THE ARREST news

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In this issue of *The Arrest News,* read about a surprising decision from Malta's Superior Court, advice on how to mitigate risks of a LOI nightmare, and piercing and lifting the corporate veil in Spanish Courts.

Malta Overrules Foreign Auction by Dr. Jean Pie Gauci-Maistre, Ms. Despoina Xynou, & Dr. Yvanka Vella, Gauci-Maistre Xynou Legal | Assurance

In an unprecedented state of events, the Maltese courts have recently upheld and justified the arrest in Malta of the Liberian registered bulk carrier Bright Star following its judicial sale by auction in a foreign jurisdiction.

In January 2018 the M.V. Bright Star (previously known as M.V. Trading Fabrizia) was sold in Jamaica for US$ 10.3 million in a judicial sale.

Following the prior registration of a mortgage against the vessel in Malta by Jebmed s.r.l., in 2016, the M.V. Bright Star was arrested while in Maltese waters on the 19th June 2018 by this same company; creditors of the vessel's owning company Capitalease S.p.A. in the amount of circa US$ 820,000.

The contestation brought by the vessel's lawyer was that the arrest in Malta was in fact unjustified since the vessel had been sold free and unencumbered in Jamaica and that any action brought subsequent to the judicial sale should be brought against the proceeds of the sale and not against the vessel itself.[1] This was especially significant in light of the fact that the sum of US$3 million had been deposited into the Jamaican court for the sole reason of satisfying Jebmed s.r.l's claim.

In this specific case, the creditor company relying on a legal opinion obtained by Jamaican lawyers, argued however that for Jebmed s.r.l. to be able to satisfy their claim and tap into the money deposited, certain additional domestic procedures needed to be instituted in Jamaica since the executive title obtained under Maltese law was not recognised by the Jamaican courts.

[1] Article 37D of the Merchant Shipping Act; Cap. 234 of the Laws of Malta

In a decision handed down by Malta's Superior Court of Appeal on the 8th February 2019, the Court acknowledged and confirmed the argument in line with Maltese law that following a judicial sale, a vessel is freed of any mortgage and therefore the interest of all creditors including mortgagees shall pass on to the proceeds of the sale of the ship. Nevertheless, it is not enough that the sale has been carried out. It is equally important to ensure that the interest of any creditor is effectively passed on to the proceeds of the sale. Unless this is the case, both by virtue of title and ranking, then the coercive effect of the registered mortgage is diminished specifically when the need for it to be enforced arises.

With reference to the legal opinion obtained in Jamaica, the Maltese Court held that since the effect which a registered mortgage offers a creditor was not recognised in Jamaica, neither was the creditor's ranking in the same way as it is provided for under Maltese law. The money available, although sufficient to cover the debt owed was there as a precaution and there was no guarantee that there would be no other higher ranking creditors in Jamaica.

As a result, filing an action against the proceeds of the sale in Jamaica would be tantamount to suing for breach of contract and Jebmed would be simply considered as having evidence of a cause of action for a debt which garners no executive or preferential force.

The legal principle of reciprocity was further emphasised by the Court. In the same way that the executive force and preferential right afforded by the Maltese registered mortgage was not recognised under Jamaican law, then the sale of the vessel free and unencumbered in Jamaica could not have the same effect as it would, had this been carried out in Malta.

The repercussions emanating from this judgment remain to be seen. Whether this will result in less confidence being placed in the historically accepted legal tenet that a vessel is sold with a clean title and without any *droit de suite* by prospective buyers in a judicial sale is unknown.

This decision has highlighted the breadth of the problem of non-recognition of foreign judicial vessel sales and can be viewed as a clear example of why the draft International Convention on Foreign Judicial Sales of Ships and Their Recognition (the 'Beijing draft') is so sorely needed.

From a Maltese perspective, what is certain is that the Maltese courts have emphatically declared that the rights afforded to creditors by virtue of the legal instruments available at law should be observed without fail.

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Letters of Indemnity for Discharge / Delivery of Cargo Without Presentation of Original Bills of Lading by Ashwin Shanker, Chambers of George A. Rebello

IMAGINE THIS: You are a fourth generation wealthy Maltese ship owner, so you've seen the ups and downs of shipping. You have a small fleet. You go for a yacht weekend with your granddaughters to one of the nearby, beautiful islands. You then receive a phone call from the office informing you that one of your vessels has been arrested. You are not alarmed. You have seen your ships getting arrested several times before. Your P&I Club has

always been there to support you. Your office claims manager will take care of things, she informs the P&I Club. They in turn contact local lawyers who provide you a copy of the Court arrest papers.

THE NIGHTMARE: You are then surprised to find out that the arrest is for a whopping 10 million US Dollars by some Bank who claims to be holding the original Bills of Lading for cargo which you had carried and delivered some months ago against, as usual, a standard format Letter of Indemnity. Your P&I Underwriters will not secure such a claim, and at most are willing to provide you only legal costs of defence. You check your Letter of Indemnity that was provided to you by the then Charterer. Your London lawyers then write to the issuer of the Letter of Indemnity making a demand for the value of the goods that they had collected against the Letter of Indemnity. The demand email bounces back undelivered. You then find out that those Charterers / indemnifiers went bankrupt since. You look around. There is nobody else who will bear this cost. Your vacation is cut short, and you're back to the office on a Saturday morning in Malta. You realise that things are going wrong from all directions with no solution in site.

WHAT IS THIS LETTER OF INDEMNITY? It is essentially an Undertaking letter from the receiver / or the charterer promising to indemnify the beneficiary ship owner against any claims that you may face arising out of your discharging and/or delivering the cargo to the non holder of the original Bills of Lading.

BEST PRACTICES: With the benefit of hindsight, what would you have done differently to avoid such a scenario?:

1) Ensure your Letter of Indemnity is issued by a financially solvent party;

2) Ensure your Letter of Indemnity is additionally bank counter signed. The counter signature should not be restricted to mere affirmation of the indemnifier's signature, it should ideally also be a guarantee from the bank.

3) Ensure your Letter of Indemnity's wordings covers risks arising out of both discharge and delivery of the cargo.

4) Ensure your Letter of Indemnity issuer is indeed going to soon have the possession of the negotiated Bill of Lading. Ask for (1) copy of documents submitted under the Letter of Credit, (2) the Letter of Credit (3) proof that the documents stand accepted by the Bank (4) proof that the BL is in transit to the indemnifiers / receiver.

5) Issue a letter as per standard format which your operations team has been instructed to write to all parties in the cargo chain, i.e. shipper, notify party, financing bank, receiver, loadport agent and discharge port agent. Inform them that you will be proceeding to issue Delivery Orders for the cargo after say 48 hours unless you have heard otherwise from anybody objecting to same. While not foolproof, it strikes at a commercial and legal balance, reduces risk, and alerts potential claimants. Practical difficulty in this present scenario are: (a) Bills of Lading normally only contain names and addresses, they do not contain email IDs and fax numbers, (b) correspondence to Banks might not have the specific Letter of Credit number for their reference. (c) Your charterers will often not be happy to see you corresponding with their sub Charterers and clients. This might make you look like a cumbersome ship owners counterparty to deal with, contrary to the generally more trusting and relaxed market practice that your competitors follow.

6) Ensure your Letter of Indemnity is from a solvent ultimate Receiver who may be a factory owner, for example, or large corporation.

If your counterpart is a small trader,

7) Ensure your Letter of Indemnity is accompanied with additional security such as post dated cheques, or registration of a charge on the company's records as a priority mortgagee.

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Spanish Courts: Arresting a Ship and Lifting the Corporate Veil

By Felipe Arizon, Arizon Abogados

About a year ago a Spanish Commercial Court granted an order for the arrest of a ship despite the owners being a different entity to the debtor on the face of the claim. The registered owners contested the arrest without success before both the Commercial Court and the Court of Appeal.

Over the last few years we have received several requests from different parties enquiring about the possibilities to arrest a ship pending the piercing and lifting of the corporate veil of the registered owners Company.

In this article I will attempt to give the readers some guidance in response to such a scenario. First of all, I will endeavour to set out the existing lines of case law under which the Spanish Courts have agreed to pierce and lift the corporate veil. Secondly, we will look at the mentioned arrest case where both Courts, the Commercial Court and the Court of Appeal, agreed to the arrest of a ship despite the registered owners not being the apparent debtors under the claim.

The Spanish Courts have applied the doctrine of piercing and lifting the corporate veil when a legal entity has been used to abuse creditors in the attempt to elude a legitimate claim. This has been held to be the case in the following instances:

1.- Where a de facto group of companies, with apparent corporate independence, uses their corporate structure to avoid obligations to third parties as a fraud to creditors mechanism, eg the Supreme Court judgment of 28 February 2014. In that case several entities - with their own and separate legal personality – operated in the traffic, distributing rights and obligations among them in the way they deemed most convenient for the interest of the group as a whole, but causing losses to third parties. The Supreme Court held that all Companies of the group were liable for the claims. This scenario is likely to be the most common line of case law applicable to shipping cases where a whole fleet is managed as a single business unit but the liabilities are formally assigned to each one ship Company to prevent the other ship owning Companies from responding to the debts of the group.

2.- Where different corporate frameworks are set to avoid payment of the debts of the original company, that is for example when several companies are created with the same corporate purpose, and same decision-making body, but with a fresh corporate face to avoid payment of the initial entity's debts. This could be the case where a ship is sold to a "new" Company shortly after a large claim is put to the former owners but the new Company is set under the same interest and managements but simulating a new independent structure with no links with the initial Company in order to avoid payment of the claim by the initial Company.

We have seen this in several shipping cases where the sale of a ship was simulated to an off-shore Company controlled by the same ownership interest. For example, in an arrest case we handled for the arresting party before the Commercial Court of Las Palmas, as well as the Court of Appeal of Las Palmas, the arrest order against a fishing vessel was upheld by both Courts (Court of Appeal judgment of 3 Nov. 2015) on the basis that the alleged new ship owners, which appeared in the proceedings to lift the arrest as they had bought the ship after the claim arose, failed to prove any payment of the purchase price but only a few contractual documents for the sale of the ship.

3.- Where the director of the Company abuses the legal personality of the corporation to avoid payment of a debt. In such case he will be held jointly and severally liable for giving rise to an undercapitalization, and leading the company to insolvency, eg Supreme Court judgment of 9 March 2015. Where the partners, in so called undercapitalization cases, depleted the company resources preventing the Company from carrying out its purpose, the Court was ready to apply the doctrine of piercing and lifting the veil to hold liable the administrators of the company's debts, i.e. judgment of Supreme Court of 22 April 1994.

4.- Where a legal entity is used to avoid compliance with a mandatory regulation. There has been case law where a Company was served a judgment, only then the Company argued that it was the mere agency or branch of another company "his principal". There the Supreme Court understood that it was a case of fraud of law where agencies or branches were used to create confusion in those who contracted with them and take unfair advantage after the appearance created.

5.- Where two companies developed businesses jointly but created confusion with the intention to avoid payment of a claim, see STS June 7, 1995 where the Supreme Court agreed to lift the veil between two companies that developed their businesses jointly as a construction company and construction management, respectively. The Court understood that it was the intention of the companies themselves to create confusion to avoid payment to a creditor.

Having outlined the line of case law where the corporate veil has been pierced and lifted under Spanish law, we shall now explore two recent reported judgments in Spain where a Commercial Court and a Court of Appeal, agreed to grant and maintain the arrest order of a Portuguese ship in a Spanish port despite the claim being, on the face of the documents, against a party different to the registered owners.

The facts of the case were as follows: a Portuguese ship was arrested to respond for a claim of about USD 20,000.00 under the 1999 Arrest Convention. The registered owners, a company named Curromar Ltda. (Portugal) appeared in the Court contesting the arrest, contending they had nothing to do with the claim which was against Curromar Shipping SL (Spain). In the hearing the creditors sustained that both Companies were very closely connected so that they should be considered as one. The owners deposited the amount claimed in the Court to lift the arrest and contested the arrest order. In the hearing the arresting party contended that both Companies had the same shareholders, management, even though one was based in Spain and the other one in Portugal.

Judgment: The Commercial Court held that Art. 3.3 of the 1999 Arrest Convention states that: "Notwithstanding the provisions of paragraphs 1 and 2 of this article, the arrest of a ship which is not owned by the person liable for the claim shall be permissible only if, under the law of the State where the arrest is applied for, a judgment in respect of that claim can be enforced against that ship by judicial or forced sale of that ship." Therefore, according to the Court only where the claim may under Spanish law end up in the forced sale of the ship, such an arrest is permissible. The Court poses then the following question: Is it clear that this claim will not end up in a judgment enforceable against the ship? The Court answers the question with a "No, it is not absolutely clear". The Court also held that this was a precautionary measure procedure where the total clarity is not demanded but a fumus boni iuris, i.e. some evidence that the claimant may have a sound claim in law. Spanish law recognizes the lifting of the corporate veil to discover the abuse committed under the principle of autonomy of the corporations. It was found that at the time the claim arose the debtor was the charterer of the ship and as charterer it had a contractual option to buy the ship that could exercise by herself or by other Corporations of the group. It was also observed that the current owner of the ship is a company that was set up two months after the claim arose, the shareholders of both companies are the same, and so are the directors. With all these details in mind it could be feasible that, to resolve the claim on the merits, the Court uses the lift ing and piercing of the corporate veil doctrine leading to sale of the ship through an auction.

On Appeal, the Court of Appeal upheld the judgment of the Commercial Court and ordered costs against the owners. The Court of Appeal considered that according to the jurisprudence of the Spanish Supreme Court the lifting of the corporate veil is a legal tool available to extend a passive legitimation to a person other than the original debtor in cases where there is an abuse of a corporate personality to defraud creditors, generally in payment of personal debts. The Court of Appeal cited another judgment of a ship arrest case of the Court of Appeal of Las Palmas.

Conclusion: These judgments are very interesting news for creditors that have no other option, or recourse available, when they hold good evidence to pierce and lift the veil, thus enabling them a last shot to collect payment. They must take into account that under Spanish law they will be required to post a minimum of 15% of the claimed amount as counter security and if they lose, owners may claim damages. Often, owners will be persuaded to lift the arrest and post security reducing the potential claim in damages to the legal interest accrued over the amount bailed.

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Upcoming Events

Arrested Vessel for Auction

MT OLESYA

Auction Date: 08/04/19
Location: Trinidad
Type: Tanker
Size: 9133 dwt
Built: 12/2009 Dongfan
IMO: 9510591

The vessel has been arrested in Trinidad since January 2018 or earlier for repairs to the main engine gearbox, which will need to be completed by the buyer. Offers are invited for submission to the exclusive brokers, CW Kellock & Co Ltd. More auction details found HERE

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