

# Why a Hanjin Fleet Came to Hong Kong

## The role of the Hong Kong court in ship mortgage enforcement

This article was jointly written by Dean A. Young, a senior consultant with Mayer Brown JSM in Hong Kong and Bill Amos, the firm's partner in charge of shipping litigation, who handled the Hanjin ship arrests.



**Mayer Brown JSM helps banks recover the largest ever maritime award in Hong Kong's history.**

The demise of Korea's Hanjin Shipping Co. Ltd. was the largest bankruptcy of a container line in history, and earlier this year it resulted in the biggest ever court sale of ships in Hong Kong, with a total sale price exceeding US\$600 million. In this article we consider Hong Kong's role as a centre for maritime legal services, and the procedures involved in ship mortgage enforcement.



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### HONG KONG'S MARITIME LEGAL SERVICES

- In May 2017, Chinese President Xi Jinping welcomed 28 heads of state and government officials to Beijing to discuss China's 'Belt and Road' initiative, referring to the revival of the ancient Silk Road economic belt and a 21st century seafaring maritime route. Connecting China to Europe, the Belt & Road will, if all goes to plan, cover more than 60 countries and repay China's investment by contributing 80% of global GDP growth by 2050.
- Under the 'One Country, Two Systems' principle set out in Hong Kong's Basic Law, Hong Kong enjoys a double advantage owing to the special treatment given by China under the Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA) and other preferential policies, whereas the 'two systems' advantage enables Hong Kong to maintain its internationally compatible legal and judicial system.
- Hong Kong's common law system is based on English law and the laws of other Commonwealth jurisdictions, and is independent from the laws of China. What is not generally known is Hong Kong's very high degree of autonomy in shipping affairs. For example, it has its own representation on major international bodies such as the International Maritime Organization.
- About 190,000 vessels, including ocean-going and river vessels, visit the port of Hong Kong each year so a maritime community (numbering around 700 companies) needs legal services to cover casualties and other shipping disputes. The city also serves as an international legal and dispute resolution centre for the Asia-Pacific region. Maritime lawyers specialised in admiralty law work are available to offer advice and dispute resolution<sup>1</sup> for shipowners, charterers, cargo owners and, of course, ship finance banks.

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Ship Finance Award

- *Seatrade Maritime Award*  
*Asia 2015*



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<sup>1</sup> In 2016, the Hong Kong International Arbitration Centre (HKIAC) handled 262 new arbitration cases, of which 22% were maritime.

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### ENFORCEABILITY OF SHIP MORTGAGES

- As an international financial centre, Hong Kong has a high concentration of banks providing ship financing services to the local shipping industry as well as foreign shipowners. Financiers both local and foreign can be reassured that the Hong Kong courts have the expertise to help them recover their loans if borrowers become insolvent or breach their loan documents.
- The recent bankruptcy of Hanjin Shipping provides a working example. Hanjin's mortgagees were faced with crippling losses if unsecured creditors succeeded in overcoming their priority. Whenever ships are located in the China-Korea-Japan range, a comparison should be made between Hong Kong and other ports in Asia to determine the safest and least costly location to seize and sell the ships so as to maximise the recovery for mortgagees. Hong Kong is generally the preferred choice for bank mortgagees because:
  - Included in the list of admiralty claims is a claim under a mortgage (regardless of the flag of the ship). Hong Kong's legal system is based on English law and brings with it a fixed order of priorities to the proceeds of sale of a ship. A mortgagee ranks ahead of all claims except for maritime liens (such as collision damage, salvage claims and crew's wages), possessory claims (such as an unpaid repair yard), and the actual costs of the arrest.
  - Hong Kong's role as an international financial centre is dependent on its legal system continuing to provide certainty and its courts continuing to adjudicate openly, impartially and free from interference or influence. There is no bias for local creditors.
  - The application process is clearly established. The mortgagee needs to file an admiralty writ in rem and an application for an arrest warrant with the Court accompanied by an affidavit proving its claim and, when obtained, a warrant of arrest is served on the ship by the Bailiff.
  - Once arrested, the procedure is very fast compared to other jurisdictions as the Court has the power to order the sale "pendente lite", meaning whilst the action is proceeding, the ship is treated as a wasting asset. The proceeds of sale that are paid into the Court stand in place of the ship while the ship can be sailed away by the purchaser. The chart below shows how fast the time line can be.
  - The bailiff's fee of only 1% compares favourably with the 2%-2.5% commission charged in other jurisdictions in the region.
  - The court will generally permit the bank to apply for payment out of court 30 days from the court sale, ensuring that the sale proceeds and mortgage loan are not tied up in court unnecessarily.
  - Lastly, but most importantly, the Court's bill of sale passes ownership to the purchaser free not just from the mortgage but also all other encumbrances, debts and liens. The ship is clean to begin trading once again.

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"The firm is a go-to for shipping finance."

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"They are experts in ship finance; they are commercial and proactive to find solutions for their clients."

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"They are very good on client care – they always put in extra work to accommodate timelines and challenging ideas and structures."

– *Chambers Asia Pacific* 2016

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- In the case of five of the largest Hanjin ships handled by Mayer Brown JSM, those that carried containers were allowed to proceed to their destination for discharge and their masters were then ordered to proceed to Hong Kong where each ship was arrested.
- A panel of international shipbrokers was instructed to value the ships to ensure that the Court's reserve price was accurate. In cases where values are hard to appraise on account of few or no current comparisons, a mortgagee bank commonly enters a protective bid to ensure that its vessel is not sold at an undervalue. The result was the largest ever court sale of ships in Hong Kong, with a total sale price exceeding US\$600 million. There were no abandoned crews, astronomical port costs or prolonged periods of idleness. The ships have since been absorbed into the fleets of other container line operators.

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## Timetable for Hong Kong Court Sale - Concurrent Procedures

WEEK	JUDGMENT AND PAYMENT OUT OF COURT	APPRAISEMENT AND SALE OF VESSEL
1 - 2	<ul style="list-style-type: none"> <li>• Serve notice of default/ acceleration notice;</li> <li>• Issue writ - serve and arrest vessel;</li> <li>• Issue application to have crew paid off and repatriated and vessel shifted to lay-up anchorage;</li> <li>• File and serve statement of claim.</li> </ul>	
3	<ul style="list-style-type: none"> <li>• Issue application for judgment in default (with supporting affidavit from lender) - judgment obtained.</li> </ul>	<ul style="list-style-type: none"> <li>• Issue application for appraisal and sale;</li> <li>• Bailiff commissions appraisal.</li> </ul>
4 - 6		<ul style="list-style-type: none"> <li>• Appraisal received by Bailiff;</li> <li>• Invitation to tender published.</li> </ul>
7 - 8	<ul style="list-style-type: none"> <li>• Search for caveators.</li> </ul>	<ul style="list-style-type: none"> <li>• Opening of tenders; completion of Court sale and purchase;</li> <li>• Notifying underwriters and register bill of sale.</li> </ul>
Thereafter	<ul style="list-style-type: none"> <li>• After 30 days from sale, issue application to determine priorities and have purchase money paid out of court, obtain order, and payment out.</li> </ul>	

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