

CMI 2012 Beijing Conference Judicial Sales of Ships

Judicial Sale of Ships in Germany

– As an example for a Civil Law Concept –

Introductio

The following presentation is a brief summary of the Judicial Sale of Ships in Germany. All of us being advisors to the maritime industry in various aspects do face these days a rather difficult situation in the shipping industry. Depressed values of ships, low freight markets, overcapacity, lack of equity and banks withdrawing their engagement in ship finance do create a situation where shipowners may be forced into Judicial Sale of ships. The instrument on Recognition of Foreign Judicial Sale of Ships comes at a time where, even if many of our clients do not like the idea, where the Judicial Sale of Ships is day-to-day business to various banks and maritime lawyers. We are talking about a current problem and the approach to unify the procedure and acceptance of Judicial Sale procedures.

The following issues are considered in order to outline the procedure of a Judicial Sale in Germany:

- Enforceable Title
- Valid Service
- Court Order of Enforcement
- Safe-custody of the Vessel
- Announcement of Auction
- Transfer of Title
- Distribution of the Proceeds.

As you all know, Germany follows the Civil Law Concept and therefore there are some substantial differences to the procedures in a Common Law Jurisdiction.

German Law has a specific Code dealing with the Judicial Sales of Ships, which is the ZVG (Enforcement Act). The Judicial Sale follows in general the same legal procedure as a Judicial Sale of immovable property. There are, however, a few specific provisions in the Enforcement Act with regard to the Judicial Sale of Ships which do apply in addition to the general provisions. This is stipulated in Sections 162-171 ZVG (Enforcement Act). I will come to this later.

1. Enforceable Title

a. Court Judgement and Arbitration Award

The condition precedent to start Judicial Sale proceedings in Germany is an enforceable title of the Creditor against the Owner of the vessel. If a German judgement is obtained and becomes final and binding there is no doubt that this would comply with the requirements of an enforceable title. Furthermore, there is no doubt that a judgement from an EU-member state being declared enforceable in Germany under the simplified procedure falls into this category as well. It becomes more interesting for judgement of Non-EU member states which have to go through an enforcement procedure in Germany. If they have been declared by a Court in Germany being enforceable they do also qualify to commence Judicial Sale proceedings.

The situation with regard to arbitration awards is similar and it depends if the arbitration award has been declared enforceable in Germany by a German Court. A settlement agreement is not an enforceable title. It could become, however, an enforceable title if there is an acknowledgement of debt included notarized by a German Notary Public or if the settlement agreement is made in Court and recorded by the Court reporter.

Excursus: "Acknowledgement of Debt"

German ship finance banks make use of this document. Part of the security documentation to be provided by the Shipowner is an acknowledgement of debt which is declared enforceable against the Shipowner and notarized by the Notary Public. The advantage for the bank is that they do not have to obtain a title in Court since this document serves as an enforceable title.

In most of the cases we are talking about a claim for money covered by the enforceable title. There is, however, also the situation that this title covers a claim for the surrender of a vessel but this would not lead to a Judicial Sale.

b. Ship Arrest

It should be noted that the ship arrest in Germany is possible for all kinds of monetary claims, not necessarily maritime claims. The concept of the arrest in Germany is to obtain an arrest order which shall secure the creditor. It is a preliminary security for the creditor to enforce a later title in the main proceedings. It is therefore that the arrest order which is enforced against the vessel and by which the vessel is detained, is not a title by which a Judicial Sale can be invoked. Otherwise, this would be a breach of the general principle that the main procedure cannot be anticipated by an arrest procedure. There is an exemption to the general rule for those cases where the costs and expenses of safe custody become unproportional in relation to the value of the vessel.

While talking about an arrest in Germany, many of you may have made the experience that it is rather difficult to obtain such an arrest order. The problem rests with the requirements under German law to provide specific reasons for an arrest. Vessels trading on a regular basis and thereby calling German ports (liner service), for example, would be prevented from being arrested. The reason is that the Courts would consider this as sufficient asset within its jurisdiction. In addition, debtors located in the EU are also protected to a certain extent as the title in the main proceedings, which shall be protected by the arrest, would be enforceable in the EU, which by itself is – other than for non-EU-debtors – no sufficient reason for an arrest.

This, however, will change materially from next year on. With the introduction of our new German Maritime Code there will be a change in the requirements for a ship arrest. The necessity of an arrest reason is then no longer required for arrests of seagoing vessels.

2. Valid Service

The enforceable title has to be served upon the Shipowner. Whether service of the title upon the Master instead of the Owner is sufficient is uncertain in some cases. In praxis it is agreed that the Master should have such authority. It is based on a legal power of representation in Section 527 HGB (Commercial Code) and Section 170, 171 ZPO (Civil Procedure Code). The new maritime law in Germany, very likely becoming effective during the first couple of months in 2013 will clarify this. The new law will provide for a legal authority of the master to accept service also in Judicial Sale proceedings (see new Section 619 HGB).

It should further be noted that the service procedure in Germany, other than in many other jurisdictions, cannot be substituted by service between the lawyers. The service needs to be carried out by the bailiff under supervision of the Courts.

Finally, there is the option for a creditor to commence a claim against the Master to accept a Judicial Sale of the vessel. In that scenario the Master would be the defendant and a judgement against the Master would be valid also against the Owner.

3. Court Order of Enforcement

The creditor of the enforceable title has to apply for a Court Order of Enforcement (Sections 165 and 15 ZVG). This Order has to be served upon the Owner as well. The Order of the Court will not only include the approval of Judicial Sale proceedings but also an Order to surveillance and custody of the vessel.

The Court will inform the ships register and the ships register will record the order (Sections 162 and 19 para. 1 ZVG) (“*Versteigerungsvermerk*”).

With regard to the competent Court for the enforcement procedure this depends on the place where the vessel is located (Section 163, 1 ZGV), in other words: in the respective German port. Should the vessel be in the Hamburg ports it can be subject to Judicial Sale procedures in Hamburg (Section 171 ZVG).

Ships not being registered, however in German ownership, are subject to the enforcement procedure for movable property which does mean that the bailiff would take them into possession and will sell them in a Judicial Sale.

4. Safe-custody of the Vessel

With the Court Order of enforcement the safe-custody of the vessel is ordered. The Court will usually instruct a bailiff to carry out the necessary measures to prevent the vessel from sailing. The vessel is detained (Section 165 ZVG). This may include the taking away of the ship's papers, relocation of the vessel in another port area and hog-tie the vessel. The bailiff will use the services of the harbour police. Alternatively, the Court can order the safe-custody being carried out by a trustee in order to secure that the costs and expenses accruing during that period are covered and the necessary works and insurances are carried out.

The safe-custody will terminate either with withdrawal of the enforcement action or completion of the Judicial Sale.

The costs for safe-custody are part of the Judicial Sale procedure and will be settled from the proceeds of sale with first priority (Section 109 ZVG). The Court will ask the creditor for a retainer for these costs.

5. Announcement of Auction

The Judicial Sale will be carried out by the competent Court as described above. This Court is obliged to announce the auction. Such announcement must be served upon the participants ("*Beteiligte*") according to Section 41 ZVG. This group includes the creditor (of the title), the debtor (shipowner) and the registered mortgagees (if any) and the other creditors on record in the ships register (if any) (Section 9 ZVG). In addition, the announcement has to be made in specific shipping magazines. In Germany we would consider the "THB" (*Täglicher Hafenbericht*) or "Hansa" as such a magazine. The announcement has to include the entries on record of the ships register, *i.e.* name of the vessel, shipowner, mortgages, time and place where the Judicial Sale will take place, the declaration that this sale is carried out by way of enforcement of a title, the invitation that rights not being on record in the ships register such as maritime liens shall be declared by the creditors at the latest at the time of the Judicial Sale and the request to make a protest

against the Judicial Sale before completion of the Judicial Sale proceedings if any party believes the Judicial Sale is not justified. The announcement can also be made in electronic form, provided the vessel is under custody in its home port and procedures are carried out by the competent Court of the home port.

Parties who have informed the ships register about a maritime lien are protected because such information is deemed to be given to the competent Court of the Judicial Sale (Section 168 b ZVG) if such filing was done 6 months before announcement of the Judicial Sale.

If the German Court shall carry out a Judicial Sale of a vessel which does not fly the German flag, the German Court shall (*“soll”*) – provided this does not delay the procedure – serve the Court Order by which the auction has been scheduled to the holders of maritime liens which can be identified from the ship’s papers and inform the foreign ships register (Section 171, para. 3 ZVG). Although this provision contains some discretion (*“Ermessen”*) of the Court, there is limited scope to avoid such notification.

6. Transfer of Title

The Judicial Sale procedure itself is made by way of a public auction. The party with the highest bid will obtain the award (Section 81 ZVG). The award is made by an order of the Court which is published in the auction or within one week after the auction took place. With this order the title is transferred to the party with the highest bid (Section 90 ZVG).

There are no requirements for a minimum offer. However, in a Judicial Sale of a German flagged vessel, the provisions of the *“geringste Gebot”* which could be translated to “lowest bid” have to be complied with. The *“geringste Gebot”* (Section 44 ZVG) means that the lowest offer must cover the costs of the Judicial Sale plus the claim amounts of creditors which are prior in ranking to the claim of the creditor having applied for the auction of the vessel. If, for example, a second-ranking mortgagee applies for a Judicial Sale of a German flagged vessel this lowest bid must cover the costs of the Judicial Sale procedure plus the amount of the first mortgagee. In praxis, this means that the bidder in the auction does auction a vessel with a mortgage attached thereto.

In case of a foreign-flagged vessel the situation is different. There is no provision for the “*geringste Gebot*”. In consequence, all the securities recorded or maritime liens are deleted with the award.

Every bidder in an auction in Germany has to provide security in the amount of 10 % of its bid. This is limited to the amount which has to be paid in cash and does not include securities which remain in place according to the lowest bid provisions (Section 44, 52 ZVG).

Any party claiming against the proceeds of sale can apply with the Courts to take the vessel into safe-custody until the proceeds of sale have been paid to the Court by the highest bidder.

7. Distribution of the Proceeds

The distribution of the proceeds is stipulated in Section 104 ff. ZVG. The Court will fix a date for distribution of the proceeds after the award was published by which the transfer of title is ordered. This date shall be published by the Court and submitted to the new Owner and the other parties claiming funds from the previous Owner. The Court may give all parties a 2-weeks-period to file their claims against the proceeds of the sale whereafter the Court will prepare a preliminary distribution plan for the proceeds. The general priority is as follows:

- The costs of the Judicial Sale procedure
- The secured claims, in particular maritime liens and mortgages;
- Other claims.

There is the possibility to object to the claims which creditors have filed against the proceeds (Section 115 ZVG). In general, the procedure is governed by the Court which in the end also arranges for the distribution of the proceeds to the approved creditors by way of bank remittance of the approved share.

8. Summary and Comment to the Draft Instrument on Recognition of Foreign Judicial Sale of Ships

After having briefly outlined the procedure in Germany and compared the procedure with the instrument on Recognition of Foreign Judicial Sale of Ships I can identify many similarities:

- a. First of all, the definition of “Judicial Sale of a Ship” or “Judicial Sale” or “Sale” in the instrument is in compliance with German law. It is a public auction under the control of a Court. What is, however, different from German law is the option to have a sale in form of a private treaty included.

- b. Article 3 deals with the notice of a Judicial Sale and specifies that the Court carrying out the Judicial Sale has to inform
 - (aa) the registered owner of the ship (same in Germany);
 - (bb) all holders of registered mortgages (same in Germany);
 - (cc) all holders of maritime liens provided that the Court conducting the Judicial Sale has received notice of their respective claims (same in Germany);
 - (dd) the authority in charge of the ships register in the State of registration (same in Germany with regard to German flagged vessels, but optional with regard to foreign-flagged vessels with some limited discretion).

- c. Next to the procedural issues about a Judicial Sale which should be coped with by the respective jurisdictions, the recognition of the Judicial Sale is of utmost importance. Within the European Union we do not have this difficulty but once we go beyond our EU-borders, we do have problems that the Judicial Sale orders are recognised and complied with. There are only general provisions in Germany referring to the principle of “*ordre public*” covering the acceptance of foreign (non-EU) enforcement actions.

I believe that the instrument of Recognition of Foreign Judicial Sale of Ships could develop to become a valuable instrument to uniform the standards of Judicial Sale Procedures and to safeguard the international acceptance of the Judicial Sale awards rendered under these standards.

Thank you for your attention.

Dr. J.-E. Pötschke