Lectures 2016-17

Asset Finance law: ships & aircraft

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This presentation can be found at...

Asset finance vs personal finance vs *patrimony* finance

Complex ship & aircraft finance transactions share many characteristics:
- assets of great value which can themselves be a significant aspect of the security to be provided;
- the intrinsically international nature of the industries;
- The importance of anglo-saxon legal notions;
- Ships and aircraft, like land, but unlike most other tangible moveable assets, require registration;
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Parts 1 - 4

Ship Registration general concepts:
Attribution of nationality to ships;
Evolution of the Genuine link question;
Modern ship registration systems

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Overview of topics 1 - 6

1. First concepts: terms
   - Nationality, flag, documentation, registration
   - What is a ship?

2. Attribution of nationality to ships
   - Nationality, Documentation, Registration
   - The evolution of the freedom of the seas doctrine
   - Extension of Territory theory
   - Modern conceptions of nationality attribution and flag

3. The genuine link question

4. Modern Ship registration systems
Part 1

Terms: nationality, documentation, etc

What is a ship?

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Nationality, Documentation, Flag and Registration

- Nationality
  - National Character of the Ship, irrespective of registration
  - Number of Connecting factors...but registration is the only universally applicable test

- Flag
  - visual evidence
  - symbol of a ship's nationality

- Registration
  - Public Records of a State
  - provides for the protection of the title of the registered owner
  - the preservation of priority rights between persons holding security interests over the vessel
  - attribution of nationality to the ship

- Documentation
  - Evidences ship’s nationality
  - May fall short of registration as does not normally deal with private law matters
    - EG. Panamanian *patente de navegacion*, generally issued by consular authority, for flag purposes (valid 6 months). No need to evidence title at that stage.
What is a ship?

- Is the question important?
- What’s so special about ships?
Is the question important?

- The importance of definitions lies in the treatment accorded to maritime property in a number of legal spheres;
- A particular and unique status at law;
- Which item of maritime property is capable of attribution of nationality (with all attendant rights and obligations)?
What’s so special about ships?

- Quasi-legal personality at law
- *In rem* proceedings and *in rem* jurisdiction;
- Maritime property capable of salvage;
- Implied warranty of seaworthiness of carrying ship in the context of sea carriage of goods;
- Limitation of liability;
- Manner and extent of insurability;
- Seaborne property which is capable of registration;
- Security interests registrable against it
- On which property can a Maltese mortgage be created?
Statutory definitions of ship

- “any self-propelled sea-going vessel used in international seaborne trade for the transport of goods, passengers or both”
  - UN Convention on conditions for registration of ships 1986, Art. 2
- “every description of vessel used in navigation, whether self-propelled or not, and it includes barges, oil rigs, pontoons, seaplanes, and any other craft and similar vessels”
  - The Authority for Transport Act, Malta (cap 499)
“every description of vessel used in navigation, whether self-propelled or not, and it includes barges, pontoons and oil rigs and other similar vessels, but not vessels propelled by oars and.....shall also include a ship under construction”

“vessel includes any ship or boat, or any other description of vessel used in navigation

- Merchant Shipping Act, Malta (cap 234)

“vessel means a steamer, motor vessel, launch, boat, hovercraft, submersible or floating craft of any description”

- Fisheries & Conservation Management Act, Malta (cap 425)
Confusion or careful differentiation?

- MSA regulates registration and national character
- The Transport Authority exercises overall control for the preservation of good order in the territorial waters of Malta
- Rowing boats do not normally ply international waters, while ships under construction require registration
- But possibility for some confusion remains
The Commercial Code includes the following as an act of trade: “any transaction relating to vessels and navigation”

  - Charles Gatt vs Alfred Bellizzi (25.3.1960), App.Civ

- This overturned Borg vs Cassar Torreggiani (Kumm. 1948) which did not distinguish use or purpose, citing Coleridge J. Tindell vs Combe, where navigation was considered synonymous to rowing

- The Court of Appeal decision should be looked up, because it cites widely
UK courts: ad hoc approach

- A vessel formerly registered, but for the last 4 years used as a coal hulk with all masts, spars and rigging removed, moored fore and aft by two anchors: not a ship but a mere chattel
  - European & Australasian Royal Mail vs. P&O (1866) 14 L.T. 704
- An electric passenger launch used exclusively on a small lake: not “used in navigation”
  - Southport Corporation vs. Morris [1893] 1 QB 359
- A motor boat used exclusively in a river behind a lock beyond which a canal connected via further locks to a tidal estuary: ship
  - Weeks vs Ross [1933] 2KB 229
“all the contribution I can make is to say that I am not convinced that the Learned Judge below was wrong. One might possibly take the position of the gentleman who dealt with the elephant by saying that he could not define an elephant but he knew what it was when he saw one...I should have liked to give a definition here because considering that these words are the words in every ordinary marine policy and in every Club policy.....it is rather a pity that the courts are not able to give a definition of the words which were constantly turning up in a mercantile transaction”

Part 2

Ships, Nationality and the doctrine of freedom of the seas

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First half of the Middle Ages, navigation on the open sea was free to everybody

When nations started organizing themselves into Sovereign Statehood (also coinciding with the great discoveries by navigators), it became common for powerful maritime states to claim ownership of the open seas:

- Venice over the Adriatic Sea
- Portugal over the whole of the Indian Ocean and the Atlantic south of Morocco
- Spain over the Pacific and the Gulf of Mexico
- Sweden, Denmark and Great Britain also laid claim to parts of the open sea.
Certain rules for the exercise of jurisdiction over vessels at sea became essential in order to avoid conditions of anarchy and a state of unregulated maritime lawlessness. This was achieved by attributing nationality to the ship itself, thereby identifying the country under the jurisdiction -and protection- of which the particular ship would travel.

This developed from Grotius’ ideas, promoting the view that the open sea is by nature free from the sovereignty of any state;

This view only became universally recognized by the end of the 1820’s.
For a long time, the attribution of nationality of ships was explained by the theory of Extension of Territory;

It was thought that for legal and jurisdictional purposes, a ship was an extension of the territory of the flag state;

- R v. Anderson (1868)
- The steamship Lotus (1927)
- Oteri v. R. (1977)
The Freedom of the Seas

- All vessels on the high seas were subject to the jurisdiction and entitled to the protection of the State under the maritime flag of which they might sail.
- From this, there logically followed a number of corollary rules.
  - No State can exercise jurisdiction over foreign ships at sea;
  - No ship can sail under a flag without proper authority from the flag state
  - Ships under an unauthorised flag are liable to capture and confiscation by the State whose flag was wrongfully raised
  - A vessel sailing without an identifiable flag was unprotected, and might be seized in suspicious circumstances
The Asya case

- *Naim Mowan, owner of motor vessel "Asya" v. A-G for Palestine (1948) AC 351*
  - Flagless, but first hoisted a Turkish flag when sighted by a British warship on the high seas close to Jaffa;
  - It hoisted a Zionist flag just prior to being boarded;
  - 1st instance ordered forfeiture (illegal immigration), but was appealed also on the basis of freedom of the seas;
  - Appeal rejected: “...for the freedom of the open sea, whatever those words connote, is a freedom of ships which fly, and are entitled to fly, the flag of a state which is within the comity of nations”
1. The high seas are open to all States, whether coastal or land-locked. Freedom of the high seas is exercised under the conditions laid down by this Convention and by other rules of international law. It comprises, *inter alia*, both for coastal and land-locked States:

   (a) freedom of navigation;
   (b) freedom of overflight;
   (c) freedom to lay submarine cables and pipelines, subject to Part VI;
   (d) freedom to construct artificial islands and other installations permitted under international law, subject to Part VI;
   (e) freedom of fishing, subject to the conditions laid down in section 2;
   (f) freedom of scientific research, subject to Parts VI and XIII.

2. These freedoms shall be exercised by all States with due regard for the interests of other States in their exercise of the freedom of the high seas, and also with due regard for the rights under this Convention with respect to activities in the Area.
UNCLOS, Article 89
- No State may validly purport to subject any part of the high seas to its sovereignty.

UNCLOS, Article 91
- "Ships have the nationality of the State whose flag they are entitled to fly. There must exist a genuine link between the State and the ship".
- "Every State shall issue to ships to which it has granted the right to fly its flag documents to that effect".

UNCLOS, Article 92 (2)
"A ship which sails under the flags of two or more States, using them according to convenience, may not claim any of the nationalities in question with respect to any other State, and may be assimilated to a ship without nationality".
Article 97: Penal jurisdiction in collision or any other incidents of navigation

1. In a collision or incident of navigation on the high seas, involving penal/disciplinary responsibility of a person in the service of a ship, only the authorities of the flag State or of the State of which such person is a national can so proceed;

2. In disciplinary matters, only the State which has issued a master's certificate shall be competent to pronounce the withdrawal of such certificates;

3. No arrest or detention of the ship, even as a measure of investigation, shall be ordered by any authorities other than those of the flag State;
Interpretations differ on some aspects; Some States have claimed rights to board foreign vessels suspected of illicit traffic of narcotic drugs, while on the high seas; Terrorism not mentioned in UNCLOS, but some States argue for such a right:

- inter-State co-operation agreement between the U.K. and U.S.A.
- Various bilateral agreements, etc
UNCLOS, Art. 108

- All States shall cooperate in the suppression of illicit traffic in narcotic drugs and psychotropic substances engaged in by ships on the high seas contrary to international conventions.

- Any State which has reasonable grounds for believing that a ship flying its flag is engaged in illicit traffic in narcotic drugs or psychotropic substances may request the cooperation of other States to suppress such traffic.
The significance of the Flag

- Ships derive their nationality from their State of registration, and such national character is evidenced by the flag which they fly.

- The flag does not constitute absolute evidence of nationality, but certainly strong *prima facie* evidence.

- It is a visual manifestation, and a symbol, of the ship's nationality.
Part 3

Flag State obligations and the Genuine link question

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Every State shall fix the conditions for the grant of its nationality to ships, for the registration of ships in its territory, and for the right to fly its flag.

Ships have the nationality of the State whose flag they are entitled to fly.

There must exist a genuine link between the State and the ship.

Every State shall issue to ships to which it has granted the right to fly its flag documents to that effect.
1. Every State shall effectively exercise its jurisdiction and control in administrative, technical and social matters over ships flying its flag.

2. In particular every State shall:
   (a) maintain a register of ships containing the names and particulars of ships flying its flag, except those which are excluded from generally accepted international regulations on account of their small size; and

   (b) assume jurisdiction under its internal law over each ship flying its flag and its master, officers and crew in respect of administrative, technical and social matters concerning the ship.
3. Every State shall take such measures for ships flying its flag as are necessary to ensure safety at sea with regard, inter alia, to:

(a) the construction, equipment and seaworthiness of ships;

(b) the manning of ships, labour conditions and the training of crews, taking into account the applicable international instruments;

(c) the use of signals, the maintenance of communications and the prevention of collisions.
Measures shall ensure:
(a) periodic surveys of ship to ensure the safe navigation of the ship
(b) that master, officers and crew possess appropriate qualifications and are sufficient in number for the type, size, machinery and equipment of the ship;
(c) crew required to observe the applicable international regulations concerning the safety of life at sea, prevention of collisions, prevention, reduction and control of marine pollution, and the maintenance of communications by radio.

Each State is required to conform to generally accepted international regulations, procedures and practices and to take any steps which may be necessary to secure their observance.

A State which has clear grounds to doubt that Flag State has exercised proper jurisdiction and control, can ask FS to investigate. FS shall investigate and take any action necessary to remedy the situation.
Genuine link as a concept which limits the unfettered discretion of States to establish conditions of attribution of Nationality

- The Muscat Dhow case (1905) (Permanent ct. Of Arbitration)
  - it was the flag and registry of a ship, rather than its ownership, which evidenced its nationality.

- Lauritzen v. Larsen (1953) (345 US 571)
  - the right of individual states unilaterally to fix the conditions for the grant of Nationality to merchant vessels was unassailable.
a post WW2 phenomenon.

- The situation was one of unfettered discretion of the Flag State in establishing the criteria of attribution of Nationality to ships.

- While the traditional maritime powers held an almost monopolistic control over international shipping and maritime commerce, the position remained quite unassailable.

- When in the 20th Century maritime interests started facing increasing costs as a result of more organised domestic legislation in the social and economic sphere, a practice started developing to operate foreign-flagged vessels to maintain commercial competitiveness.
Linked to the development of “flags of convenience”

- This practice led to the development of so-called flags of convenience by States, who would attract tonnage to their flag by establishing liberal and attractive conditions for shipping operations for ships flying their flag...without much regard to exercising effective jurisdiction over their ships.

- This eventually led certain traditional maritime nations to seek to put some limit on the unfettered discretion of States in establishing the conditions for the attribution of their Nationality to ships, thereby preventing national maritime interests from flagging out in order to free themselves from the effects of domestic legislation.
Traditional powers & labour interests located there were principal proponents for the need of a genuine link over and above the other duties of Flag States

- Nottebohm case (1955) – ICJ (non-maritime case)
  - “... it is for every sovereign state, to settle by its own legislation the rules relating to the acquisition of its nationality ... nevertheless a State cannot claim that its rules are entitled to recognition by another State, unless .... there is a genuine connection in existence and a real and effective link...”
  - “nationality is a legal bond having as its basis a social fact of attachment, a genuine connection of existence, interests and sentiments, together with .....reciprocal rights and duties.”
The 21st Century is very different to the 1950’s

Technology, transport, globalization

True for individuals, and more so for ships, whose vocation it is to link, rather than differentiate between populations

The social fact of attachment, therefore, is not to any particular grouping of people

ships as instruments of int’l trade, with an inherent and inescapable mobility, often owned by international investment groupings
“Each State shall fix the conditions for the grant of its nationality to ships, for the registration of ships in its territory and for the right to fly its flag. Ships have the nationality of the state whose flag they are entitled to fly. There must exist a genuine link between the state and the ship; in particular the state must effectively exercise its jurisdiction and control in administrative, technical and social matters over ships flying its flag...”.

Prior to 1956, the draft provisions emphasised economic considerations, including references to the nationality of the owners of ships to be registered, as a condition for recognition of nationality by Third States.

However, this was dropped possibly as a result of American pressure, since they were concerned about protecting American owned tonnage registered in Panama and Liberia.
Wrong articulation of a valid concept

- Judge Jennings: "the assumptions that the genuine link formula, invented for dealing with people, is capable of immediate application to ships and aircraft, smacks of a disappointing naiveté ... a provision which might seem to encourage governments to make subjective decisions whether or not to recognise the nationality of this aircraft or that vessel is clearly open for abuse and for that reason to grave criticism".

- IMCO case: advisory opinion on whether the maritime Safety Committee of the Inter-Gov’tal Maritime Consultations Organization was properly constituted in terms of Art. 28 (a) of Geneva Convention

  - “the...committee shall consist of....the largest ship-owning nations...” Panama and Liberia (unelected) protested.

- ICJ: "...the test of registered tonnage is that which is more consonant with international practice and with maritime usage ... and it is unlikely that the test should be the nationality of stock holders and of others having beneficial ownership".
Other developments

- The US Department of State position post 1958 convention:
  - the requirement of a genuine link is not a condition for recognition of the nationality of the ship, but an independent obligation to exercise jurisdiction and control effectively.

- Tacke defines genuine link as follows:
  - "The legal and functional responsibilities assumed by the flag state when it confers national character upon a ship. Registration represents the legal requirement while the functional component pertains to periodic surveys, safe and proper working conditions, and social welfare of the crew".

- By the time UNCLOS 1982 came onto the scene, not much progress was made either way. Art. 91, 94, 211 & 217

- It was not until the 1986 United Nations Convention on Conditions for Registration of Ships that a real attempt was made to identify better what is meant by "genuine link" in an international convention.
UN Convention for Registration of ships, 1986

- Article 1: establishes the objectives: ensuring or strengthening genuine link principle

- Article 4: general provisions included in UNCLOS and the 1958 Convention as being declaratory of established principles of international law.

- Article 5: the flag State must have a competent and adequate national maritime administration subject to its jurisdiction and control.

- Articles 8, 9 and 10 attempt to identify further the genuine link required in terms of ownership, manning as well as management of ships.
Convention has not achieved the goals that inspired it

- Ready: "... the Articles relating to ownership, manning and management leave so much of their detailed implementation and interpretation to the flag State that their effect may largely be negated. Viewed in this light, the provisions can be seen as little more than statements of principle".

- Kasoulides: “...the Convention reaffirmed the flag State's supremacy and institutionalised the status quo, leaving the required concepts of genuine link and beneficial ownership still nebulous and controversial. ... It also appears to have influenced the recent establishment or activities leading to the establishment of international registers by developed countries, and a number of developing countries are considering the advantages of open registries".
over 50 years after the concept of the "genuine link" was put forward as a reaction to the growth of the open registries, as they were conceived then, there is a real need to finally reject the term as understood in terms of nationality of ownership, manning and management of ships.

The concept is important, but must finally be framed correctly as a reference to the legal and functional responsibilities assumed by the flag state, comprising registration, periodic surveys, safe and proper working conditions as well as social welfare of the crew.
Part 4

Modern Ship Registration Systems

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Different Ship Registration Systems (1)

- Ship Registration as a service industry
- Different criteria for classification
- UNCTAD Review of Maritime Transport (2005) uses different criteria, grouping all open registers together, or distinguishing:
  - “open registers” (eg. Panama, Liberia, Bahamas, Malta, Cyprus);
  - “international registers” (eg. NIS, Hong Kong, Marshall Islands, Isle of Man, DIS)
UNCTAD Review further sub-divides as follows:

- **Major Open Registers:**
  - Panama, Liberia, Bahamas, Malta, Cyprus, Bermuda

- **Minor Open Registers:**
  - St. Vincent, Antigua, Cayman Is., Luxembourg, Vanuatu, Gibraltar

- **International Registers:**
  - NIS, Hong Kong (China), Marshall Is., Isle of Man, DIS, Kerguelen Is., Netherlands Antilles
Different Ship Registration Systems (3)

1. a Nationality-driven view-point
2. an administrative philosophy view-point
   - Centralized
     - Greece, Cyprus, China (Hong Kong)
   - De-centralized
     - Panama, Singapore, Bahamas, Malta
   - Out-sourced
     - Liberia, Marshall Islands
Registration pre-dates nationality

- Registration systems pre-date the concept of nationality, and can be found in Roman law, as well as the city states of medieval Italy.

- Concept became important as a matter of international law in the aftermath of the discovery of the New World, with Sovereignty pitched against Freedom of the High Seas.

- Registration involves the entry of the ship into the public records of a State.

- Maltese system built around UK model (therefore British judgments remain relevant, but not conclusive).
“there are two points of public policy....the one a policy regarding the interests of the nation at large, relating to the question who shall be entitled to the privileges of the British flag....; and the other a policy being similar to that which gave rise to the acts for the registration of titles to land – the object being to determine what should be a proper evidence of title in those who deal with the property in question”
Public & private law functions

- **Public law functions:**
  - Subjecting ship to jurisdiction of the flag State;
  - Conferment of right to hoist the flag
  - Right to Flag State diplomatic protection and consular assistance;
  - Right to naval protection by the Flag State;
  - Right to engage certain activities in territorial waters (e.g., coastal fishing or cabotage – trading between local ports);
  - Determine rules of war and neutrality in war

- **Private law functions:**
  - Protection of title of registered owner
  - Protection of title and priority of security interest holders
Prima facie evidence of nationality and title

“Although the legislature has now taken greater security to see that the person registered as owner is properly registered than it had done before, all it has done is to make the register *prima facie* evidence of ownership. In fact, it assumes that anybody may displace altogether the statutory effect which has been given by proving what the facts really are”

- Lord Herschell in Baumvoll Manufaktur Von Kail Scheibler v. Furness (1893) AC 8

- X, the registered owner of the motor yacht Bineta, sold her to Y, but remained in possession pending payment, despite Y being registered as owner. When Y defaulted, X sold yacht to Z, exercising his seller’s lien, as he was entitled to do. Y objected to Z’s registration. HELD: although X had ceased to be the registered owner, he had conferred a good title to Z who was entitled to be registered as owner in place of Y.

- The Bineta [1966] 2Lloyd’s Rep 419
The Eastern Belle (1875):

- A shipowner sold certain shares in a ship, but the purchaser neglected to register the sale. The shipowner subsequently mortgaged the whole ship to a third party without knowledge of the sale. The mortgage was to secure an amount in excess of the value of the ship. When the purchaser eventually tried to register the sale, he discovered the mortgage and commenced an action against the co-owner. The mortgagee intervened, seeking a release of the ship, and the court found in his favour.