principal and interest, and should the shipowner fail to pay, the mortgagee will be entitled to recover judgment for the whole amount so due and unpaid, together with such further amounts as shall be sufficient to cover the reasonable costs and expenses of collection.
20. The proceeds of a sale of the vessel and the net earnings of any charter operation or other use of the vessel by the mortgagee under any of the powers given and any and all other moneys received by the mortgagee pursuant to or under the terms of the mortgage or the deed of covenants or in any proceedings hereunder, shall be applied as follows:
 - (a) to the payment of all expenses and charges, including the expenses of any sale, the expenses of any retaking, attorney's fees, court costs, and any other expenses or advances made or incurred by the shipowner in the protection of its rights or the pursuance of its remedies, and to provide adequate indemnity against liens claiming priority over or equality with the lien of the mortgage and the deed of covenants;
 - (b) to the payment of all the outstanding promissory notes in any order determined by the mortgagee, and accrued interest thereon to the date of full payment and of all other sums payable to the mortgagee hereunder or under the mortgage;
 - (c) to the payment of any surplus thereafter remaining to the shipowner or to whomsoever may be entitled.

If the proceeds are insufficient to pay the mortgagee, he is entitled to sue for the balance from the shipowner, or any other person liable therefor.

21. Sundry provisions — all the covenants, promises, stipulations and agreements of the shipowner in the mortgage and the deed of covenants are binding on the shipowner, its successor and assigns and are to inure to the benefit of the mortgagee, and its successors or assigns.

EVALUATION OF THE SECURITY ARRANGEMENTS

An evaluation of the security must take into account the nature of the ship as a collateral,²² the remedy *in rem* in the ship, the efficacy of the registered mortgage and the personal covenants under the deed of covenants.

22. "Collateral" refers to the subject-matter of the security device.

Nature of Collateral

One of the most important features of a ship, in determining its value as a collateral, is its seaworthiness. It is fortunate that the registry in Singapore requires a high standard of seaworthiness and only recognises the certificates²³ issued by surveyors of the following classification societies: Nippon Kaiji Kyoikai, Bureau Veritas, Det Norske Veritas, Germanische Lloyd, Lloyd's Register of Shipping and the American Bureau of Shipping. Although a newly-constructed vessel would be assured of seaworthiness when the mortgage is taken immediately on delivery, the fact remains that it is subject to rapid deterioration, wear and tear and obsolescence. Hence, the shipowner undertakes, in the deed of covenants, to maintain the ship in a seaworthy condition and to effect necessary repairs.

Another inherent weakness is that a ship is a floating collateral and once it sinks that is the end of it—it may then be either an actual or constructive total loss.²⁴ Apart from such a risk, there are a number of hazards and perils of the sea that might jeopardize the security. To safeguard the mortgagee, the insurance policy is required to contain a "Loss Payable" clause which directs the underwriter to pay all claims, with certain defined exceptions, to the mortgagee.

Risks Prejudicial to the Mortgagee

A ship trades from port to port. In the course of its voyages it may run into all kinds of risks which might render her liable to third parties and hence impair her ability to pay off the mortgage debt. Some risks such as those relating to oil pollution and liability for damage to cargo are not ordinarily insurable or are inadequately insured with insurance companies. But a Protection and Indemnity Association or Club will cover such risks.

The shipowner is required to enter the ship in such a club (see clause 11 of the deed of covenants noted above).

Priorities

Since the purchase of the newly constructed ship is financed by a mortgage at the time of delivery, the mortgage will be the first transaction recorded in the Register. Hence, no claim to priority of other registered mortgages can arise.

23. These are class certificates, tonnage certificate, safety construction, safety equipment, load line and safety radio certificates.
24. Actual loss occurs where the subject matter insured is completely destroyed so that it ceases to be the thing insured. A constructive total loss is one where the subject matter insured is reasonably abandoned on account of its actual total loss appearing to be unavoidable, or because it could not be preserved from actual total loss without an expenditure which would exceed its value. Where there is a constructive total loss the assured may either treat the loss as a partial one or abandon the subject-matter insured to the insurer and treat the loss as if it were an actual total loss. See the English Marine Insurance Act 1906, s. 61. The Act applies in Singapore under s. 5(1) of the Civil Law Act, Cap. 30.

Under section 416F of the Act a registered mortgage of the ship is not affected by an act of bankruptcy²⁵ committed by the shipowner (mortgagor) after the date of the record of the mortgage, notwithstanding that the mortgagor at the commencement of his bankruptcy had the ship in his possession, order or disposition, or was the reputed owner thereof. The mortgage enjoys preference over any right, claim or interest of other creditors of the bankrupt shipowner.

The above section does not apply where the mortgagor is a corporation. However, section 291(2) of the Companies Act applies the bankruptcy rules with regard to the respective rights of secured and unsecured creditors which will ensure that the mortgagee who is undoubtedly a secured creditor will be able to enforce and retain the benefit of his security against the liquidator.

Maritime Liens

A ship has a legal personality of its own and is capable of being sued *in rem*. The newly constructed vessel may subsequently be liable for maritime liens and the contest between the registered mortgagee and a maritime lien holder must be considered.

The Act is silent as to what a maritime lien is; it is also silent on the question of priorities between the registered mortgagee and the maritime lienholder. In the absence of any express provisions, the English law relating to maritime liens is applicable by virtue of the Second Charter of Justice, 1826.²⁶

A maritime lien has been described as "a claim against a ship or other maritime property which can be made effective by the seizure of the property in question".²⁷ The following characteristics have been attributed to it:²⁸ "(1) it is an inchoate right which adheres to the ship *eo instanti* of the incident giving rise to it, and an execution relates back to the instant of adherence for determination of its priority,"²⁹

25. See Bankruptcy Act, Cap. 18, Singapore Statutes, Rev. Ed., 1970, s. 3. S. 54 of the Bankruptcy Act, which protects *bona fide* transactions for value, may apply only where the available act of bankruptcy is committed before the mortgage and the receiving order is made after the mortgage. S. 416F applies where the available act of bankruptcy is committed after the recording of the mortgage and takes the mortgage out of s. 47(1) (b) (iii) of the Bankruptcy Act which may make the mortgaged ship available as the bankrupt's property by virtue of reputed ownership. See *The Ruby* (1900) 9 Asp. Mar. Law Gas. 146. But see *Halsbury's Laws of England*, 3rd ed., vol. 35, para. 140 and note (h).

26. This Charter extended the jurisdiction of the Court of Judicature of Prince of Wales's Island to Singapore and Malacca and there was a change of nomenclature. It contained the same provisions as the First Charter of 1807. In a number of decisions it was held that this Charter introduced the English law as it existed on 26 November 1826. See e.g. *Regina v. Williams* (1858) 3 Ky. 16.

27. Lord Chorley and Giles, *Shipping Law*, 5th ed., p. 33.

28. Wiswall, F.L. Jr., *The Development of Admiralty Jurisdiction and Practice Since 1800*, 1970, p. 167.

29. *The Bold Buccleugh*, (1850-1) 7 Moo. P.C. 267, 284-5.

(2) it may be extinguished prior to execution by payment in full satisfaction,³⁰ (3) it is not extinguished by fruitless actions *in personam*,³¹ (4) laches may prevent the execution of a maritime lien,³² (5) it may be extinguished by giving bail for the ship's release following arrest upon a warrant *in rem*,³³ and (6) it is completely executed by sale of the ship by order of the court pursuant to an action *in rem*³⁴ which sale vests a perfect and indefeasible title in the purchaser of the ship, free from all maritime liens, 'suits and claims of every kind'; and upon sale the liens released from the ship attach to and may be enforced against the proceeds of the sale while in the hands of the Court."³⁵

It is not altogether clear what are maritime liens apart from a few well-recognised ones, *viz.*, those created by bottomry³⁶ and *respondentia*,³⁷ salvage, seamen's and master's wages and their claims for wrongful dismissal, and the master's disbursements; there are also those created by tortious acts, such as collisions. Under English law, no maritime lien exists in the case of a ship repairer for the balance of the debt due to him.³⁸ Wiswall has remarked: "The entire subject of maritime lien seems to be a source of great confusion in English Admiralty at the present time...."³⁹

Under English law a maritime lien has priority over a registered mortgage even though it is created subsequent to it.

It is interesting to note that under the deed of covenants there is a prohibition against the creation of liens except for "crew's wages and/or salvage." These two liens are maritime liens and will enjoy priority over the registered mortgage. The deed excludes from the exceptions the other maritime liens which may rise from money due under a contract—a *bottomry bond* and a *respondentia bond*. It may be that these two types of liens seldom arise today as rapid means of communication render it unnecessary for the master to pledge the ship for necessities by means of such bonds to enable it to continue its journey. This might explain why they were omitted from the deed of covenants under study. Nonetheless, the provision in section 416D of the Act, that a mortgagor shall not be deemed to have ceased to

30. E.g. *William [Moake's] Money*, (1827) 2 Hag. Adm. 136.

31. Price, Griffith, *The Law of Maritime Liens*, 1940, p. 88.

32. E.g. *The Point Breeze* [1928] P. 135.

33. See, e.g., *The Point Breeze* [1928] P. 135.

34. See, e.g., *The Saracen* (1847) 2 W. Rob. 451.

35. Williams and Bruce, *Jurisdiction and Practice of the English Courts in Admiralty Actions and Appeals*, 3rd ed., p. 319.

36. A *bottomry bond* is a contract in writing by which the owner or master of a ship pledges the ship and cargo as security for a loan of money to enable her successfully to complete the voyage.

37. A *respondentia bond* is a hypothecation of the cargo only for the purpose of enabling the ship to complete her voyage.

38. *The Two Ellens*, (1872) L.R. 4 P.C. 161; *The Henrich Bjorn*, (1885) 10 P.D. 44.

39. *Op. cit.*, at p. 171.

be the owner of a mortgaged ship, except as far as may be necessary for making the ship available as a security for the mortgage debt, does not prevent the ship from being made the subject of a *bottomry bond* or a *respondentia bond*. The prohibition operates as breach of a personal undertaking between the shipowner and mortgagee for which the mortgagee may exercise his rights under clause 16 of the deed of covenants (noted above). But the lender on *bottomry bond* and on a *respondentia bond* may enjoy priority and thus impair the mortgagee's security.⁴⁰

Realisation of Security

Under section 416E(2) of the Act, a registered mortgagee is entitled to enforce his mortgage by an action *in rem* in admiralty⁴¹ 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. Subsection (1) of the above section empowers a registered mortgagee to dispose absolutely of the ship or share therein and to give effectual receipts for the purchase money.

The mortgagee's right to take possession, actual or constructive, is generally governed by the deed of covenants which accompanies the mortgage deed. Apart from the express provisions contained in the deed of covenants, the mortgagee can take possession if the mortgagor were to unduly impair the security by, for example, overburdening it with maritime liens so as to exhaust the value of the ship as security.⁴²

Section 416E(1) empowers the registered mortgagee to dispose of the ship or share therein. As the shipbuilder (in our study) is the first registered mortgagee, he will find his position intact as a second or subsequent mortgagee cannot sell without the concurrence of every prior mortgagee, unless he obtains an order of the High Court.

It is not always easy to dispose of the ship at a reasonable market price at a time when the shipowner is unable to pay its debts because the ship may be operating at a loss. For the value of the ship would largely depend on its earning capacity. Difficulties may also be encountered in seizing the ship as it may be at some place other than in Singapore at the moment when there is a need to realise the security.

As an alternative to disposing of the ship the mortgagee can operate it to recoup himself from the profits.⁴³ But this is not an attractive proposition as it involves attendant responsibilities: the mortgagee will have to honour all the existing legal obligations of the shipowner and has to meet all expenses for the operation of the ship. Although the mortgagee is entitled to recover from the profits of the enterprise, still,

40. But see *The Ripon City* [1897] P. 226; *The St. George* [1926] P. 217.

41. See s. 3(1)(c) of the High Court (Admiralty Jurisdiction) Act, Cap. 6, Singapore Statutes, Rev. Ed., 1970.

42. *The Manos* [1907] P. 339; *The Aline* (1839) 1 W. Rob. 111; *The Mary Ann* (1865) L.R. 1A & E. 8; *The Julinder* (1853) 1 Spinks 71.

it is too troublesome and will only be resorted to where the mortgagee is convinced that it is the only way out.

Finally, it may be noted that under the deed of covenants and section 416D, the mortgagee of a ship becomes entitled to all rights and liable to perform all the duties of an owner from the time of his taking possession. Amongst the rights so accruing to him is that of receiving all freight remaining due when possession is taken.⁴⁴ But he is not entitled to unpaid freight which became due before the date of his taking possession of the ship.⁴⁵ As the mortgagor remains the owner up to the time possession is taken he can bind the mortgagee by a charterparty.

B. SECURITY ARRANGEMENTS BETWEEN SHIPBUILDER AND BANKER.

The shipbuilder needs finance for his total operational costs of construction of a number of vessels at a given time. He also needs finance to sell on deferred payment terms.

The shipbuilder cannot carry the burden of financing and looks to the banker to provide both loan and banking facilities: the former type is used for financing the shipowner while the latter, for operational purposes.

The banker takes a fixed and floating charge over the shipbuilder's assets for the loan and banking facilities. Although the amount payable under the promissory notes issued by the shipowner is included in the above charge, nonetheless, the promissory notes are specifically endorsed over to the banker. The registered mortgage of the ship and such other security between the shipowner and the shipbuilder are also transferred to the banker.

Although the security for the loan and the banking facilities could be incorporated in one debenture, nonetheless, two debentures are executed, *viz.* one for loan and the other for banking facilities. The reason for this is that the banker may resort to another financier to finance part of the undertaking. As such, it would be convenient to have two debentures so that one of them could be assigned to the other financier, if need be.

Debenture for Loan Facilities

The debenture sets out, *inter alia*, the nature and purpose of the loan facilities, the disbursement schedule, the conditions precedent to

43. See *European and Australian Royal Mail Co. Ltd. v. Royal Mail Steam Packet Co.* (1858) 4 K & J. 676, where it was held that a mortgagee of a ship has power under s. 70 of the United Kingdom Merchant Shipping Act 1854 to use, as well as to sell, the ship. The section is in *pari materia* with s. 416E of the Singapore Merchant Shipping Act.

44. *Brown v. Tanner* (1868) L.R. 3 Ch. 597.

45. *Shillito v. Biggart & Anor.* [1903] 1 K.B. 683.

disbursement, payment of loans and interest, security, covenants, default in payment of expenses, security enforcement in certain events and right of consolidation.

The following are the main terms and conditions in the debenture under study:

1. *Conditions precedent before disbursement of loan:* the shipbuilder must have obtained from the shipowner of the vessel constructed and financed by the banker prior written consent to —
 - (a) execute promissory notes in favour of the shipbuilder and the subsequent endorsement on assignment to the banker, such promissory notes being in respect of the balance of the purchase price of each vessel payable by instalments after delivery of the same under the shipbuilding contracts made between the shipowner and the shipbuilder;
 - (b) execute in favour of the shipbuilder first statutory mortgages on the vessels and collateral deeds of covenants on terms and conditions acceptable to the banker and the subsequent transfer or assignment thereof to the bank;
 - (c) furnish to the shipbuilder such other security as the banker may require to cover 20%-30% of the contract price of the vessels, such security to be in one or more of the following forms:
 - (i) a first mortgage of one of the shipowner's vessels (other than the subject vessel) acceptable to bank;
 - (ii) a guarantee or an irrevocable letter of credit issued or confirmed by a first-class bank carrying on business in Singapore.
2. The debenture is secured by a fixed and floating charge over the property and assets of the shipbuilder.
3. Before executing any mortgage to be registered, the shipbuilder must disclose in writing to the banker the existence of any maritime lien, prior mortgages, or other liability in respect of the ship to be mortgaged which is known to the shipbuilder. Where the shipbuilder fails to comply with this requirement, the mortgage debt is, at the election of the banker, immediately due and payable, notwithstanding anything to the contrary in the mortgage. The onus is on the shipbuilder to disclose all prior encumbrances to the banker before executing a mortgage.
4. The banker is entitled to the right of consolidation of all the shipbuilder's accounts and liabilities with the bank.
5. The shipbuilder is to deposit with the banker all the deeds and documents of title relating to the security.
6. Where the banker makes a payment under guarantees in relation to the construction of vessel, the shipbuilder shall indemnify

the banker in full against all liability losses damages costs and expenses together with interest.

7. The shipbuilder is prohibited from making any other charges without the prior written consent of the banker.
8. *Covenants of the shipbuilder*: the shipbuilder covenants, *inter alia*:
 - (a) that the loans shall be used solely for the purpose stipulated;
 - (b) that the shipbuilder is to carry on business with due diligence;
 - (c) that the shipbuilder duly observe perform and comply with all the terms and conditions imposed under contracts entered into by the shipbuilder and in respect of which the banker has issued guarantees for their due observance performance and compliance by the shipbuilder;
 - (d) that the shipbuilder will furnish and provide the bank with and permit the banker to obtain all such information as the banker may reasonably require;
 - (e) that audited balance sheet and profit and loss accounts be submitted to the bank annually;
 - (f) that the shipbuilder shall not effect any form of reconstruction including amalgamation with another company without the prior written consent of the banker;
 - (g) that the shipbuilder will insure and keep insured all its property and assets comprised in the security against losses or damage by fire lighting burglary riots and such other risks as the banker may require to have insured.
9. *Security enforceable in certain events*: the principal loan or any part thereof outstanding, together with interest, and the security created are to become enforceable in the event of the following:
 - (a) if the shipbuilder defaults for 14 days in the payment to the banker of any one of the instalments of any loan;
 - (b) if the shipbuilder ceases or threatens to cease to carry on its business;
 - (c) if a distress or execution of writ of seizure and sale or attachment is levied upon or issued against any of the property or assets of the shipbuilder and remains unsatisfied for 7 days;
 - (d) if a receiver is appointed of the shipbuilder's property assets or undertaking;
 - (e) if an order is made or a resolution is passed for winding up the shipbuilder other than for the purpose of reconstruction or amalgamation to which the banker has given its prior written consent;

- (f) if the shipbuilder commits or threatens to commit a breach of any of the covenants undertakings stipulations terms conditions and fails to remedy it within 7 days after notice from the banker;
 - (g) if in the opinion of the banker the security or the business of the shipbuilder is in jeopardy.
10. *Assuming control of shipbuilder's assets:* where moneys are payable in the circumstances above stated, the banker or any person authorised by it may enter into the land or premises of the shipbuilder without notice and may take possession and control of such premises and all goods merchandise plant machinery books of account documents of title or other movable property and may take possession and control of any other such property belonging to the shipbuilder as may be found in any other place without being liable as a mortgage in possession. A receiver would then be appointed for the purpose of realising the security.
11. *Application of moneys by receiver:* the net profits of carrying on the business and the net proceeds of any sale shall be applied by the receiver subject to the claims of all secured or unsecured creditors ranking in priority to this debenture:
- (a) firstly, towards payment of all costs charges and expenses of and incidental to the appointment of the receiver, including the reasonable remuneration of the receiver;
 - (b) secondly, payment to the bank of all interest remaining unpaid on the balance of the sum owing to the bank;
 - (c) thirdly, in or towards payment of all principal moneys and other sums due to the bank;
 - (d) fourthly, any surplus is to be paid to the shipbuilder.
12. *Right of consolidation:* Section 21(1) of the Conveyancing and Law of Property Act⁴⁶ is to be excluded from the debenture.

Debenture for Banking Facilities

The debenture for banking facilities is secured by way of a second floating charge on all the current assets of the shipbuilder including its goodwill and uncalled capital raw materials works in progress finished products and book debts, and is to rank immediately after the floating charge created in favour of the bank under the debenture for loan facilities for the financing and construction of vessel and the sale of the same on deferred payment terms.

The terms and conditions of this debenture are very similar to those of the first one. However, there are no conditions precedent to the disbursement of money from banker, as there are under the debenture for loan facilities. This is because, unlike a loan debenture which

46. Cap. 268, Singapore Statutes, Rev. Ed., 1970.

is to secure a term loan which the banker is obliged to honour, the banker under the debenture for banking-facilities can at any time discontinue granting the facilities. As the banker can control its grant, there is no necessity of requiring stringent conditions in the form of "conditions precedent". In any case, a banker who is granting the loan facilities may also be the one granting banking facilities. Hence, there is no necessity of having conditions precedent in the latter debenture.

The rule in *Clayton's* case⁴⁷ may operate against the banker who grants overdraft facilities. Suppose the banker, who has the first statutory mortgage for overdraft facilities, were to have notice of a second statutory mortgage, he cannot claim priority over the second statutory mortgage for subsequent payments. And to avoid the operation of the rule in *Clayton's* case, he should cancel the shipbuilder's account and open a separate account. The following clause is found in the debenture:

If the shipbuilder were to create any further or subsequent mortgage, charge or incumbrance fixed or floating over or otherwise deal with any of the property or assets comprised in the security in favour of any other person, the bank may on receiving such notice open a new or separate account with the shipbuilder and if the bank does not in fact open such new or separate account the bank shall nevertheless be deemed to have done so at the time when the bank received or was deemed to have received such notice. And all payments in account made from and subsequent to the notice by the shipbuilder shall be placed to the credit of the new or separate account and shall not go in reduction of the amount owing by the shipbuilder to the banker at the time of notice.

C. CONCLUSION

Whatever weaknesses there may be in a ship as a collateral, the banker is reasonably well secured by the fixed and floating charge and other security over the assets of the shipbuilder. In the event of a financial collapse of the shipowner, it would be the shipbuilder rather than the banker who would suffer. But this is a calculated risk which, so far, has proved to the Singapore shipbuilder to be worthwhile.

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47. (1816) 1 Mer. 572.

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