

An Introduction to Cross-Border Maritime Insolvency

As has been observed, insolvency law is tricky enough to navigate in the context of domestic insolvency proceedings brought against companies registered and operating in the forum. Where foreign companies and/or windings-up are involved, they are murky and treacherous and must be navigated with care.¹ However, it is impossible to ignore the interaction between the admiralty process and insolvency proceedings, however underdeveloped that interaction may be – as to which Thomas put the position aptly:²

The law of [insolvency] seems to have developed with little regard to the Admiralty proceeding *in rem*. Certainly it is difficult to fit the Admiralty proceedings into the legislative language of the relevant statutes which regulate [insolvency proceedings]. Yet the need for the latter to accommodate the action *in rem* and the potential conflict between the two processes is plain. A *res* may concurrently be the subject of an arrest in the Admiralty Court and an asset capable of liquidation in [insolvency proceedings]. In such a circumstance it is important for a maritime claimant to be able to ascertain whether it is the jurisdiction of the Admiralty Court or some other court which prevails and which mode of legal process is available for the satisfaction of the claim.

CMI has as one of its main aims the harmonisation of maritime law. By harmonisation we do not necessarily mean uniformity. We aim, however, for a level of “predictability” in the application of maritime legal principles internationally wherever a dispute may fall to be determined. What is peculiar to maritime law is the centuries old interconnection between the international parties involved in international transactions and enterprises and the consequent juxtaposition of national and transnational laws which are all required to deal with similar legal issues. Consequently, since the earliest days of sea trade there has developed a remarkable homogeneity in maritime law around the world so that maritime parties can expect their legal disputes to be dealt with on relatively similar footings, whether they are seeking to resolve their dispute in Australia, Hong Kong, China, France, Argentina or wherever.

¹ Derrington & Turner, *The Law & Practice of Admiralty Matters* (OUP, 2006), 200.

² D R Thomas, *Maritime Liens* (1980), para 99.

Now, the same is not true of most other areas of the law, where international conventions and bilateral and multilateral treaties have been superimposed on areas of the law that have only relatively recently become international in character, without the benefit of centuries of organic development.

The Model Law on Cross-Border Insolvency

Cross-border insolvency is one such example. Indeed, it was not until the recession of the late 80s that states turned their minds to the need for such an international convention. The *Model Law on Cross-Border Insolvency* represents an attempt to impose a universalist approach.

In the Asia-Pacific region, it has been adopted only by the US, Australia (*Cross-Border Insolvency Act 2008*), New Zealand, Korea and Japan but notably not in Hong Kong. It is enacted in Canada, although Canada has not proclaimed the Model Law. If one compares this number with the more than 100 parties to the Hague Rules, we can see that the *Model Law on Cross-Border Insolvency* has some way to go to catch up with uniform régimes in maritime law. Nonetheless, the promulgation and adoption of the Model Law is yet another example of what we might call newcomers to transnational law seeking to impose uniformity on an area of law without regard to maritime law as a whole or to whether uniformity is in fact necessary to achieve a coherent and harmonised system of law.

Article 1 of the Model Law provides that the Law applies where:

- (a) Assistance is sought in this State by a foreign court or a foreign representative in connection with a foreign proceeding; or
- (b) Assistance is sought in a foreign State in connection with a proceeding under [a law of the enacting State in relation to insolvency];
- (c) A foreign proceeding and a proceeding under [a law of the enacting State in relation to insolvency] in respect of the same debtor are taking place concurrently; or
- (d) Creditors or other interested persons in a foreign State have an interest in requesting the commencement of, or participation in a proceeding under [a law of the enacting State in relation to insolvency].

Article 4 provides:

The functions referred to in the present Law relating to recognition of foreign proceedings and cooperation with foreign courts shall be performed by [the courts competent to provide those functions in the enacting State].

The recognition of foreign insolvency proceedings as “main proceedings” gives rise to an automatic stay which will apply to certain types of creditor actions including: the commencement of proceedings concerning the debtor company’s assets, rights, obligations or liabilities; execution against its assets and/or the transfer or disposal of its assets.³ The Model Law makes no specific reference to admiralty claims but makes reference to the preservation of rights *in rem* in Article 32 which preserves, to some extent, the position of secured claims or rights *in rem*.

If a State has enacted the Model Law, the logical order of enquiry as to its impact, if any, on *in rem* proceedings is as follows:

- (1) *Whether there is a foreign proceeding and/or a foreign main proceeding.*

A foreign proceeding is a judicial or administrative proceeding pursuant to a law relating to insolvency; a foreign main proceeding means a foreign proceeding taking place where the debtor has the centre of its main interests.⁴ This would normally be the place of its registered office although the term is not defined.

- (2) *Whether an application has been made to the court for recognition of the foreign proceedings in which the foreign representative has been appointed.*

A foreign representative means a person or body, including one appointed on an interim basis, authorized in a foreign proceeding to administer the reorganization or the liquidation of the debtor’s assets or affairs or to act as a representative of the foreign proceedings.⁵

- (3) *Whether the application has been brought in accordance with Article 15(2).*

³ Article 20.

⁴ Article 2.

⁵ Ibid.

Prior to the Model Law, the relevant question was whether the forum where the *in rem* action is proceeding will recognise the foreign liquidation.⁶ In general terms, a foreign liquidation would be recognized if the shipowner was incorporated or traded in the jurisdiction in which the liquidation is being conducted (or if the law of its incorporation would recognise the liquidation), or if it submitted to the jurisdiction of the foreign court.⁷ There is little room left for the exercise of any discretion as to whether or not to recognize the foreign proceedings.⁸

(4) *The consequences of recognition.*⁹

Article 20 provides that upon recognition of a foreign proceeding that is a main foreign proceeding:

- (a) Commencement or continuation of individual actions or individual proceedings concerning the debtor's assets, rights, obligations or liabilities is stayed;
- (b) Execution of the debtor's assets is stayed;
- (c) The right to transfer, encumber or otherwise dispose of any assets of the debtor is suspended.

The Model Law does not define the term 'execution.' It has been held in the Australian case of *Danny Morris & Anor v The Ship "Kiama"*¹⁰ that the arrest and subsequent sale of a ship pursuant the judicial order of an admiralty court does not amount to a process of execution. The English authority on this precise issue is unsettled. It was held in *In re Australian Direct Steam Navigation Company*¹¹ and *The Constellation*¹² that a sale following an arrest is the equivalent of execution within the meaning of the Insolvency Act. The contrary view was reached in *The Zafiro*¹³ and it was the latter view that found favour with Carr J in *The Kiama* on the basis that, "...as a matter of law, the arrest of the

⁶ *Felixstowe Dock & Rly Co v United States Line Inc* [1989] QB 360; *Banque Indosuez SA v Ferromet Resources Inc* [1993] BCC 112; *Fournier v The Ship "Margaret Z"* [1997] NZLR 629; *Turners & Growers Exporters Ltd v the Ship Cornelis Verolme* [1997] 2 NZLR 110.

⁷ Smart, *Cross-Border Insolvency*, (2nd edition, 1998), p 182. See, too, Dicey & Morris, *The Conflict of Laws*, § 30R-091f.

⁸ Article 17.

⁹ Articles 20-21.

¹⁰ [1998] FCA 256.

¹¹ 1875) LR 20 Eq 325 .

¹² [1966] 1 WLR 272.

¹³ [1960] P 1.

ship did not occur as part of a process of execution. It came about at the behest of the plaintiffs in accordance with the Admiralty Rules.”

Where, however, no security has been obtained over a ship at the time when a foreign winding-up order is made, the result is likely to be that the maritime claimant will be unable to bring *in rem* proceedings, and – unless the foreign court grants permission to sue *in rem* – will be limited to proving in the foreign liquidation. This is, in part, because a court exercising admiralty jurisdiction will not be a court exercising jurisdiction pursuant to a law relating to insolvency and so admiralty proceedings, of themselves, cannot be “foreign proceedings” within the definition of Article 2 of the Model Law. It may have been desirable had the Model Law included a provision along the lines of Article 5.1 of the EU Insolvency Regulation, which provides that:

The opening of insolvency proceedings shall not affect the rights *in rem* of creditors or third parties in respect of tangible or intangible, moveable or immoveable assets ... belonging to the debtor which are situated within the territory of another Member State at the time of the opening of proceedings.

However, it will be noted that this provision only operates where the relevant asset is elsewhere within the EU when the (winding up) proceedings are commenced, which may very well not be the case in relation to a ship. In any other case, the ranking of claims is a matter for the law of the court in which the liquidation is proceeding.¹⁴ That means of course that there may be very different and often less desirable priority determinations for *in rem* claimants.

Insolvency law differentiates between a stay of proceedings in liquidation, where, as it were, the bar comes down to stop the race among creditors, and creditors’ claims can then be swiftly and economically valued and the company’s assets distributed to the creditors. In contrast, where a company is placed in administration, the purpose of a stay is to enable the company’s business to survive as a going concern, by stopping its creditors from destroying the assets and selling them to satisfy its debts.

Where a ship is involved, a stark difference of approach emerges. We have on the one hand, maritime law’s reliance on the *res*, which can be arrested and used to recoup the debt, and which is broadly

¹⁴ art 4.2(i).

understood by all ships' creditors, especially financiers, as the primary source of the security. On the other hand, we have the emphasis that insolvency law places on protecting the interests of creditors. The lack of understanding of the interaction between admiralty and insolvency is neatly illustrated by the Canadian case of *Holt Cargo Systems Inc v ABC Containerline NV (Trustees of)* [2001] 3 SCR 907. In that case, the Bankruptcy Court in Canada, in effect, framed an anti-suit injunction to prevent the parties proceeding in the Federal Court of Canada to dispose of a ship that had been arrested.

The aim was to send the proceeds of the ship back to Belgium to satisfy the creditors in the Belgian liquidation. Happily, the Supreme Court of Canada made clear that the maritime jurisdiction was not obliterated by the supervening bankruptcy, and held that the Bankruptcy Court ought not to have made such an order.

In Australia, when the *Cross-Border Insolvency Act 2008* is invoked in an administration, creditors will be prevented from taking any action against any of the company's ships for the duration of the administration. This is a powerful weapon which may enable shipping companies to keep its ships trading and free from arrest, and as has been noted by Douglas Lindsay in *The Maritime Advocate*, the use of this provision could fundamentally alter the marine world, accustomed as it is to treating arrests and the Admiralty Marshal's sale of a vessel as the source of last recourse. He says:

If this is now denied to creditors, including banks, we may have to start again from scratch in working out how financial redress is obtained in the maritime world.

There are already several examples of the difficulties that might arise in the application of the cross-border insolvency laws to maritime claims. One such example arose in *Harms Offshore AHT 'Taurus' GmbH & Co KG v Bloom* [2009] EWCA Civ 632; [2009] All ER (D) 276 – a decision of the English High Court. The case involved an offshore oil and gas company incorporated in the UK which chartered the appellant's vessels "Taurus" and "Magnus" pursuant to charter parties that were subject to English law and that contained a London arbitration clause. The company went into administration, and the Companies Court made an order authorising the administrators to enter into a loan agreement with specified lenders to raise funds for the post-administration liabilities.

Without notice to the administrators, the appellants obtained a Rule B attachment order in the New York District Court, thereby attaching the loan moneys that had been authorised to be raised by the English Court. The administrators sought an order vacating the attachments on the basis that the Bankruptcy Court in New York should recognise the administration order under principles of comity embodied in Chapter 15 of the *US Bankruptcy Code*. Simultaneously, the administrators sought relief in the English High Court which granted them an injunction restraining the appellants from taking steps in the substantive proceeding commenced in New York.

In this case the conduct of the appellants could be considered to be wholly unconscionable, and so the injunction was probably rightly granted, but what is of concern is the comment made by the English Judges. They said [26]:

The question is not as to where a dispute as to liability or damages should be determined, but whether the appellants should be able to secure the benefit of their attachments, and thus promote themselves from unsecured to secured creditors.

This is the very point of the action *in rem*: maritime claimants can promote themselves to secured creditor status. It strengthens the view expressed in the note in *The Maritime Advocate*, referred to above, that maritime creditors may now need to rethink the basis of their underlying security. The result will now be in many cases that maritime creditors will be unable to commence *in rem*, and will be limited to proving in the foreign liquidation. This is illustrated by the decision of Justice Sotomayor in *In re Millenium Sea Carriers Inc* 419 F 3d 83 (CA2: 2005).

Personal Property Securities regimes

It is not only the Model Law which does and will impact on the interaction between insolvency and admiralty law. An increasing number of States are enacting legislation, derived from the US Commercial Code, in relation to personal property securities.¹⁵

¹⁵ eg: *Personal Property Securities Acts* in various Canadian provinces; *Personal Property Securities Act 1999* (NZ); *Personal Property Securities Act 2011* (Cth of Australia).

These particular pieces of legislation tend to look to the substance, not form, of a security interest and will impact on the very existence of maritime claims in the event of insolvency, as well as on the ranking of priorities.

The legislation raises such issues as:

- whether the right of an insurer to take over maritime property the subject of a notice of abandonment under the constructive total loss provisions of the *Marine Insurance Act* is a security interest which must be registered in order to be enforced?
- whether a charterparty lien, a salvor's lien or a warehouseman's lien needs to be registered to be enforceable and attract priority
- the need to register mortgages and charges of ships and property associated with ships
- the need to register charters of vessels for an indefinite term or in excess of specified periods (usually 90 days) as they will be held to be security interests
- whether other charters might also be considered security interests.

Conclusion

In light of these, and no doubt many other issues of concern to particular States, it is the view of the working party that it is timely to survey the position of all member States with the object of ascertaining whether there is any scope for sensible harmonisation of the approach to the interaction between insolvency and admiralty law.

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