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Industry insight: Hanjin collapse washes up on Australian shores

Hanjin is the latest casualty of the slump in freight rates and oversupply of tonnage. The company was placed into receivership by a Seoul court on 1 September 2016. Hanjin collapsed with debts totalling over USD5 billion. At the time of the collapse, Hanjin had 97 container ships, of which 60 were chartered by the company and 37 were owned by Hanjin. It was South Korea's largest container company.

The South Korean court handling Hanjin's insolvency proceedings has announced plans to dispose of Hanjin's subsidiaries involved in handling Asia-US cargo, along with staff, vessels and 10 overseas operations. The Seoul court is fielding interest from potential buyers; bidders are required to submit proposals by 4 November 2016. It is not yet known if any companies have shown any interest in the assets. The sales plan comes as creditors continue to prepare claims for recovery of debts owed by the collapsed company.

Since its collapse, Hanjin has been seeking to have the South Korean receivership proceedings recognised in more than 30 jurisdictions, so as to obtain a stay of any arrest proceedings commenced against the company's property. As of last month, Germany, Singapore, Spain and the United States have recognised these proceedings. China has not recognised the receivership proceedings, as the country's law do not have such provisions.

At least ten of Hanjin's vessels have been arrested globally, including the recent arrest of the container ship Hanjin California in Sydney Harbour for a bunkering debt. These vessel arrests present a difficulty for both the company and its shippers, with approximately USD14 billion worth of merchandise packed into containers on board Hanjin vessels. The company has been unable to disclose how many containers have been affected by the arrests, as some vessels have been able to discharge their cargo.

Key issues

- In an insolvency context, Australian courts distinguish between proceedings to enforce an existing security right such as a maritime lien, and proceedings to satisfy a judgment out of proceeds of sale of a ship. Only the former can proceed as an action by a secured creditor within the exception allowed under s471C of the *Corporations Act*.
- Timing is crucial to the question of whether the court will allow proceedings concerning statutory rights *in rem* to proceed in the face of a cross-border insolvency. Under Admiralty law, a secured interest only attaches upon the writ being filed.
- First instance decision in *The Sam Hawk* was overturned on appeal. The decision of the Full Federal Court of Australia limits the range of liens that can found a ship arrest.

Given the international nature of both Hanjin's business and its insolvency

proceedings, the arrest of the Hanjin California raises two hot topics in shipping law:

1. Can foreign bankruptcy proceedings limit the rights of maritime claimants to arrest ships, and obtain security for their claims ahead of other creditors in cross-border insolvency situations; and
2. Under what law should the validity of any such maritime claims be assessed – the *lex causae* (law of the cause) or the *lex fori* (law of the forum)?

We will explore each of these questions in turn.

Ship arrests v cross-border insolvency: Two worlds collide

When a ship that is owned or chartered by a company that is the subject of foreign bankruptcy proceedings enters Australian territorial waters, the company's foreign insolvency representative may apply to the Australian courts under the *Cross-Border Insolvency Act 2008* (Cth) (**CBIA**) for an order that those foreign proceedings be "recognised". Recognition results in an automatic stay of proceedings, which prevents the commencement or continuation of any proceedings or execution against any of the assets of that company, and allows the foreign representative to seek a range of orders to assist them in carrying out the cross-border restructure or liquidation of the debtor's assets. The scope of that stay is subject to Australia's insolvency laws, which relevantly includes s471B and C of the *Corporations Act 2001* (Cth) (**Corporations Act**).

The effect of s471B is largely the same as the CBIA: while a company is being wound up, proceedings against it or in relation to the company's property (or enforcement process in relation to such property) cannot begin or proceed, except with leave of the court. Section 471C operates as an exception to s471B in respect of a secured creditor's right to realise or otherwise deal with the security interest.

The effect of foreign bankruptcy proceedings (and the associated stay of local proceedings) on the rights of creditors to arrest ships is dependent on whether their claims give rise to a "security interest" within the meaning of s471C. It is therefore necessary to consider the nature of the claims that give rise to the right to arrest a vessel under the *Admiralty Act 1988* (Cth) (**AA**), such claims are maritime liens and proprietary claim or general maritime claims in respect of the vessel or other property.

An important distinction between a maritime lien and a proprietary or general maritime claim, is the timing at which the secured interest attaches.

- A maritime lien is created at the time of the occurrence of the event from which the lien arises, unlike a proceeding *in rem* on a general or propriety maritime claim, and travels with the ship as a secured right of the injured party, regardless of changes in ownership or the granting of subsequent mortgages or charges, until the lien is discharged: *Kim v Daebo International Shipping Co Ltd* [2015] FCA 684. On this basis, *in rem* proceedings commenced in respect of a maritime lien are brought for the purpose of enforcing a pre-existing security: *Yu v STX Pan Ocean Co Ltd (South Korea), in the matter of STX Pan Ocean Co Ltd (receivers appointed in South Korea)* [2013] FCA 680 at [40].
- A claimant who commences *in rem* proceedings on a proprietary or general maritime claim against a ship has a secured interest in respect of that claim that arises at the time those proceedings are commenced: *Kim v Daebo International Shipping Co Ltd* [2015] FCA 684; *Programmed Total Marine Services Pty Ltd v "Hako Endeavour", "Hako Excel" and "Hako Esteem"* [2014] FCAFC 134.

This distinction is important. Section 471C preserves the rights of secured creditors to commence proceedings or an enforcement process to realise their "security interests". An action *in rem* to enforce a maritime lien falls within the exception provided by s471C, in that the claimant's "secured interest" may arise prior to the recognition of foreign bankruptcy proceedings (and the automatic stay), such that the stay will not affect any arrest proceedings: *Yu v STX Pan Ocean Co Ltd (South Korea)* [2013] FCA 680; *Kim v SW Shipping Co Ltd* [2016] FCA 428.

Timing is crucial in respect of proprietary and general maritime claims. Although this question of law has not been settled, it is possible that arrest proceedings commenced in respect of a proprietary claim or general maritime claim after the recognition of the foreign bankruptcy proceedings may fall outside the exception in s471C, as the claimant did not have a "secured interest" prior to the bankruptcy proceedings: *Kim v*

Daebo International Shipping Co Ltd [2015] FCA 684 at [8].

Given the privileged position occupied by maritime liens in a cross-border insolvency context, in light of recent case law, it is important to give consideration to the scope of claims that will be recognised as maritime liens by Australian courts.

Arrest of the "Sam Hawk": based on foreign maritime lien

Clifford Chance has published two detailed briefing notes concerning the Federal Court's decision in *Reiter Petroleum Inc v Ship "Sam Hawk"* [2015] FCA 1005, and its subsequent appeal in *Ship "Sam Hawk" v Reiter Petroleum Inc* [2016] FCAFC 26. On this basis our remarks here will be brief.

At first instance in *The Sam Hawk,* the Federal Court of Australia held that a vessel could be arrested under the AA based on a foreign maritime lien. The court held that the validity of foreign maritime liens is a question of substantive, not procedural, law and on this basis, its validity is to be determined by the foreign *lex causae* not the local *lex fori*. The court recognised that its *in rem* jurisdiction can be enlivened by a claim which gives rise to a maritime lien under foreign law, even if that claim is not recognised as a maritime lien under Australian law; meaning an expanded range of maritime liens could be claimed.

The decision was however unanimously overturned on appeal on 28 September 2016. Now a foreign maritime lien is not recognised in Australia as a basis for an arrest unless the claim corresponds or is sufficiently analogous to a claim that is recognised as a maritime lien under Australian law. By a majority of 4:1, the court held that whether a maritime claim is capable of being recognised as a maritime lien is determined by the *lex fori*, being Australian law (not the foreign law). The AA provides a limited list of claims which give rise to a maritime lien. Although Rares J upheld the appeal, his Honour was firmly in dissent on the question of how the validity of a maritime lien is to be addressed; holding that the existence of a lien is a matter of substantive, not procedural law, and as such, the proper law governs the determination of the parties' rights, not the law of the forum. It is not yet known whether the respondent will seek leave to appeal this decision; so it remains to be seen what the final state of Australian law will be on this question. In the meantime, a number of ships arrested on the basis of the first instance decision are now being released.

For further reading on this topic, we direct you to our briefing notes which are available at http://www.cliffordchance.com/briefings/2015/12/landmark_decisionarrestofthevesselsa.html and https://www.cliffordchance.com/briefings/2016/10/beware_of_foreignmaritimeliensaustralia.html.

In light of the Full Federal Court's decision, any creditors of Hanjin seeking to arrest its vessels in Australian waters on the basis of a maritime lien, should first ensure the circumstances giving rise to that claim are also recognised as a maritime lien under the AA.

Conclusion

The collapse of Hanjin, and the arrest of one of its vessels in an Australian port, serves to highlight the current tension in Australian law. On the one hand, the courts have shown a willingness to cooperate with foreign courts in cross-border insolvencies and restructuring proceedings by recognising and upholding foreign proceedings, while yet preserving the privileged position occupied by maritime creditors. However, on the other hand, the finding in the appeal of *The Sam Hawk*, that maritime liens are determined according to the *lex fori*, appears somewhat inconsistent with the internationalist approach to creditors' rights contained in the Model Law, which has been enacted in Australia under the CBIA.

Contacts

Pat Saraceni
Director of Litigation and Dispute Resolution
T: +61 8 9262 5524
E: pat.sarceni@cliffordchance.com

Kate Sherrard
Partner
T: +65 6661 2023
E: kate.sherrard@cliffordchance.com

Nicholas Summers
Associate
T: +61 8 9262 5538
E: nicholas.summers@cliffordchance.com

Gervais Green
Partner
T: +65 6410 2252
E: gervais.green@cliffordchance.com

Alastair Macaulay
Consultant
T: +852 2825 8988
E: alastair.macaulay@cliffordchance.com

Clifford Chance, level 7, 190 St Georges Terrace
Perth, WA, 6000, Australia

www.cliffordchance.com