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Sales *pendente lite* and direct sales

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Introduction

1. This paper attempts to outline the principles applicable to an order for the sale of a ship before judgment, but after arrest, and discusses the evidence that might be needed in support of such an application. The paper then discusses the approach that has been taken in a number of courts to applications for a direct sale.
2. The Rules clearly contemplate that an order for sale may be made before judgment. Rule 69 of the Admiralty Rules provides:
 - (1) The court may, on application by a party to a proceeding and either before or after final judgment in the proceeding, order that a ship or other property that is under arrest in the proceeding:
 - (a) be valued;
 - (b) be valued and sold; or
 - (c) be sold without valuation.
 - (2) An application for valuation or sale of a ship or other property shall be in accordance with Form 26.
 - (3) An order for valuation or sale of a ship or other property shall be in accordance with Form 27.
 - (4) An application under subrule (1) constitutes an undertaking by the party who made it to pay, on demand, to the Marshal an amount equal to the amount of the fees and expenses of the Marshal in complying with the order.
 - (5) If the ship or other property is deteriorating in value, the court may, at any stage of the proceeding, either with or without application, order it to be sold.
3. Such an order may only be made by the Admiralty judge and not by the Registrar.

The principles applicable to an application for a sale *pendente lite*

4. A court should not make an order for the appraisalment or sale of a ship *pendente lite*, whether or not the action is defended, except for good reason (*The Myrto* [1977] 2 Lloyd's Rep 243, 260; *The Guiseppe di Vittorio* [1998] 1 Lloyd's Rep 661).
5. The principles applicable to such an order were identified by Brandon J in *The Myrto* [1977] 2 Lloyd's Rep 243.
 - Normally an order for sale before judgment will be sought only where there is default of appearance or defence. In such circumstances, it is common practice for the court to make an order on the basis that the security for the claim will be diminished by the continuing costs of maintaining the arrest to the disadvantage of all those interested in the ship.

- If the action is defended, then the court will examine the question of whether there is good reason for making the order more critically, and a significant factor influencing that decision will be the effect of maintaining the arrest on the value of the claimant's security (*The Gulf Venture* [1985] 1 Lloyd's Rep 131; *Marinis Ship Suppliers Pty Limited v The Ship Ionian Mariner* (1995) 59 FCR 245; *Bayside Air Conditioning Pty Ltd v The Owners of the Ship Cape Don* [1997] FCA 690; *The Beluga Notification* [2011] FCA 665). This is true even where the claim is vigorously defended, as it was in *The Cape Don*, but where, on all the evidence it was deteriorating, was held under AMSA detention, required substantial sums to bring it up to a state where it could be moved to another port, and the owner was not contributing to any expenses. Cooper J held that the interests of creditors general, of the owner, and of the claimants against the vessel were best served by ordering appraisal and sale *pendente lite* so that the funds may be paid into court for the benefit of all parties interested in them.
 - Subrule (5) is not predicated on a requirement of affirmative proof that the ship is deteriorating in value. Even if a ship is being maintained by the crew in accordance with the maintenance schedules, it is inevitable that there will be some deterioration in condition by reason of rust below the waterline and other factors affecting the hull that cannot be arrested until the next dry-docking. Secondly, in the absence of evidence of a rising market or ships of the particular age or type, the natural inference is that there will be some depreciation in value, merely by the passage of time, even with full and adequate maintenance (*Marinis Ship Suppliers Pty Limited v The Ship Ionian Mariner* (1995) 59 FCR 245).
6. Where a vessel is sold *pendente lite*, it is still the Marshal who must appraise the vessel and advertise and invite offers for the sale of the vessel.

Evidence in support of an application for sale *pendente lite*

7. Evidence in support of such an application might include:
- (1) the overall value of the claim;
 - (2) the number of caveats against release and other claims against the ship and their likely value;
 - (3) the value of the ship and its likely diminution in value during the course of the arrest;
 - (4) the costs of maintaining the vessel's arrest, including such costs as port and berth charges, ship's keeper, crew wages and emoluments, supply of domestic fuel to the vessel, and so on, and the consequent diminution in the claimant's security;
 - (5) any (prospect of) deterioration in the condition of the ship;
 - (6) any necessary work to be done on the ship either to keep it afloat or to enable it to be moved;
 - (7) the unwillingness of the shipowner to contribute to the costs of the arrest;
 - (8) the financial position of the shipowner and his unwillingness or inability to provide security for the ship's release;
 - (9) the likely intervention of claimants with higher priority;
 - (10) humanitarian considerations in relation to the crew;
 - (11) whether, if the claimant obtains judgment in his favour, the judgment can be satisfied by the defendant without the need to sell the ship in any event.

Private sale before order

8. At any time up until an order for sale is made, the shipowner is at liberty to arrange for its sale. Even if such a sale is made, the ship will remain under arrest and subject to the claim upon it. In *The Monmouth Coast* (1922) 12 Ll L Rep 22, the court approved a private sale but on condition that the proceeds of sale be paid to the Marshal on account of his expenses. Once an order for sale has been made, however, it is a contempt of court for the owner to attempt to sell the ship (*The Ruth Kayser* (1925) 23 Ll Rep 95; *The Jarvis Brake* [1976] 2 Lloyd's Rep 320, [1976] 2 All ER 886; *The APJ Shalin* [1991] 2 Lloyd's Rep 62).

Applications for a direct sale

9. The economic climate has, in recent years, encouraged a spate of applications by mortgagees for a directed sale of the arrested ship in order to attempt to minimise the costs that accrue between arrest and sale. The question of whether an order for a direct sale should be made is important; it goes to the question of whether such a sale retains its character as a "judicial sale" sufficient to convey clean title to the purchaser. It is perhaps worth noting however that, were the CMI *Draft Instrument on the Judicial Sale of Ships* to be promulgated, it is likely that a direct sale would fall within the definition within that Instrument, being:

any sale of a ship accomplished by the competent court or under the control of a State by way of public auction or private treaty or any other appropriate ways provided for by the law of a State where the judicial sale takes place by which clean title of the ship is given to the purchaser and the proceeds of sale are made available to the creditors.

10. Such applications have generally been refused by courts on the basis that "powerful special features" or "special circumstances" would need to be shown before such an application were acceded to. Absent those circumstances, the court will not order the Marshal to sell to a purchaser found by the arresting party, even if the proposed price appears to be at or around the market value for the vessel (*Bank of Scotland Plc v Owners of the Union Gold (The Union Gold)* [2014] 1 Lloyd's Rep 53). There seems to be some misunderstanding, at least amongst some academic commentators (see for example Zournatzi, 'A Convention on judicial sale of ships?' *Shipping and Trade Law* 5 May 2016), to the effect that these types of applications are granted as a matter of course in England, Singapore and Hong Kong such that, "in common law jurisdictions the time period between arrest and sale may be as little as a few weeks" if the mortgagee makes such an application. But as Teare J held in *The Union Gold* [20]:

...it is wrong in principle for the court to depart from the usual order that the Marshal sell a vessel by appraisal, advertisement and inviting bids to purchase the vessel...it may give the impression that the Marshal is acting for a particular claimant in rem rather than as an officer of the court who must have regard to the interests of all claimants in rem and of the defendant shipowner.

11. The decision in *The Union Gold* reflects sentiments voiced by Waung J in the earlier Hong Kong case of *The Margo L* [1997] HKEC 767 and a much earlier decision of the Canadian Federal Court in *International Marine Banking Co v Dora (No 2)* [1977] FC 603.

12. In *The Turtle Bay* [2013] 4 SLR 615, Ang J of the High Court of Singapore agreed with Teare J but went on to observe that, in seeking the court's sanction of a private direct sale as an admiralty judicial sale, a party is essentially seeking to attract the benefits and advantages of a judicial sale, while retaining the liberty to sell the vessel to a party of its choice and at a price agreed between the two parties. Whilst acknowledging that such orders had been granted in the past, Ang J cautioned that, "it would be misguided to think that from those instances there now existed in Singapore an established practice of the court, in exercise of its admiralty jurisdiction, to sanction private direct sales of arrested vessels as judicial sales."
13. In *The Sea Urchin* [2014] SGHC 24, Ang J was similarly unpersuaded to make an order for a direct sale. It was argued by the mortgagee that the direct sale of the Vessel to a named buyer at a specified price was necessary to enable the Vessel under new ownership to carry the cargo (soya beans) to China. Ang J distinguished the circumstances in *The Union Gold* and *The Nel* in concluding that without satisfactory evidence as to her value, the Bank's assertion that the value of the security represented by the Vessel would be progressively reduced by the costs of maintaining her under arrest (even with the presence of a perishable, and perishing, cargo) was not made out and that the offer to employ the crew members, by itself, did not constitute a "special circumstance".
14. The submission was made in *The Sea Urchin* that the high cost of discharging the cargo was a factor that should be taken into account by the court given, so the submission went, that this would reduce the sale proceeds available to the *in rem* creditor. Ang J, with respect correctly, dismissed the submission on the basis that as a matter of general principle, the costs of discharging cargo are not part of the Marshal's expenses and, as such, are an irrelevant consideration in determining whether to allow a direct sale. Her honour referred to the decisions of Sheen J in *The Jogoo* [1981] 1 WLR 1376, Harrington J of the Federal Court of Canada in *The MCP Altona* (2013) 225 ACWS (3d) 292, and Cons J of the Supreme Court of Hong Kong in *The Mingren Development* [1979] HKCU 19.
15. Special features were shown to exist in relation to one of the four vessels for which a direct sale was sought in *The Union Gold*. The characteristics of the *Union Pluto*, which persuaded Teare J to direct a sale on the application of the mortgagee, included:
 - the age of the vessel (built in 1984)
 - its value of €315,000
 - the buyer was in a position to retain and operate the long-term contract which provided business for *Union Pluto* and other vessels and employed 21 crew
 - the bank's claim against *Union Pluto* was €13.5m and none of the other claimants had a higher priority than the bank
 - the proposed buyer had a particular reason to buy the vessel and unless a sale took place immediately there was a risk that that reason would disappear.
16. In Canada, orders approving direct sales have been granted where the evidence is that the vessel is losing value, timing is essential to obtaining the best possible price, and there is convincing evidence that prior efforts to sell the vessel have not led to higher offers. In *Bank of Scotland v The Nel* (1997) 140 FTR 271, the Vessel had a cargo of sulphur on board that was to be shipped from Vancouver to Tunisia. The cargo was the extraordinary circumstance in that case; the court observing that should there be corrosion, the vessel's seaworthiness would be affected thus making it difficult to sell at a good price. There was evidence that that

the vessel “could well, within weeks and certainly months, become unsaleable except as scrap or at a minimal speculative price” [16]. The court observed that:

[10] ...In addition to the sulphur being aboard the vessel for some six weeks here in Vancouver with, as I have said, warmer than usual temperatures, she still had to complete her voyage. A usual voyage from Vancouver to Tunisia, not taking into account delays at the Panama Canal and delays in discharge at Tunisia, would take about 26 days, assuming a speed of 15 knots. Taking into account that most of the voyage from Vancouver, through the Panama Canal, to Tunisia would take place in sub-tropical and tropical climates, the concern of a corrosive reaction, between steel plate and wet sulphur, was a real and valid concern...

17. In *Offshore Interiors Inc v Worldspan Marine* (2014) FC 655, the following factors persuaded Mosley J that “it is fair just and in the interests of all concerned that the [directed] sale of the Vessel be approved”:

- the Vessel had been under arrest for four years
- the value of the Vessel had already substantially deteriorated since its arrest
- At least 25% of the work required to complete the build remained to be done
- the Vessel had been aggressively marketed, without success, for several years; the market for super yachts is very specialised; a vessel of this nature had a very limited market; the evidence is that further advertisement or other marketing efforts would not produce a prospective buyer at a price greater than that on offer
- any potential purchaser faced considerable risk due to the complexity and cost of completion.

Summary

18. An application for sale *pendente lite* can be made whether the claim is defended or not, where it is clear that the security for the claim will be diminished by the continuing costs of maintain the arrest to the detriment of all who are interested in the ship.
19. Cogent evidence of a variety of factors will be important to persuade a court to make such an order.
20. There is no emerging trend in favour of orders for direct (or directed) sale of ships under arrest and, in principle, they should be avoided unless there are compelling circumstances analogous to those that arose in *The Nel*.
