OWNERS OF THE "BLUEYED LADY" v. DEN NORSKE BANK A.S.

COURT OF APPEAL (Fieldsend, P., Davis and O'Connor, JJ.A.): March 21st, 1994

Shipping—forced sale of ship—strength of case for sale—applicant to show good reason (beyond balance of convenience) for sale under Rules of Supreme Court, O.29, r.4—more critical examination of applicant's case required on defended application than in default action

Shipping—forced sale of ship—adequacy as security for debt—prima facie case for sale under Rules of Supreme Court, O.29, r.4 if ship no longer good security for debt—no sale merely because realizable value diminishing during arrest—exception if owner deliberately delaying proceedings or no bona fide defence to claim

Shipping—forced sale of ship—interests of other creditors—if ship good security for primary debt, irrelevant that may not cover claims with lower priorities—interests of other creditors not positive consideration under Rules of Supreme Court, O.29, r.4 unless likely to be prejudiced by sale—creditor so prejudiced may intervene

The respondent applied for the appraisement and sale of the appellant's ship *pendente lite.*

The respondent bank advanced moneys to the charterer of the appellant's ship for repairs. The loan was guaranteed by the appellant, whose obligations were secured by a mortgage of the ship. The appellant's owner gave a counter-guarantee. Following a dispute with the charterer, the appellant terminated the charterparty, entitling the respondent to call in the loan. Neither the charterer nor the appellant met its obligations and the respondent arrested the ship in Gibraltar and instituted proceedings against the appellant under the mortgage, claiming the amount of the loan plus accrued interest. Each party valued the ship at a sum exceeding the loan, and there were other creditors with claims against the ship of both lesser and higher priority than the respondent.

The respondent obtained an order from the Supreme Court for the appraisement and sale of the ship, under O.29, r.4 of the Rules of the Supreme Court, pending the determination of the bank's action against the appellant. The court considered as factors relevant to the exercise of its discretion: (a) the owners' failure to insure the ship or give other security for the bank's claim; (b) the existing and contemplated litigation in Gibraltar and England against the appellant and its owner; (c) the likelihood that the

ship would remain berthed for a further 6–12 months; (d) the fact that the ship was being kept at the bank's considerable expense; and (e) the fact that its value would diminish whilst the bank's expenses remained constant.

On appeal, the appellant submitted that (a) since a sale would deprive it of its property before the determination of the claim against it, the bank must prove beyond the balance of convenience that a sale was necessary; (b) a sale was unnecessary, as the ship constituted sufficient security for the bank's claim; and (c) the fact that its value would be diminished by the continuing costs of arrest did not itself justify an order for sale.

The respondents submitted in reply that (a) the value of the ship as security was uncertain, since it would deteriorate whilst in dock without adequate maintenance and the market for tankers fluctuated considerably; and (b) the interests of other creditors must be considered, including those ranking below the respondent in priority.

Held, allowing the appeal and setting aside the order:

(1) An order under O.29, r.4 of the Rules of the Supreme Court should not be granted except for good reason. The respondent was required to prove its case for sale beyond the balance of convenience and, since the proceedings were defended and the appellant opposed the application, the court must examine the issue more critically than it would in a default action. The primary consideration was whether the ship remained good security for the bank's claim. If not, there was a *prima facie* case for ordering its sale. If the ship remained sufficient security, the mere fact that it incurred further liabilities whilst under arrest which diminished its net realizable proceeds would not justify its sale. Other circumstances, however, *e.g.* the owner deliberately delaying the proceedings or doubt as to the *bona fides* of its defence, might justify sale even if the value of the ship sufficed to cover the debt (page 288, lines 20–32; page 289, lines 16–25; page 291, lines 5–20; page 292, lines 15–20).

(2) The interests of other creditors were not to be regarded as a positive factor to be taken into account. If the ship constituted good security for the claim, it was irrelevant that its value might not cover other claims with lower priorities. The court might refuse an order for sale if other creditors were likely to be prejudiced by it, and a creditor who believed he would be so prejudiced could intervene (page 290, line 33 – page 291, line 8; page 292, lines 29–34).

(3) On the evidence, the ship remained good security for the appellant's debt, and none of the other reasons which might justify an order for sale was present here. The appeal would be allowed and the order set aside (page 289, lines 22–25; page 291, line 44 – page 292, line 14; page 292, lines 21–26; lines 35–40).

Cases cited:

(1) *Castrique* v. *Imrie* (1870), L.R. 4 H.L. 414, considered.

(2) *Gulf Venture (No. 2), The*, [1985] 1 Lloyd's Rep. 131, followed.

(3) *Hadmor Prods. Ltd.* v. *Hamilton*, [1983] 1 A.C. 191; [1982] 1 All E.R. 1042, applied.
(4) *Myrto, The*, [1977] 2 Lloyd's Rep. 243; on appeal, [1978] 1 Lloyd's Rep. 11, followed.

Legislation construed:
Rules of the Supreme Court, O.29, r.4(1): The relevant terms of this paragraph are set out at page 288, lines 11–17.

A.J.S. Glennie, Q.C. for the appellant;
H.B. Eder, Q.C. for the respondents.

FIELDSEND, P.: This is an appeal against an order for the appraisement and sale of the *Blueyed Lady* pending the determination of an action by the Den Norske Bank ("the bank") against Oltenia Shipping Corporation, the owner of the ship ("the owner").

For the purposes of this appeal, the background can be dealt with very shortly. In September 1992 the owner chartered the ship to Blueyed Navigation Inc. ("the charterer") under a bareboard charter, the charterer being obliged to have done a considerable amount of work on the ship, and being authorized to borrow US$8m. for that purpose. Under a series of agreements the bank advanced the charterer US$8m., whose obligations under the loan were guaranteed by the owner, which obligations were in turn secured by a mortgage of the ship and a collateral agreement. The owner's parent company, Petromin, gave a counter-guarantee of the owner's obligations to the bank.

Following a dispute between the owner and the charterer, the owner terminated the charterparty, which entitled the bank to reclaim the US$8m. advanced to the charterer. Neither the charterer nor the owner has met its alleged obligations and the bank has instituted proceedings in Gibraltar against the owner under the mortgage, having arrested the ship here. The bank is also suing Petromin in England under the counter-guarantee. All these proceedings are defended.

The bank obtained an order from the Gibraltar court for the appraisement and sale of the ship, and it is against this order that the owner now appeals.

The bank's claim is for US$8m. plus interest up to December 13th, 1993 of US$88,615.91 plus further interest as it accrues. This, it was accepted, would be at the rate of US$50,000 to US$60,000 a month.

There are other creditors with claims against the ship, namely: (a) the charterer, with a claim of some US$10m., which would rank below that of the bank; (b) the American Bureau of Shipping, with a claim of US$256,000 for Classification Society fees, which it can be expected will be paid by the Admiralty Marshal and will rank above that of the bank; (c) Wallem Ship Management, with a claim of US$215,000, which may

rank above that of the bank; and (d) A.P. & A. Ltd., with a claim of US$1.9m., which would rank below that of the bank.

There were two desk valuations of the ship, one by each of the parties, which valued it in December 1993 at between US$12m. and US$13m. It was accepted too that the continuing costs of arrest would amount to about US$120,000 a month or US$1.4m. a year.

The application for appraisement and sale was based upon O.29, r.4 of the Rules of the Supreme Court, as applied in *The Myrto* (4) ([1977] 2 Lloyd's Rep. at 260) and *The Gulf Venture* (2) ([1985] 1 Lloyd's Rep. at 134). Order 29, r.4(1) reads:

> "The Court may, on the application of any party to a cause or matter, make an order for the sale by such person, in such manner and on such terms (if any) as may be specified in the order of any property (other than land) which is the subject-matter of the cause or matter or as to which any question arises therein and which is of a perishable nature or likely to deteriorate if kept or which for any other good reason it is desirable to sell forthwith."

These two cases do no more than set out, in very general terms, the criteria to be applied by the court in exercising its discretion as to whether or not to grant such an application. In summary, it is said that a court should not grant the application except for good reason, whether the proceedings are defended or not, but where they are defended and the defendants oppose the making of the order it must examine more critically than it would in a default action the question whether good reason for the making of the order exists or not: see *The Myrto* ([1977] 2 Lloyd's Rep. at 260, *per* Brandon, J.).

It must be borne in mind that the effect of ordering a sale will be to deprive an owner of his property before the determination of the claim against him, and that is the reason why there must be a good reason for the grant of the order. There must be something more than a mere balance of convenience in favour of a sale, and it is for the applicant to establish this. Where, however, a creditor with a claim greater than the value of the ship which secures it can see his security diminishing day by day because of the continued arrest, there would seem to be a good *prima facie* case for ordering a sale because, in those circumstances, the care the creditor has taken to secure his claim will be progressively lessened with the passage of time.

Mr. Glennie, for the appellant owner, contended that in this particular case the primary point—if not the only point—for consideration is whether or not the ship constitutes a sufficient security for the bank's claim and will continue to do so for the reasonably foreseeable future. So far as the future is concerned, it was accepted that the disputed claim by the bank should be determined at the latest by the end of 1994.

On the facts, he argued that the value of the ship at present could be taken as US$12m., and that about US$1.4m. should be allowed for

continuing expenses to be met. Ahead of the bank's claim there might be claims with higher priority totalling about US$471,000. Accordingly, the proceeds at the end of the year from the sale of the ship should be not less than US$10m., against the bank's claim including interest being then no more than US$8.8m. This, he contended, was an ample margin upon which the court below should have concluded that, on this basis, there was no good reason for ordering a sale *pendente lite*.

Mr. Eder, Q.C., for the bank, contended that the figure for the value was speculative having regard to the fact that the vessel must deteriorate whilst in dock without adequate maintenance, and that the figure of US$12m. to US$13m. was uncertain anyway due to the fluctuating market for tankers where oil prices varied. On such facts, he argued that the bank's security was not as great as contended for by the owner. He stressed that a ship left in dock under arrest was a wasting asset, the value of which would diminish, so providing less security.

The mere fact that a ship remains under arrest, incurring further liabilities which diminish its net realizable proceeds, cannot itself be a good reason for ordering a sale *pendente lite* against the wishes of the owner. This is the automatic result of keeping a ship under arrest and, in my view, something more must be required to constitute a good reason. This may be that the ship's value is unlikely to realize sufficient money to meet the claim of the petitioning creditor. It could be that an owner is deliberately delaying the proceedings or that its defence, whilst not frivolous, is so doubtful as to suggest that it is not *bona fide*. Neither of these last two factors is applicable here.

This brings me to the point so strongly urged by Mr. Eder that consideration must be given to the interests of other creditors, including even those who rank in priority below the bank. He starts from the *dictum* of Blackburn, J. in *Castrique* v. *Imrie* (1) (L.R. 4 H.L. at 428):

> "Our Courts of Admiralty, when property is attached and in their hands, on a proper case being shown that it is perishable, order … that it shall be sold and the proceeds paid into Court to abide the event of the litigation. It is almost essential to justice that such a power should exist in every case where property, at all events perishable property, is detained."

There is a footnote to the word "order" reading "For the benefit of all parties concerned." This footnote (presumably added by the editor of the law report) was specifically noted by Brandon, J. in *The Myrto* (4) ([1977] 2 Lloyd's Rep. at 259).

In the latter case, the plaintiff's bank had a claim for US$1.96m. secured in part by a first mortgage and in part by a second mortgage. The value of the ship was about US$650,000. There were other persons who, it was alleged by the owners, might be prejudiced by an order, namely the charterers and owners of a cargo on board.

The owners contended that the fact that the value of the property as security for the plaintiff's claim would be diminished by the continuing cost of maintaining the arrest was not a special reason for making an order. Brandon, J. held ([1977] 2 Lloyd's Rep. at 260) that as a matter of law, such diminution of value could amount to a good reason and might often do so, as in his view it did in that case. Indeed, that must have been so, as the security which was, on the facts, insufficient was being further eroded daily.

Mr. Eder relies upon another passage (*ibid.*) where, having referred to the continuing erosion of the security, Brandon, J. also said this diminution of value would be "to the disadvantage of all those interested in the ship including, if they have any residual interest, the defendants." This is far from saying that he was taking into account as a positive factor in favour of ordering a sale the interests of other creditors. It is merely an indication that other parties would not be prejudiced by the order.

In *The Gulf Venture (No. 2)* (2), a plaintiff with a claim of about £410,000 arrested the ship in July 1984 and applied in October 1984 for an order for appraisement and sale on the basis that the ship was a wasting asset costing over £5,000 a month to maintain. The value of the ship was said to be £425,000.

There were other potential creditors, including two mortgagees, one with a claim of about £2.6m. Apparently, the second mortgagee opposed the application, being fearful that the first mortgagee would be entitled to the whole of the net proceeds of the sale, leaving the second mortgagee unsecured. As Sheen, J. said ([1985] 1 Lloyd's Rep. at 136), a continuation of the arrest could not assist the second mortgagee. It had also been argued for the defendants that if an order were granted the plaintiffs would be disadvantaged, in that there was a risk that the mortgagees would intervene with a prior claim and the plaintiff would get nothing. The learned judge held (*ibid.*, at 134) that if the mortgagees were going to intervene, the sooner the better, as it would save the plaintiffs further costs.

In short, neither of these cases supports Mr. Eder's argument that the interests of creditors other than the one applying for an order for sale are to be regarded as a positive factor to be taken into account. If, of course, they might be prejudiced by the order, that may be a factor to refuse an order.

The various references to the need to sell a ship *pendente lite* "for the benefit of all creditors" do no more than point to the fact that the sale is not for the sole benefit of the creditor seeking the order. Indeed, each creditor will participate according to the priority of its claim in the net proceeds. They also point to the fact that if a creditor thinks he may be prejudiced by a sale *pendente lite*, he may intervene.

In my view, Mr. Glennie's contention is correct, namely, that the primary point for consideration is whether the ship constitutes a sufficient

security for the claim of the creditor seeking an order for sale *pendente lite*. If it does constitute sufficient security, it is irrelevant that there may be other claims with later priorities which might not be covered by the value of the ship. They will not of themselves provide a good reason, especially in a contested case, for the grant of an order. Of course, as I said earlier, there may be some other circumstances, such as unwarranted delay by an owner, which may amount to a good reason, even if the security is sufficient to cover the debt said to be owed to the applicant.

The learned judge purported to adopt the approach enunciated by Brandon, J. in *The Myrto* (4) and by Sheen, J. in *The Gulf Venture (No. 2)* (2) that the application should not be granted except for good reason, whether the proceedings were defended or not. But where they were defended and the defendant opposed the making of the order, the question of whether there was good reason for the granting of the order had to be examined more critically.

The issue is whether, in applying this approach, he exercised his discretion properly (see *Hadmor Prods. Ltd.* v. *Hamilton* (3)). In my view, the primary basis—if not the only basis—in this case upon which good reason could be found for ordering a sale *pendente lite* would have been that the ship provided insufficient security for the bank's claim.

The learned judge set out the factors which—disregarding the claim of other creditors—led him to order a sale. These seem to have been:

(a) the inaction of the owner in taking steps to insure the ship or to give security for the bank's claim;

(b) the actual and contemplated litigation in Gibraltar and England;

(c) that the ship was likely to remain berthed for at least 6 months or more, and probably for 12 months or more;

(d) that the ship—a deteriorating asset—was being kept at considerable and unreasonable expense to the bank; and

(e) there would be a substantial diminution of its value and no lessening of the heavy burden on the bank of maintaining the arrest.

As to the owner's inaction, I do not think that it is a relevant consideration that the owner cancelled the P. & I. and H/M insurance on November 11th, 1993, when the ship was in Gibraltar and the charterparty had been cancelled, nor that since November 18th, when the ship was arrested, the owner has taken no steps to give security or to maintain the ship. Having no charterer for the ship, it is not surprising that the owner has taken no steps to obtain its release. And in any event, the bank alleges that the ship is the owner's only asset. To give security for its release could easily limit its financial position so far as to make it difficult to meet the costs of the pending action.

For the rest, the factors are all matters which could have relevance in a case such as this, but with respect to the learned judge, they are really

only of importance if they lead to the conclusion that the ship will cease to provide security for the bank's claim. It was vital, therefore, for a calculation to be made as to the adequacy of the ship to secure the bank's claim. This the learned judge does not seem to have done save in the most general terms.

On the figures that emerge from the evidence which I have set out earlier, the ship should realize not less than US$10m. against the bank's claim by then of some US$8.8m.

This would seem to provide an adequate margin of security for the bank. It is true that the affidavit of the bank's solicitor alleged that the value of tankers was "notoriously variable" and could fall millions of dollars even over a month. Such an allegation cannot be given much weight in undermining the valuation of the bank's experts on December 23rd which must be taken to stand today in the absence of any correction.

It is, after all, for the applicant in a case such as this to establish the facts upon which it contends that there is "good reason" for forcing an owner to part with his property against his will before it is established that he is under a liability to the applicant. It is not enough for an applicant to show, for example, as contended in the respondent's heads of its argument, that this security is "at least very doubtful."

Had the learned judge properly weighed the value of the ship, even as at the end of 1993, against the amount of the bank's claim at that time, he cannot but have concluded that it constituted sufficient security. In that event it would have been wrong to have ordered a sale. *A fortiori* it shows a misapprehension of the evidence to have ordered a sale in January 1994. Of course if circumstances change and further facts emerge, such as a fall in the value of ships like the *Blueyed Lady*, it would always be open to the bank to renew its application.

If the learned judge's decision was based at all on actual or potential claims taking precedence only after the bank's claim, that in my view would have been an error of principle. The authorities seem to say that such claims may possibly be a factor against granting an order for sale, but an applicant creditor cannot pray them in aid in support of his application.

In my view, the learned judge did not sufficiently weigh the relevant evidence as to the adequacy of the security, and the court is entitled to consider the whole question and substitute its own judgment.

In my view, the bank did not sufficiently make out its case for a sale *pendente lite*. The appeal must be allowed and the order for appraisement and sale set aside. There will be liberty to apply.

DAVIS and **O'CONNOR, JJ.A.** concurred.

Appeal allowed.