SUN MOBILITY
Insurance and Claims Services Limited

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To: Transport Industry Operators

Ship release's security

On 9/5/2008, the Hong Kong High Court ordered the shipowner of the "Hua Tian Long" to provide security of US$65 million before the vessel can be released from arrest.

This case raised a point of Admiralty law and practice not often ventilated, namely that of fixing the amount of bail for an arrested vessel, absent agreement between the shipowner and the arresting party. The "Hua Tian Long" is a large floating derrick/crane with very substantial lifting ability. In technical terms it is described as a '4000 ton Revolving Construction Barge'. Normally it is based in Guangdong, but its services urgently were required in Hong Kong in order to salvage a sunken Ukrainian tug which recently was in collision with another vessel in the harbour, and which sadly sank with substantial loss of life. The "Hua Tian Long" had succeeded in lifting the unfortunate Ukrainian tug from the seabed to the surface. The "Hua Tian Long" was arrested after it had completed this salvage job, and prior to its return to Guangdong. The plaintiff is a Malaysian company with whom the defendant ("shipowner") entered into a Charterparty dated 1/2/2007 and signed on 3/2/2007. Under this Charterparty the plaintiff ("charterer") had agreed to hire the vessel "Hua Tian Long" for a minimum period of 100 days from the date of delivery, which was specified to be on or around 15/6/2007. The charterer is in the business of providing professional engineering, project management, procurement, construction and fabrication, transportation and installation and retrofitting and commissioning activities in terms of projects in the oil and gas, building and infrastructure industries. The particular work for which the charterer had required the services of the "Hua Tian Long" was construction work relating to offshore oil developments for Newfield Malaysia Inc and Talisman Malaysia Ltd and other third parties. The charterer successfully had bid for these projects, and thus had required the services of the "Hua Tian Long" in order to fulfil its own contractual commitments: hence an initial Memorandum of Agreement signed by both charterer and shipowner on 19/1/2007, the subsequent Charterparty of 1/2/2007, and a further Memorandum of Agreement dated 1/2/2007.

The charterer's case was that the shipowner let it down; the "Hua Tian Long" never was delivered, and by letter dated 7/11/2007 the shipowner had finally intimated its intention not to deliver the vessel. The barge was not delivered because, the charterer said, it was on-hire elsewhere, notwithstanding 'Letters of Commitment' which the charterer said it variously had received from the shipowner. Accordingly, the charterer maintained that it had suffered very substantial loss and damage, and that it was forced to take steps to mitigate the allegedly extensive losses caused by the substantial delays to the projects the charterer itself was obliged to perform, delays which the charterer said were directly consequential upon the non-delivery of the "Hua Tian Long". Nor did the charterer relied simply on a cause of action in contract for breach of the charterparty; in addition the general indorsement upon the writ *in rem* pleaded a case in fraudulent/negligent misrepresentation against the shipowner arising as a result of various representations contained in Letters of Commitment issued by the shipowner on 25/12/2006 and 10/1/2007, the Memorandum of Agreement of 19/1/2007, and a letter confirming the Confirmation of the Charter dated 24/1/2007. The variety of the charterer's alleged consequential losses was set out in schedules in its lawyer's affidavit backing the warrant of arrest – an affidavit in which it *then* was alleged that the scale of this claim against the shipowner was in or around US$59 million, including interest and costs.

In normal course the issue of the amount of money required to be posted in the form of a bail bond or other security never is publicly canvassed. For the most part arrested vessels are entered with a P&I Club, which generally offers the security demanded in the form of a standard letter of undertaking, and the vessel thus is immediately released.

However, the "Hua Tian Long" is not entered with any P&I Club, and is, in effect, owned by a department of the Chinese Government. The Chinese shipowner had taken exception to the amount of bail thus demanded by the charterer in this case. The shipowner disputed the demand made by the charterer and referred to its application to strike out the action, and further to the existence of an arbitration clause within the charterparty, and to the consequent possibility of an application for a stay of the proceedings in favour of arbitration. The shipowner subjected the charterer's claim for loss and damage to critical comment, and objected to the adequacy of the documentation as being insufficient to maintain such a claim for security. The shipowner asserted that the claim for

loss was significantly overstated, and said that "according to our own calculation, their claim for these items of losses should be no more than US$37,083,372.77".

Clearly, therefore, there was an impasse between the parties as to how much this claim was worth, and hence the amount of security correspondingly to be provided in order to procure the release of the shipowner's vessel. At the same time, the "Hua Tian Long" was languishing under arrest in the harbour, under the supervision of the Court Bailiff, and by reason of the arrest the shipowner was losing hiring fees for this barge of in the order of some US$100,000 per day.

On 28/4/2008, the shipowner issued a Notice of Motion asking that the writ and the action be struck out, that the warrant of arrest of the "Hua Tian Long" be set aside and the vessel released from arrest, and that there be an inquiry into damage suffered by the shipowner as the result of the arrest. The grounds prayed in aid for the Motion were that the charterer's action did not fall within the Admiralty jurisdiction of the High Court, that the affidavit leading the warrant of arrest did not establish that the charterer was entitled to bring an admiralty action *in rem* against the shipowner and to arrest the vessel, and that the charterer's claim was scandalous, frivolous and vexatious and an abuse of process. It was entertained by Reyes J, the Admiralty Judge, at an urgent hearing on 30/4/2008, and consequent upon that hearing the learned Judge ordered that the shipowner's application to strike out the writ and the action be dismissed, the application to set aside the warrant of arrest be dismissed, and that the costs of the Motion be to the charterer, to be taxed if not agreed. The hearing of the Motion did not take a great deal of time, and that the Admiralty Judge had no difficulty in divining that the admiralty jurisdiction of the Hong Kong court indeed had been engaged: hence his Order.

The charterer sought a very substantial increase upon the amount of security initially sought, and in lieu of the US$59 million figure within the affidavit leading the arrest, sought a sum in security of in or around US$140 million.

The court's power to order the release of a vessel from arrest is discretionary; it may order the arrested vessel to be so released absent any security being provided: see *Meeson, Admiralty Jurisdiction and Practice*, (3rd ed), para 4.65, at 143. As an integral element of its power to order the release of a vessel from arrest, the court may determine the amount of security required to secure the release of the vessel: see *"The Moschanthy"* [1971] 1 Lloyd's LR 37, in which Mr Justice Brandon (as he then was) stated, *op cit*., at 44:

> *"The principle to be applied is, in my view, as follows: The plaintiff is entitled to sufficient security to cover the amount of his claim with interest and costs on the basis of his reasonably arguable best case…"*

The right of arrest and the associated power to exact security is a strong power which must not be used oppressively. The power of the court to order the release of the arrested vessel and to control the amount of security is derived from its inherent jurisdiction to prevent abuse of the process of the court or the use of court procedure in an oppressive manner: see *The "Polo II"* [1977] 2 Lloyd's LR 115.

The Judge took the view that the shipowner's applications should not be permitted to become over-complex affairs – just as, in the Commercial Court, for example, applications for security for costs are treated very much on a 'broad brush' basis. At such early interlocutory stage, the court had to get a 'feel' of the case, and thereafter to exercise its best judgment, in accordance with established principle, as to the correct figure to order in terms of security, but in the Judge's view it most definitely was *not* the case that the judge had to accept at face value the assertions made by the plaintiff, *qua* arresting party, as to the probable value of its claim; were this to be the position, the task of the judge would be no more than administrative, and the Judge rejected such thesis unequivocally.

The shipowner mounted a strong attack against the security sought by the charterer. The shipowner's argument essentially was threefold. First, the shipowner maintained that all that was before the court, at least at the time of the arrest, consisted of 'bare assertions' only within the affidavit of the charterer's lawyer, and that the charterer had placed no admissible evidence before the court in support of the figure that it had put forward as representing the amount of the alleged loss. The Admiralty jurisdiction was a "draconian jurisdiction". The arrest of the vessel inevitably would cause financial loss, and there was every reason to believe, should the shipowner succeed at trial, that it will be very difficult to obtain sufficient compensation from the charterer in respect of the losses arising from this arrest. Moreover if the shipowner was unable to obtain the release of its vessel by the due provision of security, the vessel then was sold *pendente lite*, the circumstances of such court-ordered sale generally ensuring that she was sold for considerably less than her actual value – which in this case appeared to be of in the order of US$150 million, according to a report of a ship broker. And even if the shipowner were to succeed at trial, the prospects of achieving redress in respect of the arrest (in terms, for example, of precluding the release of the vessel save at a grossly inflated security figure) were limited. In the circumstances, therefore, the shipowner submitted that the charterer was under an obligation to ensure that the affidavit leading the warrant properly deposed to all material facts which were said to justify the invocation of the admiralty jurisdiction: see *The "Asian Atlas"*, CACV 257 of 2007, Judgment of the Court of Appeal dated 11/4/2008. Second, and without prejudice to the contention that the

material before the court at the time of arrest was deficient and insufficient, the shipowner made several points as to the quality of the information / evidence subsequently prayed in aid by the charterer, in the form of a lately-filed Affirmation of one executive director of the Malaysian charterer wherein the amount of the claim appeared to have increased from the amount of US$59.8 million to a sum which was at US$140,699,732. In terms of the strength or otherwise of the underlying claim as to liability, the shipowner drew the attention of the court to Clause 14 of the 2nd Memorandum of Agreement, allegedly signed on the same date as the Charterparty, that is, 3/2/2007, which had made it clear on its face that the Charterparty expressly was subject to the shipowner obtaining approval from the China Offshore Oil Engineering Company – which had *not* been obtained. The shipowner also drew the attention of the court to Clause 14(c) of the Charterparty itself, which was headed 'Consequential Damages', and which on its face appeared to rule out liability "for any consequential damages whatsoever arising out of or in connection with the performance or non-performance of this Charter Party" – and yet, said the shipowner, all save about US$7 million of the sums variously claimed would fall into such category of 'consequential loss'. Third, the shipowner mounted a spirited attack on the charterer's figures for alleged loss and damage, and in particular the shipowner criticized the figures put forward for adapting for heavy lifting other existing barges already in use on the project as containing a substantial element of double counting. The shipowner characterized the claim for security as "oppressive". From the viewpoint of the shipowner, the most that should be put up was the relatively nominal figure, inclusive of interest and costs, of in or about US$10.186 million.

The charterer maintained that the sum of US$140.6 million was both proper and achievable, and the charterer asked the court to order such amount in order for the vessel to be released from arrest. The charterer made the point that at the date of the affidavit leading the arrest the figure of US$59.8 million, inclusive of interest and costs, was of necessity provisional only, and that when the charterer had had more time to consider the loss and damage position it had transpired that such figure had had to undergo substantial revision; indeed, the charterer's lawyer in his affidavit had stressed that he "reserved the right to add to the claims as and when further details of loss and damage become available", and thus there should be no criticism of such revision as had occurred.

Upon the court pointing out, as a matter of basic contract law, that a party claiming for breach of contract could mount a claim for loss of profit *or* wasted expenditure, but not for both. The claim for some US$33.449 million could not be supported by reason of the application of this principle.

In the event, the charterer was minded to ask for a sum of US$80 million in security. As to the liability objections, the charterer suggested that the court should not be drawn into a liability debate at this stage, that undoubtedly there would be difficult and extensive legal argument at trial, but that there existed perfectly reasonable legal responses to the shipowner's criticisms (for example, the economic duress under which the 2nd Memorandum of Agreement had been signed), and that the court now should proceed on the basis of the "reasonably arguable best case".

As to the shipowner's first fundamental criticism, namely that at the time of the arrest there was insufficient material before the court to establish a claim of the amount then put forward, and that there was nothing then in play but bare and inadmissible assertion, the Judge did not agree. The charterer's lawyer's affidavit was full in terms of narrative, and exhibits in schedule formed some 8 pages of heads of claim said to have arisen as the result of the shipowner's contractual breach. The costs and expenses listed did not provide detailed explanation, but it seemed to the Judge that to expect the type of full and detailed documentation of a claim within the affidavit leading the warrant of arrest was to ask for too much within a jurisdiction in which time was often crucial, and in which the 'window' to effect an arrest of a vessel was often highly circumscribed. Accordingly, to argue that an admiralty solicitor had to endow the affidavit leading the arrest with the extent and type of detail as suggested by the shipowner simply was to ignore practical commercial reality. The affidavit in support obviously must be full and fair and truthful, and must clearly depose to the claim and the manner in which it arose, but to demand more at that stage struck the Judge as an insupportable counsel of perfection. So far as the Judge was concerned, the affidavit was sufficient in order to effect the arrest of the "Hua Tian Long".

As to the shipowner's second point that this claim clearly could be seen to be demurrable on its face, the Judge declined as firmly as he might to become embroiled within liability arguments at this very early interlocutory stage. It *might* be that it would transpire that the deponents were exaggerating or were not being full and frank, it *might* be that there in fact were strong defences to the liability assessment, defences to be pleaded out and tried in the fullness of time, but the court simply was not now in a position fairly to sound to the viability of such contentions, absent the clearest and most obvious 'knockout blow', which the shipowner was unable to administer. In this connection the shipowner trailed the suggestion that in any event its liability criticisms properly could be placed within the 'discretionary mix' when it came to deciding an appropriate quantum figure, but in the Judge's view this approach analytically was unsound: either proper and sufficient security was to be ordered, or it was not, and if not, the reason to refrain from so doing itself had to be clear and unequivocal. In deciding the quantum issue the court

had of course to get a 'feel' of the case in terms of the specific heads of recoverability as put forward, but to dilute the quantum of security simply because of the existence of liability issues, which might or might not be decided in favour of the arresting party, in the Judge's view was not the correct course to take; as the authorities make plain, the court is expected to proceed on the basis of the plaintiff's "reasonably arguable best case".

If the shipowner succeeded in any part of its argument, it was in terms of its third main point, namely as to the quantum as ultimately put forward in the charterer's affirmation. Whilst the court was against the shipowner's primary thesis that the affidavit leading the arrest was insufficient for purpose, the Judge should have been disposed to have been more critical had further information subsequently not been forthcoming from the charterer in terms of the quantum of such security as sought, and the basis thereof – albeit criticism had been in any event given by the Judge that the charterer clearly had 'overegged' its quantum claim from a figure of US$59 million to US$140 million, an astonishing increase by any yardstick. Indeed, so great was the increase in security sought that it seemed to the Judge that such inadvertently gave some credence to the shipowner's contention that the whole exercise was oppressive and over-inflated. Clearly if liability were subsequently to be established, in the Judge's view there would be a significant claim, but in terms of security against release from arrest the Judge was unable to understand how such vastly increased sum seriously was put forward. According to the charterer, the dispute with the shipowner, and the non-delivery of the "Hua Tian Long" also had resulted, the deponent speculated, in loss of another contract "with a potential profit element of US$20 million". This element of alleged loss, the Judge apprehended, was but a reformulation of that which originally was characterised as a claim for the charterer's 'loss of reputation'. This struck the Judge as an wholly unsupported submission. Looking at the case in the round, and after carefully considering each head of alleged loss, the Judge came to the following conclusions in terms of the component elements of the overall sum of US$65 million as was ordered to be furnished by way of security in order to release the "Hua Tian Long" from arrest:

(i) the difference between the contract hire price and the substitute equipment hire price: *US$47 million*;
(ii) additional costs incurred due to extension in duration of the existing projects arising from the non-delivery: *US$ 5million*;
(iii) incurring of additional financing costs due to extension of the existing projects duration: *US$3 million*;
(iv) wasted expenditure in terms of preparation for arrival of the "Hua Tian Long": *US$6 million*;
(v) the interest element for the intervening period prior to trial: *US$2.5 million*;
(vi) potential legal costs: *US$1.5 million*

Total: US$65 million

The amount of security as thus ordered might turn out to be right, or it might turn out to be wrong: unfortunately the court had no access to a convenient crystal ball, and simply had to do its best and to exercise its judgment upon the material put forward. As Sheen J commented in *The "Gulf Venture", op cit.*, there indeed was "plenty of scope for debate" as to the amount of security, but ultimately, as Sheen J noted that he had done in the case before him, the judge seized with the matter could do no more than to review the available material and to strive fairly to exercise his discretion thereon. In the Judge's view, therefore, the sum of US$65 million represented appropriate, or, at the least, not inappropriate security; the Judge had a suspicion, no more, that such might well prove to be on the high side, but for the present, and in the context of a claim which was likely to be lengthy and hard fought, in the Judge's view this represented a not unfair award.

Please feel free to contact us if you have any questions or you would like to have a copy of the Judgment.

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