KEY POINTS

- As the law currently stands a shipowner will be unable to obtain any compensation for losses sustained while its ship is under arrest absent proof of bad faith by the bank (the arresting party).
- There is no requirement for the bank to show a "good arguable case" or that the affidavit in support of the application for the issuance of the warrant of arrest be "full and frank".
- The court does have a residual power/discretion to require a cross-undertaking as a condition for allowing the *continuation* of the arrest although this was not used in the recent decision of *The Alkyon*.

Feature

Author Sir Bernard Eder

Enforcing security by the arrest of a ship: the urgent need for change

The recent decision of the Court of Appeal in *Stallion Eight Shipping Co. SA v Natwest Markets Plc* (*The Alkyon*) [2018] EWCA Civ 2760 (11 December 2018) highlights, once again, the fundamental injustice of English law concerning the arrest of ships – and the urgent need for change.

The dispute in the case arose out of a loan agreement which was secured by a mortgage over the vessel, *The Alkyon*. In the usual way, the loan agreement stipulated that in the "event of default" (as defined), the lender (the Bank) would be entitled to accelerate the loan, ie render the total amount of the outstanding loan immediately due and payable. One such event of default was if the value-to-loan (VTL) ratio was less than 125%. In the event, the Bank notified the shipowner in March 2018 that the market value of the vessel was US$15,250,00 which was only 112% of the aggregate amount of the loan then outstanding and so less than the required VTL ratio of 125%; and that the shipowner was therefore required to provide an additional US$1.75m to fill the "gap", failing which there would be an event of default. The shipowner disputed that valuation and provided the Bank with higher valuations.

Notwithstanding, after the shipowner was given further time to cure the alleged shortfall, the Bank sent a Notice of Acceleration declaring that the whole of the loan was immediately due and payable. Shortly thereafter, on 26 June 2018, the ship was arrested by the Admiralty Marshal pursuant to a warrant of arrest issued on behalf of the Bank.

Since that date, the ship has remained under arrest and, so far as I am aware, will continue to remain under arrest until, at least, sometime later this year pending a trial.

As I understand, the main issue in the trial is whether the Bank's assertion that there was a shortfall in the VTL ratio is correct. This was – and remains – hotly disputed by the shipowner. I do not propose to engage in the merits of that dispute. No doubt, this will have to be determined at the trial.

For present purposes, my main focus concerns the continuing arrest of the ship in circumstances where, unlike the position of any plaintiff who obtains a freezing injunction (or indeed any other type of injunction), the Bank has not been required to give any cross-undertaking in damages[1] as a pre-condition of the grant of the warrant of arrest. Anyone unfamiliar with admiralty law may find the absence of such requirement somewhat surprising – but there is no doubt that that is the current legal position or at least the current practice with a long pedigree.

The result is that even if the Bank fails at trial, it is well established that the shipowner will be unable to obtain any compensation for losses sustained while the ship will have languished under arrest for perhaps over a year or more absent proof of bad faith or *crassa neglientia* (forgive the latin) by the Bank. Needless to say, that is a very high threshold. Again, anyone unfamiliar with admiralty law might be surprised if not gobsmacked by such a state of affairs. However, it is a "rule" which goes back some 150 years to the decision of the Privy Council in *The Evangelismos* (1858) 12 Moo PC 352; and remains "good law" although, as fairly recognised by Gross LJ at para [83] of his judgment in *The Alkyon*, such rule can work harshly leaving a shipowner uncompensated for substantial losses flowing from an unfounded arrest even in circumstances where bad faith or gross negligence cannot be established.

As is well known in admiralty circles, it is my view that the current state of the law concerning the arrest of ships is (to say the least) unsatisfactory in the respects referred to above as well as in other important respects; and, for some 30 years, I have been campaigning to try to change the law: see, for example, my lecture to the London Shipping Law Centre entitled 'Wrongful Arrest of Ships' in December 1996 and 'Wrongful Arrest of Ships: A Time for Change' 38 *Tulane Maritime Law Journal* 115 (2013). For a summary of my views, I would refer to my case note on the judgment by Teare J at first instance in *The Alkyon* at *Lloyd's Shipping & Trade Law*, Vol 18, Issue 7.

I do not propose to repeat what I stated there. For present purposes, I would only highlight just two other somewhat surprising features of the law in this context *viz*. that there is no requirement for the arresting party to show a "good arguable case" or that the affidavit in support of the application for the issuance of the warrant of arrest be "full and frank". Yet again, anyone unfamiliar with admiralty law might be somewhat surprised if not astonished by such a regime.

Although my campaign has (so far) been a complete failure, I would challenge any right-minded lawyer to say that the present law and practice in this jurisdiction relating to arrest of ships is satisfactory.

The fact that the present framework is supposedly justifiable by reference to what Gross LJ describes as "longstanding domestic law" (see para of [83] of his judgment) is, to my mind, no excuse for sticking to a system which is fundamentally unjust. The common

law is better than that. I wonder what Lord Atkin would have said to such an argument in *Donoghue v Stevenson*; or Lord Reid in *Hedley Byrne v Heller*; or, nearer the mark, Lord Denning in *The Mareva* which, in effect, ditched the law going back almost 100 years to *Lister v Stubbs* and gave birth overnight to what we now know as the freezing injunction.

In para [84] of his judgment, Gross LJ referred to what he described as "formidable considerations which can properly be said to support the status quo or, at least tell against departing from existing law and practice in the present case …". He then set out such supposed "formidable considerations" – some eight in total: see paras [85]-[92].

I am prepared to accept that certain of these considerations support the view that some aspects of the present system are valuable, important and should be retained, eg the unique feature of the claim *in rem* (para [85]); the efficacy of the remedy of arrest and the threat of arrest (para [87]); and the fact that a ship arrest is, unlike a freezing injunction, asset specific [para 88]). Equally, I accept that the analogy between maritime arrests and freezing injunctions is not exact (para 89]). However, all these points are, with respect, beside the point so far as the central question is concerned, ie whether an arresting party should generally be required to provide a cross-undertaking in damages, if necessary fortified by appropriate security.

Moreover, other supposed formidable considerations highlighted by Gross LJ are, in my view, of little, if any weight. Thus, the fact that it was decided in 1883 that an arrest was no longer a requirement for establishing Admiralty jurisdiction and that no further reconsideration of the law and practice relating to maritime arrests in this jurisdiction has taken place (see para [90]) is, I would suggest, hardly a "formidable consideration" for retaining the status quo in 2019.

Equally, the fact that Gross LJ considers that there is a powerful inference that there is no "pressure" from the maritime industry for a change in the balance struck for so long between shipowners, on the one hand, and potential claimants, on the other hand (see para [91]) or that the arrangements and systems currently in place are premised on the settled, existing state of the law and practice (see para [92]) is, I would suggest, no justification of itself for retaining the status quo.

As for "pressure" for change, I would only say that I am not a lonely heretic, see:

- the judgment of Colman J in *The Kommunar (No.3)* [1997] 1 Lloyd's Rep. at p 33;
- 'Shipping lawyers: land rats or water rats?' by Stewart Boyd QC [1996] LMCLQ 317;
- 'Damages for the wrongful arrest of a vessel' by Shane Nossal [1996] LMCLQ 368;
- 'Damages for Wrongful Arrest: Section 34, Admiralty Act 1988' by Michael Woodford (2005) 19 *MLAANZ Journal* 115; and
- 'Wrongful Arrest of Ships: a case for reform' by Dr Aleka Manderaka Sheppard (2013) 19 JIML 41.

So far as concerns other jurisdictions, I would refer the reader to the important work which has been and continues to be carried out by the International Working Group on Liability for Wrongful Arrest of the Comité Maritime International[2] under the chairmanship of Dr Sheppard referred to by Gross LJ at paras [70]-[76] of his judgment. If I might add, it is perhaps of some interest to note that Prof Francesco Berlingieri, surely one of the greatest international shipping lawyers in recent times, changed his mind on this topic as a result of reading my article: see his book, *International Maritime Conventions Vol II*, Chapter 9, footnote 129.

As for the absence of any apparent pressure from the maritime industry, this is readily explained by two factors. First, there has been a substantial reduction in the number of maritime arrests in recent years. Second, in most cases, the underlying claim will be covered by a P&I Club which will normally provide a suitable letter of undertaking or guarantee in advance of or immediately following any arrest. In this respect, the *The Alkyon* is most unusual ie the claim by the Bank was not a P&I risk.

The main focus of the argument in the Court of Appeal in *The Alkyon* was a point which I first raised some years ago *viz*. whether it is at least possible to say that although there is no requirement for an arresting party to provide a cross-undertaking in damages at the time of the original arrest, nevertheless the court does have a residual power/discretion to require such cross-undertaking as a condition for allowing the continuation of the arrest.

I am pleased to say the Court of Appeal in *The Alkyon* recognised that this was at least a possibility even under the existing Rules of Court and without the intervention of Parliament and the Rules Committee: see para [95]. However, the court declined to exercise that power/discretion on the facts of the case, in particular on the basis of what were considered to be "completely standard facts": see paras [94]-[99] in particular at para [94].

I am also pleased to say that the Court of Appeal did not close the door completely on a change of the law or practice. At para [95], Gross LJ stated:

> "… It is open to the Court itself to reconsider the position, but it should only do so if properly informed as to the views of the maritime community, including the practical ramifications of any proposed changes and the preferred route to be adopted if any such changes are decided upon. Moreover, the Court would wish to be informed of the likely consequences for this jurisdiction internationally if the status quo was to be altered. In short, the Court would wish and need to have a clear understanding of the industry implications of any proposed change before acceding to it. It is unnecessary to be prescriptive as to how the views of the maritime community should be obtained (whether by way of consultation or otherwise) or whether a consensus would need to be apparent – but, plainly, a case for change would be much strengthened if it could rely on significant support from the maritime community, extending much wider than the views of (even eminent) legal commentators. Additionally, it would be for the Court entertaining such a challenge to consider the impact on the

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rule in *The Evangelismos* of a departure from the existing practice."

Following the decision of the Court of Appeal, the topic has been the subject of consideration by the Admiralty Bar Group; and I very much hope that this will result in recommendations for change. So perhaps my campaign may bear fruit.

In terms of possible change, there are, of course, strong arguments in favour of the abolition of the "rule" in *The Evangelismos*. Such kind of "rule" may be necessary and desirable in the context, for example, of claims for false imprisonment where questions of public policy are involved. However, the arrest of a ship is an entirely private law matter involving "ordinary" monetary claims. In such circumstances, I see no reason why the claimant seeking to arrest a ship should stand in a position different from any other claimant seeking a freezing injunction. Whilst I fully recognise that there are, of course, differences between a freezing injunction and a maritime arrest, I see no reason for requiring a cross-undertaking in damages in the former case but not the latter.

Moreover, it is important to note that the introduction of such a requirement would not necessarily involve the abolition of the "rule" in *The Evangelismos*. Indeed, it is important to note that the general requirement that a claimant for any injunction provide a cross-undertaking in damages was introduced because of the very fact that absent such cross-undertaking, the defendant was unable to claim compensation without showing bad faith or *crassa negligentia*. Indeed, it seems that it was for this very reason that the Courts of Equity decided during the 1840s that there should be a general requirement for a claimant to provide a cross-undertaking in damages (if necessary fortified by appropriate security): see *F Hoffman La Roche & Co. v Sec of State for Trade & Industry* [1975] AC 295 at p 360 and *National Australian Bank Ltd v Bond Brewing Holdings Ltd* [1991] 1 VR 386. According to Sir George Jessel in *Smith v Day* (1882) 21 Ch 421, the practice of requiring this kind of cross-undertaking in damages was "invented" by Sir James Knight Bruce VC. At first, it was applied only to injunctions granted *ex parte* but after 1860 it was extended to all interlocutory injunctions. It is perhaps a great pity that he was never the Admiralty Judge.

Meanwhile, I understand that *The Alkyon* continues to languish under arrest …. ■

Sir James Knight Bruce VC
The "inventor" of the cross-undertaking in damages

1 The standard form of undertaking is: "If the court later finds that this order has caused loss to the respondent, and decides that the respondent should be compensated for that loss, the applicant will comply with any order the court may make."

2 http://comitemaritime.org/work/ liability-for-wrongful-arrest/

Further Reading:

- LexisPSL: Banking & Finance: Shipping finance – enforcement of security.
- LexisPSL: Banking & Finance: Guide to insolvency in the shipping industry.