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Waking Up from the Shipowners' Nightmare!

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Introduction

1. One still gets the sense from reading news about the global shipping industry that market conditions and growth are difficult − technological developments and regulatory requirements add to the cost of doing business, manpower and operational challenges and of late, the decline in the lifespan and hence the book value of ships because the average age of scrapped vessels has declined from 32 years in 2009 to 26 years in 2016.[2] In recent times, the demise of big names like Hanjin Shipping, Rickmers Trust Management Pte Ltd, Swiber Holdings, and Swiss Co is a signal to the rest of the shipping industry that no company is too big to fail. The domino effect of shipping insolvencies is clearly a "shipowners' nightmare".

2. Waking up from it, I will first discuss two recent Singapore decisions involving shipowner's liens and thereafter the impact of the latest changes in Singapore's insolvency regime on maritime creditors. Has Singapore's amendments to its Companies Act, which came into effect on 23 May 2017, come at an opportune time for the restructuring of financially distressed companies? The amendments also adopted the UNCITRAL Model Law on Cross-

[1] I'm grateful to Ms Deborah Koh, a former legal associate of M/s Ang & Partners and now consultant with the Singapore Mediation Centre for her assistance in preparing this paper. All views expressed are personal and do not represent those of the Supreme Court of Singapore. All errors are entirely mine.
[2] Kari Reinikainen "More ships head to early grave", Fairplay (20 July 2017) at p18.

Border Insolvency ("Model Law"), making foreign insolvencies more easily recognised in Singapore.

3. I will leave you the audience to decide at the end of my session whether shipowners have woken up from or are still living a nightmare of endless bad news.

Lien on sub-freights

4. In the controversial decision of *Duncan, Cameron Lindsay and another v Diablo Fortune Inc and another matter* [2017] SGHC 172, the Singapore High Court held that a contractual lien on sub-freights was a charge registrable under s 131 of the Companies Act[3] (a similar provision is found in s 353 of Malaysia's Companies Act 2016). The contractual lien was not registered so it was held to be void against the liquidator and the creditors of the company.

5. This case has caused dismay in Singapore amongst admiralty practitioners, shipowners and people in the insurance industry. It highlights the tension between maritime and insolvency practitioners. For shipowners and admiralty practitioners, there is no commercial reason why contractual liens should be registered, as registration is impracticable and inconvenient given the volume of charters entered into worldwide, on a daily basis, that contain standard contractual lien clauses. Further, the duration of the charter could vary significantly from short to medium and long term. More to the point, charters are often concluded by shipbrokers and the contracts are contained in exchanges of e-mails culminating in fixture recaps. Besides, most financing agreements which provide for a lien over the goods (or proceeds thereof) are "rolling agreements", meaning that they continue until terminated.

[3] Cap 50, 2006 Rev Ed.

6. Conversely, the registration of contractual liens would give creditors notice of the lien. More importantly, a shipowner with an unregistered contractual lien should not take priority over other creditors at the winding up of the charterer. This High Court decision is currently on appeal, and I do not intend to comment on the merits of the case in this paper. In the interim, to enforce such security interests, shipowners would have to call upon their charterers (*ie,* the chargors) to register lien clauses on, or shortly after, execution of the charterparty, where a Singapore-incorporated charterer is involved. Shipowners can register the contractual lien as a charge if the Singapore-incorporated charterers do not do so. I am here referring to s 132(1) of the Companies Act which provides that a chargee (shipowner) may undertake registration as he is an interested person under the provision. Ordinarily, it is the chargor (charterer) who has to register the contractual lien because it is he who faces risk of penal sanction under the Companies Act if he fails to register the charge (s 132(1)). One final point is that existing holders of contractual liens may have to apply to have those liens registered out of time. What you have just heard is the legal consequence of the decision in *Diablo Fortune Inc*. But business people have been quick to get around this legal setback with a simple practical and workable solution, which is to use SPV companies not incorporated in Singapore to enter into charters.

7. In *Diablo Fortune Inc,* the liquidators of Siva Ships International Pte Ltd ("Siva Ships"), a company incorporated in Singapore, sought a determination that the owners, Diablo Fortune Inc ("Diablo")'s lien over sub-freights or sub-hire due from V8 Pool Inc ("V8") to Siva Ships was void against the liquidators pursuant to s 131 of the Companies Act for want of registration.

8. Diablo had bareboat chartered a vessel to Siva Ships who in turn entered a pooling arrangement with V8 whereby V8 agreed to pay Siva Ships charter hire based on the actual earnings from the pooling arrangement. Siva Ships was subsequently wound up in Singapore and prior to that the vessel was redelivered to Diablo. In December 2016, Diablo sent V8 a

notice exercising its lien under clause 18 of the bareboat charter. V8 did not make payment of the December charter hire to Siva Ships on account of that lien notice. By early January 2017, Siva Ships' liquidators learned that the vessel was on route to Spain pursuant to a sub-charter between V8 and Repsol Petroleo SA ("Repsol"), so Diablo issued Repsol a clause 18 lien notice in January 2017. The argument there was that freight due under that bill of lading was assigned to Diablo by virtue of clause 18 and as such, Diablo was entitled to receive freight from Repsol.

9. The vessel was allowed to complete its voyage, cargo was discharged and certain payments were made pursuant to a settlement agreement. However, V8 withheld sums covered by the lien notices(s) until the dispute over the validity of Diablo's lien was resolved. Diablo then commenced arbitration proceedings against Siva Ships in London and obtained protective orders from the Spanish Courts over its two lien notices to prevent V8 and Repsol from paying out monies to any parties pending the outcome of Diablo's claim in arbitration.

10. The Liquidators obtained an order from the London High Court recognising the Singapore liquidation and an automatic moratorium or stay on all proceedings, including the London arbitration, was granted.

11. The issues before the Singapore court were whether:

i. a stay should be granted in favour of arbitration;

ii. Singapore law should govern the registration of charges and priorities in insolvency matters;

iii. the lien over sub-freights or sub-hire came within s 131 of the Companies Act and should be registered; and

iv. an extension of time should be given to Diablo to register its lien under s 137 of the Companies Act.

12. On the issue of the stay, the High Court noted that the present dispute was concerned with whether the charge was void against the liquidators for want of registration, and did not pertain to the validity of the lien between Diablo and Siva Ships. A stay was refused since the express language of the arbitration clause did not cover the precise challenge raised by the liquidators.

13. The second to fourth issues are relevant for present purposes. On the second issue, the High Court held that the law governing the registration of charges and the priorities of security interests in insolvency proceedings must be determined by the law of the country where the winding up is commenced. In the present case, Siva Ships was incorporated in Singapore and winding up proceedings were also commenced here. Therefore, s 131 would apply.

14. The third and most important question for shipping practitioners and shipowners was whether a lien over sub-freights or sub-hire (a contractual lien) was a "charge" under s 131. The English authorities have held that a contractual lien gives rise to an equitable assignment by way of a charge, which is registrable under the UK Companies Act and may be void for want of registration against a liquidator and creditors of the company. Such liens were characterised as a charge within the meaning of the UK Companies Act,[4] and registrable either as a charge on a book debt (*The Ugland Trailer* [1986] Ch 471) or as a floating charge (*The Annangel Glory* [1988] 1 Lloyd's Rep 45).

15. In contrast, in Hong Kong, a contractual lien is not characterised as a charge under s 334 of the Hong Kong Companies Ordinance (the "HK Ordinance").[5] Section 334(4) expressly

[4] See s 95 UK Companies Act 1948, s 395 UK Companies Act 1985, and s 860 UK Companies Act 2006.
[5] Cap 622.

states that "[f]or the purposes of subsection (1)(d) and (j), if a company charters a ship from a shipowner, **the shipowner's lien on the subfreights** for amounts due under the charter is **not to be regarded as a charge on book debts of the company or as a floating charge on the company's undertaking or property**". A consultation paper by the Hong Kong Financial Services and the Treasury Bureau titled "*Second Public Consultation on Companies Ordinance Rewrite*" dated 2 April 2008 explains why a contractual lien is excluded from the definition of a charge (at para 5.17):

> Essentially a lien on subfreights is a provision in the charterparty (lease) of a vessel stating that the shipowners shall have a claim upon all amounts due under sub-charterparties for payments in respect of the headcharter. The provision gives the shipowner the personal right to intercept sub-charter payments before they reach the charterer but the provision nevertheless seems to lack the proprietary characteristics of a charge. Registration is also inconvenient from a commercial perspective since charterparties are usually negotiated by shipbrokers and not by lawyers and are normally of a relatively short duration.

16. Unfortunately, there was no clear intention of the Singapore Parliament to reduce or limit the effect of the general words of s 131. While the High Court recognised the tension between admiralty and insolvency practitioners, ultimately, s 131 had the protection of unsecured creditors in mind.

17. The High Court preferred the English approach of a contractual lien operating as an equitable assignment and found, in substance, the nature of the rights and obligations via a contractual lien consistent with the rights and obligations intended by a grant of a charge. The contractual lien had the characteristics of a floating charge as well as a book debt, and thus fell within the meaning of a charge under s 131, either as a floating charge under s 131(3)(*g*) or a charge on book debts under s 131(3)(*f*).

18. The final issue was whether an extension of time for registration under s 137 ought to be granted. Diablo stated that it has never been the case nor the industry practice for a contractual lien to be registered. It was unaware of any such requirement under Singapore law.

19. The High Court found that unawareness of the requirement for registration sufficed as inadvertence for the purposes of s 137. However, Diablo was unable to persuade the court to exercise the discretion to extend time in its favour. As Siva Ships had been wound up, an order extending time would not ordinarily be made save in an exceptional case such as fraud. No such exceptional case was shown, neither was it just and equitable to do so as it would have prejudiced unsecured creditors by giving Diablo an unfair advantage over them. A liquidator was bound by statute to distribute the net proceeds *pari passu* among the unsecured creditors. The application for extension of time was refused.

Lien over cargo

20. The same reasoning recounted above on the application and effect of s 131 of the Companies Act on a contractual lien for sub-freight or sub-hire could have arisen in *Five Ocean Corp v Cingler Ship Pte Ltd* [2016] 1 SLR 1159 if the sub-charterer, a Singapore incorporated company, had been wound up. Creditors had filed winding up proceedings against the sub-charterer who managed to stave off winding up proceedings by seeking protection by way of the scheme of arrangement process to restructure its debts. From the wording of s 131, it appears that registration is only required at liquidation where the charge would otherwise be void against "the liquidator and any creditor of the company". Such argument would fail under a scheme of arrangement.

21. I would like to mention another scenario on s 131 registration in the context of a lien on cargo like in *Five Ocean*: Can a contractual lien over cargo for amounts due under the charter give the shipowner an equitable assignment of a chose in action by way of security? The answer is yes, if the cargo belongs to the charterer and he is able to create a contractual lien over his asset. But if the cargo does not belong to the charterer, there is, so to speak, nothing to create an equitable assignment over. Retuning to s 131, if the charterer, a Singaporean company, creates an equitable charge on the cargo for amounts due under the charterparty, at law, a floating charge on the property of a company is created and registration is required.

22. *Five Ocean* illustrates how the insolvency of the sub-charterer down the charterparty chain could burden the shipowner and frustrate its business operations and employment of its vessel even if its immediate charterer has paid the hire. Corrina Maritime Inc ("Owners") came to the aid of their immediate time charterers, Five Ocean, when the sub-charterer, Cingler Ship Pte Ltd ("Cingler"), became insolvent. It was in the Owners' interest to free the vessel of the cargo so it could be deployed again. Five Ocean was concerned that its contractual lien would be worthless as security as the unpaid freight, detention and expenses due from Cingler far exceeded the value of the cargo on board. Thus, Five Ocean as the plaintiff, applied for a sale of cargo to preserve the value of the cargo of steam coal as an interim measure in aid of arbitration between the parties in Singapore. This application was supported by the Owners who filed supporting affidavits and also confirmed that they would abide by a court order made in the sale application. At the same time, the Owners and Five Ocean were also concerned that the cargo showed visible signs of heating damage, and the safety of the vessel and crew were in issue. The vessel was in international waters off the last nominated port of India because of the ongoing dispute and a delay by Cingler in nominating a discharge port. Five Ocean and the Owners had feared losing their lien rights if the vessel proceeded to an Indian port for discharge.

23. Cingler had in turn voyage chartered the vessel to PT Commodities & Energy Resources ("CER"). Cingler failed to pay freight to Five Ocean when it became due and failed to nominate a discharge port on time. CER, interveners in the proceedings, refused to pay sub-freight to Cingler because of a running account between Cingler and CER; additionally, they were embroiled in a separate dispute. Initially, CER, wanted an adjournment of the hearing to allow it time to negotiate the sale of the cargo to one "Adani group of companies". This was tricky as there was already a worldwide freezing order granted by the High Court of England over CER's assets as a result of an unrelated dispute, and a corresponding injunction had been granted over CER's assets in Singapore.

24. The head voyage charterparty between Five Ocean and Cingler contained the usual lien clause (clause 8):

> The owners shall have a lien over the cargo and on all sub-freights payable in respect of the cargo for freight, deadfreight demurrage claims for damages and for all other amounts due under this Charter Party including costs of recovering the same.

25. The sub-voyage charter between Cingler and CER was on the Gencon 1994 form. Upon loading the cargo a set of Gencon 1994 form bill of lading was released to CER naming them as shipper and Adani Enterprises as the notify party. The bill of lading was consigned "to order" and signed by the load port agent as agent for and on behalf of the master of the vessel.

26. Both the head voyage charter and the Bill of Lading were governed by English law. On the strength of the authorities and fact that the word "freight" was used in the Bill of Lading, the position at English law was that the charterparty incorporated in the Bill of Lading was the

head voyage charterparty between Five Ocean and Cingler which gave the Owners a lien on the cargo for sub-freight and all other amounts described in clause 8.

27. The Owners and Five Ocean separately gave notice of lien and the exercise of lien over the sub-freight and cargo to Cingler, CER and Adani Enterprises. Parties were in settlement talks but no resolution was reached so Five Ocean issued a notice of arbitration. Cingler did not respond. Despite the existence of the s 210 scheme application, leave of court was obtained to enable the sale application to continue against Cingler. Cingler's counsel was present at the hearing and he did not oppose the application to sell the cargo.

28. The issue in this case was whether Five Ocean could claim the benefit of a contractual lien on cargo against CER, to whom the cargo belonged and with whom Five Ocean had no contract, for unpaid freight and other sums owing to Five Ocean by Cingler. The hearing proceeded on the basis that the cargo belonged to CER and physical possession was with the Owners. Against this factual backdrop, two main questions arose in the sale application. First, Five Ocean's legal basis for bringing the sale application. Second, the court's power of sale, which is independent of the legal proposition that a typical lienee has no power of sale, and there is no provision for a sale in clause 8.

29. On the first question, the High Court held that the lien clause for sub-freight gave Five Ocean, as equitable assignee, the right to payment of money owed by CER to Cingler. Five Ocean could "intercept" the unpaid sub-freight. Five Ocean was an equitable assignee, at least of the sub-freight, but as to its contractual lien over cargo, Five Ocean could not truly exercise it. Cingler did not own the cargo and possession of the cargo was with the Owners. Fortunately for Five Ocean, the Owners made use of the Bill of Lading to exercise its contractual lien over

the cargo against CER, as trustee, for the benefit of Five Ocean. Hence, Five Ocean's legal basis for bringing the sale application, its *locus standi,* would be its beneficial interest in the Owners' exercise of the lien. Coupled with that beneficial right, as against Cingler, clause 8 gave Five Ocean the personal right to direct the Owners to postpone discharge and delivery of the cargo until the sums secured by the Owner's lien were paid. In the judgment, the combined rights in the cargo was termed collectively as Five Ocean's "right to detain possession".

30. On the High Court's power to sell the cargo subject to a lien, since the dispute would be decided at arbitration, counsel for Five Ocean relied on the urgent interim sale provisions in the International Arbitration Act ("IAA").[6] The argument was that the nature of Five Ocean's right to detain possession was an "asset" which could be properly preserved by an order of sale of the cargo as an interim measure.

31. Related to that issue is the inquiry into whether the right to detain possession of the cargo could be preserved through an order for sale of the cargo. The court held that it had power to order interim measures in aid of arbitration[7] as the court had *in personam* jurisdiction over the parties. Cingler was a Singapore incorporated company present in the jurisdiction while CER had submitted to jurisdiction, having intervened. The main legislative intention behind the enactment of s 12A of the IAA was to give the court powers over assets and evidence situated *in Singapore* and to make orders in aid of arbitrations that were *seated in Singapore and overseas.* As the cargo was in international waters, the grant of the sale order would not interfere with the jurisdiction of any court.

[6] s 12A(4) read with s12(1)(d) of Cap 143A, 2002 Rev Ed.
[7] s 12A(4) of the IAA.

32. The High Court found that Five Ocean's right to detain possession *vis-à-vis* Cingler was not "security" in the conventional sense, but was in effect a mechanism to enforce payment of the sums due to Five Ocean under the head voyage charterparty over the cargo. As a chose in action, it was an "asset" which could be preserved under s 12A(4). Equally, the Owner's contractual lien was a chose in action and was an "asset" under the same provision.

33. Next, could the right to detain possession of the cargo be preserved through an order for sale of the cargo? At first glance, an order for the sale of the cargo appeared inconsistent with the concept of a right to detain, which typically would not give rise to a right to sell unless expressly provided for in the contract.

34. Besides the IAA, there is Order 29 r 4 of the Rules of Court and there was clear evidence of the deteriorating condition of the cargo. The rationale behind O 29 r 4 is that where goods are perishable or are a wasting asset if kept, the value of the movable property the subject matter of the proceedings would be lost.[8] This rationale fits squarely into the intention behind the IAA provisions[9] to preserve the property which is or forms part of the subject matter.

35. Thus, Five Ocean's right to detain possession could be effectively preserved through an order for sale − its right to detain possession would then be transferred to the proceeds of sale. An order to sell represented a fair balance of the respective interests – preservation of the value of the cargo and the safety of the vessel and crew – in the absence of a satisfactory and reasonably agreed solution in place amongst Five Ocean, Cingler and CER despite numerous opportunities. The last minute request for an adjournment of the sale application for CER to

[8] See *Emilia Shipping Inc v State Enterprises for Pulp and Paper Industries* [1991] 1 SLR(R) 411.
[9] s 12A(4) read with s 12(1)(*d*).

negotiate a sale with the Adani companies was pointless as they could still buy the cargo after the order of sale was made.

Singapore's new restructuring laws and cross-border insolvency

36. At the outset, I mentioned the demise of Hanjin Shipping, a leading Korean shipping company whose ships, whether owned or chartered, would sail around the globe to numerous ports. One cannot ignore the international dimension when an entity like Hanjin Shipping faces insolvency; there are cross-border issues that have to be addressed. Typically, the question is whether a foreign restructuring order would be recognised and given effect in Singapore.

37. If so, what would its effect be on the commencement of and/or continuation of proceedings against the assets of the foreign entity in Singapore? In a shipping context, the query is whether the foreign restructuring order, which usually contains a moratorium order, would be recognised, so that local proceedings, for instance, to exercise a contractual lien, could not start, or the sale application discussed earlier would have to stop. The answer to whether the foreign moratorium order has world-wide effect depends on whether the order is recognised in Singapore and the scope of the order. Equally, one needs to bear in mind the nature of the proceedings or intended proceedings: whether *in rem* or *in personam*.

38. Prior to the adoption of the Model Law, the established position was that foreign winding up orders (including any foreign winding up orders to stay proceedings in the forum) would not be recognised. However, the Singapore courts could assist foreign liquidation proceedings through the courts' existing procedural powers, on a case-by-case basis: *Beluga Chartering GmbH (in liquidation) v Beluga Projects (Singapore) Pte Ltd (in liquidation)* [2014] 2 SLR 815.

39. After May 2017, once a foreign main proceeding is recognised under the Model Law, a moratorium is in place which, under Art 20(1)(a), effectively stops the commencement of actions or proceedings concerning the debtor's property, rights, obligations or liabilities. I make two observations. First, the Model Law does not apply to group enterprises. There is no provision in the Model Law dealing with cross-border enterprises comprised of multiple entities. In the shipping industry, we see one-ship companies and this is recognised as a legitimate way of managing risk. This observation on shipping company ownership structures feeds into the scope of the foreign moratorium order, and an examination of the foreign order is a must. If the foreign order extends to the debtor's related entities, there is an overreach which is contrary to the Model Law. Second, in so far as Singapore is concerned, the separate entity doctrine still applies in insolvencies. Hence, the single economic entity concept has no place in Singapore and again, under Model Law, any foreign moratorium order that seeks to extend the foreign moratorium over assets of related entities in the jurisdiction is an overreach that is contrary to Singapore law and should not be recognised.

40. On the domestic front, what is the legal position in Singapore brought about by the amendments to the Companies Act where there is an automatic or court moratorium? I have to limit the overview of the amendments in the interests of time. Broadly, the ostensible answer comes from Singapore's Ministry of Law's statement[10] clarifying that there is no change in the law with respect to maritime claims in liquidation and judicial management situations. The only difference is that now, if an automatic or court-ordered moratorium in a scheme situation is in place, maritime claimants will have to apply for leave to proceed with their claims (in the same way that they have always had to do in liquidation and judicial management situations).

[10] https://www.mlaw.gov.sg/content/dam/minlaw/corp/News/Note%20on%20Debt%20Restructuring.pdf

41. Under the new regime, where creditors' schemes of arrangement are in place, an automatic moratorium (with worldwide effect that extends to debtors' related entities whether in Singapore or not, *ie*, subsidiaries and holding companies may also apply for a moratorium)[11] kicks in. The Ministry's comments that if a 30-day moratorium in a scheme situation is granted, leave has to be sought to proceed against a vessel. This area is new. In future, the court may be asked to adjudicate on whether the scheme moratorium applies to *in rem* claims as the wordings of the statute refers to "the commencement or continuation of any proceedings … *against the company*" (s 211B(c)). *In rem* actions are against the vessel, the asset of the company rather than the company itself. Section 211B(d) refers to an order restraining the "levying of any execution, distress or other legal process against any property of the company". The words "other legal process" read in *eusdem generis* could refer to similar legal processes like garnishee proceedings. If *The Daien Maru No 18* [1983-1984] SLR(R) 787 is not distinguishable today, an arrest would fall outside the scope of these processes. Thean J there explained that an execution proceeding is to enforce a monetary judgment *in personam*. In contrast, a judgment *in rem* is against the *res* and such a judgment can be enforced against the *res* by a remedy *in rem*. In that case, the arrest of the ship was to obtain security for the judgment.

42. Similarly, under Malaysia's Companies Act 2016, the power of the court to restrain proceedings under s 368 in schemes applies to "further proceedings in any action or proceeding against the Company".

43. As regards the statement that the amendments to the Companies Act have not changed the law with respect to maritime claims in liquidation and judicial management situations, there

[1111] S211B.

are some cases that are useful. Under Singapore law, *in rem* creditors like maritime lien holders and others whose *in rem* rights are derived from the High Court Admiralty Jurisdiction Act[12] and have taken steps to file their *in rem* writs early enough are essentially distinguishable from the company's general body of creditors. They are regarded as secured claimants in admiralty proceedings. Where an *in rem* writ was filed and issued but not served *before* commencement of winding up, the plaintiff was considered a secured creditor and the court would ordinarily exercise its discretion to grant leave to proceed with the action under s 262(3) of the Companies Act: *Lim Bock Lai v Selco (Singapore) Pte Ltd* [1987] SLR (R) 466 referring to in *Re Aro Co Ltd* [1980] Ch 196. Conversely, if the *in rem* writ was issued *after* the petition for the winding up, the plaintiff would not be considered a secured creditor under s 262(3): *The Hull 308* [1991] 2 SLR(R) 643.

Conclusion

44. I leave you with several disparate thoughts. These thoughts offer a "case study" in how insolvency can affect different players in the global shipping system in very different ways. For shipowners, they can range from a headache to a disaster. It is rare that disruptions can be lucrative. Singapore's restructuring regime could offer relief to ailing shipowners, but as with many cases, the desire to save the business depends a lot on its viability.

Thank You

[12] Cap 123, 2001 Rev Ed.