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125 Plus Ways for an Owner or Lender to Lose a Vessel

There is a multitude of ways that the title to a vessel can be in jeopardy and a lender can lose its preferred ship mortgage position. Obviously, if the owner's interest in the vessel is in question, then a preferred ship mortgage that acts as security for a loan on that vessel is likewise in question. The position of the mortgage holder can be at risk even if title is not at issue and a preferred mortgage can be unenforceable even if properly recorded. Following are a series of legal cases and other references which illustrate these points. They identify situations in which vessel title insurance would have been of value. The list is not intended to be exhaustive; it merely is intended to be illustrative. The below references, while listed under one category, often have relevance to other categories.

I. Title Issues:

1. STOLEN BOATS AND ALTERED HIN NUMBERS

A boat was stolen off a Charlotte County, FL boat dealer's lot and the thief altered the hull identification number and the engine serial number. He then attempted to sell the vessel. *State of Florida, Dept. of Environmental Protection Media Release 99-3B-8*

2. FEDERAL REGISTRATION DOES NOT PROVE TITLE

Federal registration does not of itself confer endowments of title and ownership to a vessel. *Jones v. One Fifty Foot Gulfstar Motor Sailing Yacht, 625 F. 2nd 44 (5th Cir. 1980)*

3. RECORDATION IS NOT CONCLUSIVE OF TITLE

Record title is not conclusive as to ownership of a vessel. *In re Lykes Bros. S.S. Co., Inc., 196 B.R. 574 (M.D.Fla. 1996)*

4. CERTIFICATE OF DOCUMENTATION IS NOT CONCLUSIVE EVIDENCE OF TITLE

Issuance of certificate of documentation is not conclusive as to ownership of vessel, but rather, courts are guided by the underlying contract. *In re Tacoma Boatbuilding Co., 81 B.R. 248 (S.D.N.Y. 1987)*

5. SHAM SALE

Charterer of vessel after arresting vessel for breach of charter, found that owner had sold the vessel to avoid its being used as security. Court declared sale a sham. *The Tjaskemolen, Lloyd's Law Reports 1997, part 5, Vol. 2 – 465*

6. PURCHASING AT A MARSHALL'S SALE IN ADMIRALTY IS THE ONLY WAY TO GET "PERFECT" TITLE

"The purchaser of a vessel who takes title in any way other than by foreclosure in admiralty acquires imperfect title. His protection consists only of the warranties in his bill of sale, for whatever they are worth, and the judicial doctrine of laches." *Tulane Law Review 558, 565 (1973), Introduction to the Law of Maritime Liens, 47(3)*

7. **CHALLENGES TO A VESSEL FORECLOSURE AND JUDICIAL SALE**

A vessel foreclosure and judicial sale which appears to be valid generally cleanses the ship of maritime liens, but it can be challenged as being void or invalid for (i) not following proper procedure (e.g. lack of notice), or (ii) the assertion of fraud.

8. **GET TITLE PROTECTION BECAUSE MARITIME LIENS ARE SECRET**

“It is of the greatest importance to the buyer that he acquire title to the vessel on the sale and that the title be free of any liens or encumbrances not known to him. The problem is particularly important in the sale of vessels, because most maritime liens are ‘secret’ and need not be recorded to be effective.” Tulane Law Review 535, 550, (1973), *Ship Sale Contracts* 47(3)

9. **TITLE TO AN ABANDONED VESSEL**

Even if a vessel has been abandoned, the owner or owner’s successor retains title to that vessel no matter how long it has been abandoned. *Emre E. Dluhos v. The Floating and Abandoned Vessel, known as “New York”*, 162 F.3d 63 (2nd Cir. 1997)

10. **ACTION TO QUIET TITLE TO A VESSEL**

In order to quiet title to a vessel against the world, an action must be pursued *in rem*. Court will not entertain an *in rem* action against a vessel to quiet title unless the vessel was arrested. *Emre E. Dluhos v. The Floating and Abandoned Vessel, known as “New York”*, 162 F.3d 63 (2nd Cir. 1997)

11. **HOW DOES A VESSEL BILL OF SALE BECOME EFFECTIVE AGAINST 3RD PARTIES**

Contracts for sale of U.S. flag vessels are governed by state law but federal laws are of great significance. To be effective against third parties, the bill of sale must be properly recorded and to accomplish that, it must be sufficient and acceptable for recording. Tulane Law Review 535, 538, (1973), *Ship Sale Contracts* 47(3)

12. **CHAIN OF TITLE ISSUES**

Chain of title documents for a vessel sale includes judicial proceedings (bankruptcy, receivership, probate, conservatorship, dissolution of marriage) and if the court has not authorized the sale, the order authorizing sale is subject to collateral attack, or the order is invalid because court lacked jurisdiction.

13. **JURISDICTIONS THAT DO NOT RECOGNIZE *IN REM* CLAIMS**

A vessel can be arrested in the United States by cargo interests when the bill of lading contains a foreign forum selection clause, but the law of the forum does not recognize *in rem* actions and a vessel is not recognized as a distinct juristic person. *Tokio Marine v. Turquoise*, 2001 AMC 1692

14. **ALTER EGO THEORY AND INTRA-CORPORATE CONVEYANCES**

A vessel title and mortgage would be in jeopardy (even if properly recorded) if documents are adjudicated unenforceable by application of the alter ego theory of liability or are executed as part of sham intra-corporate conveyances. *Equilease Corporation v. M/V Sampson*, 568 F. Supp 1259 (E.D. La. 1983); *Flood v. American Oil Screw Trawler Francis L. MacPherson*, 258 F. Supp 768 (D. Mass. 1966)

15. **STATUTORILY TIME BARRED ACTION ALLOWED**

Following a foreclosure and judicial sale of a vessel, a claim was made for wages. The purchaser of the vessel argued that the claim was statutorily time barred. The court permitted the claim to proceed (and ultimately found against the bank) because a claim (but not an “action”) had been filed with the U.S. Coast Guard. The court, following “equitable principles,” allowed the intervention against the proceeds and found that the claimant’s lien survived the sale of the ship. *Key Bank of Washington v. Southern Comfort*, 106 F.3d 1441 (9th Cir. 1997)

16. **CERTIFICATE OF DOCUMENTATION DID NOT OVERCOME PRIOR SALE OF VESSEL**

Hozie bought a vessel from Mignano, left it moored where it was, though Hozie was responsible for future mooring costs and for paying the bank the payments that Mignano had been making. Hozie did not record the sale. Mignano tried to rescind the sale but Hozie refused. Hozie then discovered the vessel’s condition was worse than represented at the time of purchase and a dispute arose over whether Hozie should continue making payments. Mignano died, and his executrix agreed to sell the vessel to Underwood who convinced her to sign a U.S. Coast Guard bill of sale (allegedly to clear title to the

vessel) which Underwood filed with the Coast Guard and he received a Certificate of Documentation. Underwood sought a summary judgment that he had title to the vessel. The court would not grant it. *Hozie v. The Vessel Highland Light*, 1998 AMC 2829

17. **CERTIFICATE OF DOCUMENTATION IS NOT CONCLUSIVE EVIDENCE OF OWNERSHIP**
Although one party has a "Certificate of Documentation" for the vessel, this is not conclusive evidence of ownership in a proceeding in which ownership is an issue. *Hozie v. The Vessel Highland Light*, 1998 AMC 2829
18. **BUILDER'S CERTIFICATE IS NOT CONCLUSIVE EVIDENCE OF TITLE**
For purpose of determining whether mortgagee proved mortgagor's ownership of vessel as part of its burden of establishing valid preferred ship mortgage, builder's certificate is prima facie, but not conclusive, evidence of title, as it is part of paperwork required by U.S. Coast Guard for the certificate of documentation process. *Chase Manhattan Financial Services, Inc. v. McMillian*, 896 F.2d 452 (10th Cir. 1990)
19. **JUDICIAL SALE DID NOT CLEANSE VESSEL OF ALL LIENS**
In the case of purchase of a vessel at a judicial sale in Greece, which was thought to be free and clear of all liens and encumbrances, the court would not permit summary judgment against maritime lien holder whose lien predated the judicial sale. *Crescent Towing and Salvage Co. Inc. v. M/V Anax*, 40 F.3d 741 (5th Cir. 1994)
20. **UNPAID INSURANCE PREMIUMS AFFECT SUBSEQUENT OWNER'S VESSEL TITLE**
Liverpool and London Steamship P & I Club insured the M/V Kappa Unity (now M/V Abra) owned by Kappa Shipping. Kappa Shipping was delinquent on insurance premiums. Kappa Shipping sold the Kappa Unity to Interforce Shipping. Liverpool and London filed suit for the unpaid premium and arrested the vessel. The court found that the failure to pay the premiums was the basis of a maritime lien which allowed for the arrest and sale of the vessel and payment of premiums out of the proceeds of the sale. Presumably, future calls from the P & I Club relating to insuring of the vessel by Kappa Shipping would, likewise be subject to the maritime lien. *Liverpool and London Steamship Protection and Indemnity Association Limited v. Queen of Leman, et al.* consolidated with *Liverpool and London Steamship Protection and Indemnity Association Limited v. M/V Abra, et al.*, --F.3d--, 2002 WL 1380876 (5th Cir. June 27, 2002)

II. Liens and Encumbrances:

1. **MARITIME LIENS FOLLOW THE VESSEL WHEN SOLD**
"Unlike most land-based liens, a maritime lien is unrecorded and arises from the moment the supply or service, which is the basis of the lien, is provided to the vessel. The security is the vessel itself and the lien can be enforced by an action against the vessel in which the vessel is arrested. An action to arrest the vessel is usually available wherever the vessel can be found. This includes the United States as well as many foreign jurisdictions. Note also that the lien follows the vessel, even when it is sold, such that you may recover for your goods or services even if the party who hired you no longer owns the vessel." *Pacific Maritime Magazine*, October 1996, *Arresting a Ship: Actions In Rem*
2. **WHEN DOES A LIEN FOR A MARITIME CONTRACT ATTACH**
Courts have long understood that maritime liens for charters and shipping contracts attach at the beginning of the contract and remain inchoate until breached.
3. **WHEN DOES A LIEN FOR REPAIRS TO A VESSEL ATTACH**
"Where repairs, being performed under contract, were begun before, but not completed until after recording and endorsement, it has reasonably been held that the entire repair claim was entitled to priority. The basis of such holding seems to be that the repair man was under a contractual duty to go forward with the work." *Bank One Louisiana, N.A. v. M/V Mr. Dean, et al.*, 293 F.3d 830 (5th Cir. June 10, 2002); *Gilmore & Black* at 755-56, citing *The Eastern Shore*, 31 F. Supp 964 (D. Md. 1940), and *The Transford*, 1929 A.M.C. 727 (E.D. NY 1929)

4. MARITIME LIEN IS NONCONSENSUAL AND UNRECORDED

A maritime lien is non-consensual and unrecorded; it also follows the vessel into the hands of even a good faith purchaser. *Admiralty and Maritime Law 3rd Ed.*, Thomas J. Schoenbaum, Vol. 1, pg. 504; *United States v. Z. P. Chandon*, 889 F. 2d. 1990 (9th Cir. 1989)

5. UCC DOES NOT APPLY TO MARITIME LIENS

The Uniform Commercial Code does not apply to maritime liens. The ship owner's charter lien upon sub-freights earned by the charterer prevailed against the bankruptcy trustee, even though the lien was not filed. *Admiralty and Maritime Law 3rd Ed.*, Thomas J. Schoenbaum, Vol. 1, pg. 504, footnote 55; *Walsh v. Placedo Shipping Corp. of Liberia (In re Pacific Caribbean Shipping)*, 789 F.2d. 1406 (9th Cir. 1986)

6. WHEN DOES A MARITIME LIEN ARISE

A maritime lien arises from the moment of the service or occurrence that provides its basis. *Admiralty and Maritime Law 3rd Ed.*, Thomas J. Schoenbaum, Vol. 1, pg. 50; *Riffe Petroleum Co. v. Cibro Sales Corp.*, 601 F.2d 1385 (10th Cir. 1979)

7. MARITIME LIENS CAN NOT BE FILED UNLESS A MORTGAGE HAS BEEN RECORDED

U.S. Code, 46 USC 31343(a), establishes the basis for filing maritime liens if the vessel already has a preferred ship mortgage (emphasis added). Unfortunately, there is no way to file a maritime lien if the vessel is not mortgaged and, thus, such liens, though unrecorded, may prime the preferred ship mortgage. *46 USC § 31343 (a)*

8. MARITIME CONTRACTS THAT GIVE RISE TO A MARITIME LIEN

Maritime contracts giving rise to a maritime lien against the vessel include: dockage; stevedoring; loading and unloading of the vessel; and stowage and securing of cargo aboard the vessel. *Inbesa America, Inc v. M/V Anglia*, (11th Cir. 1996)

9. STATUTE ESTABLISHING MARITIME LIEN FOR “NECESSARIES” IS BROADLY CONSTRUED

The maritime lien for “necessaries” includes not only the services included in the statute, but is “broadly construed to mean any goods or services that are useful to the vessel, keep her out of danger, and enable her to perform her particular function...Necessaries may be money, skill, labor, and personnel services, as well as materials.” *Admiralty and Maritime Law 3rd Ed.*, Thomas J. Schoenbaum, Vol. 1, pg. 508; *Equilease Corp v. M/V Sampson*, 793 F.2d. 598 (5th Cir. 1986)

10. CANNOT PURCHASE A VESSEL FREE OF EXISTING MARITIME LIENS

Though a new owner may have purchased a vessel free of any personal obligations under an existing time charter, the purchaser could not terminate the vessel's obligations under the charter that may be the subject of a maritime lien. Thus, the vessel can be arrested pursuant to that maritime lien. *Bargecarib Incorporated v. Offshore Supply Ships Incorporated*, 168 F.3d 227 (5th Cir. 1999)

11. BREACH OF CHARTER COULD GIVE RISE TO A MARITIME LIEN

Breach of a time charter by the owner could give rise to a maritime lien. It is based on the fiction that the vessel may be a defendant in a breach of contract action where the vessel itself has begun to perform under the contract. *E.A.S.T., Inc. of Stamford, Conn. v. M/V Alaia*, 876 F.2nd 1168 (5th Cir. 1989); *Bargecarib Incorporated v. Offshore Supply Ships Incorporated*, 168 F.3d 227 (5th Cir. 1999)

12. STATE LIENS

A lien may be recognized under state law for something furnished to a vessel that is not accorded lien status under the Lien Act. Such state legislation, maritime in nature but applicable to areas not covered by federal maritime law, may be enforced *in rem* in federal court under the maritime jurisdiction of the United States. *Stephens Boat Co. Inc. v. The Barge Orr 1 et al.*, 791 F. Supp, 145, (E.D. La. 1992); *City of Erie v. S.S. North American*, 267 F.Supp. 875 (W.D. Pa. 1967); *Burdine v. Walden*, 91 F.2d. 321 (5th Cir. 1937); *Goudy & Stevens Inc. v. Cable Marine, Inc.*, 665 F.Supp. 67 (D. Me 1987); *Cary Marine, Inc. v. M/V Papillon*, 872 F.2d. 751 (6th Cir. 1989)

13. FINANCIAL UNSEAWORTHINESS OF THE VESSEL

Damage to cargo resulted from breach of contract of carriage by the vessel and also from the physical and financial unseaworthiness of the vessel and the negligence of her owners and/or operators. That claim primed the liens of the preferred ship mortgages. Additionally, expenses of unloading vessel after seizure were necessary to maintain its value, and thus were *custodia legis* expenses and primed the preferred ship mortgage. *Associated Metals and Minerals Corp. v. M/V Alexander's Unity*, 41 F.3rd 1007 (5th Cir. 1995)

14. MARITIME LIENS ARE INCIDENTS OF MOST MARINE TRANSACTIONS

"A maritime lien is an incident of most maritime transactions. (A) court has the right to create new [maritime] liens as the need arises." *Tulane Law Review* 558 (1973), *Introduction to the Law of Maritime Liens*, 47(3)

15. SUBROGATION OF MARITIME LIEN RIGHTS

The issue was whether a group of investors who paid off refurbishing costs and thus eliminated the possibility of a maritime lien against the vessel by the refurbisher are entitled to be subrogated to the rights of the refurbisher and the refurbishers maritime lien. They would then prime the position of the defendant, C.I.T. Based on the facts of this case, the court did not allow the subrogation of the maritime lien though it found that the general rule is that a creditor who advances money for the discharge of a maritime lien is subrogated to the lienor's rights. *Wilkins, et al. v. C.I.T., No. 97-3182* (11th Cir. 1998)

16. MARITIME LIENS DURING VESSEL CONSTRUCTION

In France and many other countries, maritime claims arising during construction of vessel are of the nature of maritime liens and subject the vessel to possible arrest.

17. LEGAL PRESUMPTION OF A MARITIME LIEN

Under the Federal Maritime Lien Act, a presumption arises that one providing supplies to a vessel acquires a maritime lien, which would prime the preferred ship mortgage if it was earlier in date.

18. MARITIME LIENS ARISING UNDER THE 1999 TREATY ON ARREST OF VESSELS

The 1999 treaty on arrest of vessels provides the basis for the arrest of a vessel in a foreign port to enforce maritime liens against the vessel. It revised the 1952 Convention and added and expanded types of maritime liens which would be covered by the treaty: costs of repatriation of the crew; marine insurance; brokerage fees; commissions and agency fees; ship reconstruction and repair costs; etc. *The International Convention on Arrest of Ships 1999*

19. MARITIME LIENS CAN BE SECRET AND OPERATE TO THE PREJUDICE OF CREDITORS AND PURCHASERS

"The maritime 'privilege' or lien is adopted from the civil law, and imports a tacit hypothecation of the subject of it. ...It accompanies the property into the hands of a bona fide purchaser. It can be executed and divested only by a proceeding *in rem*. ... (T)his privilege or lien, though adhering to the vessel, is a secret one; it may operate to the prejudice of general creditors and purchasers without notice." *The Yankee Blade*, 19 How. 82 (1857)

20. KNOWLEDGE BY OWNER UNNECESSARY FOR THE CREATION OF A MARITIME LIEN ON THE VESSEL

The U.S. Supreme Court ruled that even though the owner of vessel was unaware that master of chartered vessel contracted for necessary supplies, the transaction created a maritime lien and thus bound the ship. (The lien would remain against the vessel when sold and would prime a subsequent preferred mortgage unless released by operation of law.) *South Coast S. S. Co. v. Rudbach*, 251 US 522 (1920)

21. HOW DOES A MARITIME LIEN AFFECT THE VESSEL

Ability to move and/or sell replica ships adversely affected as a result of liens placed against the ships by the guarantor of the civic group who leased the vessels. Guarantor stated that liens were "more of an attention-getter." That result was achieved, as the vessels could not be used, moved or sold. *Spain U.S.A. Foundation as Owner of the Vessels Nina, Pinta and Santa Maria v. Durrill*, No. H-00CV4465 (S.D. Texas); *The National Law Journal*, January 23, 2001, *Liens Ground Columbus Fleet*

22. **THE MARITIME LIEN FOR NECESSARIES – EXAMPLES**

The maritime lien for necessities is broadly construed by the courts. “[W]hat is considered a necessary may come as something of a surprise. Liquor for the bar and restaurant on a passenger ship...[c]igarettes supplied to a fishing vessel for a trip of four to five months duration...A company which removed passenger baggage from a ship to fumigate it so as to prevent the entry of typhus germs into the United States...provided a necessary service...[t]ravelers checks issued for the purpose...that they be used to advance crew wages...[p]reparing and filing documents in connection with the procurement of a marine mortgage..., and clerical services furnished to a vessel.” *Pacific Maritime Magazine*, October 1996, *Arresting a Ship: Actions In Rem*

23. **CAN A JOINT VENTURE PARTNER GET A MARITIME LIEN ON THE VENTURES VESSEL**

In anticipation of a joint venture, potential joint venture partner began making renovations to vessel. Court found that potential joint venture partner was entitled to a maritime lien on the vessel for work done on it. *Captain Mark Rose v. M/V Gulf Stream Falcon*, 186 F.3d 1345 (11th Cir. 1999)

24. **ENFORCING THE MARITIME LIEN**

“Under United States maritime law, a company that supplies goods or services to a vessel in a U.S. Port, such as stevedoring services, pilotage, line handling, provisions and stores, or repairs, has a maritime lien on the vessel for the unpaid amount of the goods or services provided. This maritime lien is a secret, unrecorded lien that can be enforced by “arresting” the vessel in a U.S. Port. But what can you do if the vessel never again calls at a U.S. Port? Fortunately, there is an international treaty which provides some relief to U.S. lienholders.” *The Quartermaster Newsletter*

25. **AGENCY CONTRACTS CAN GIVE RISE TO MARITIME LIENS**

The U.S. Supreme Court overruled a case that said that agency contracts were not subject to admiralty jurisdiction. In so doing the court said that you must look at the nature and subject matter of the transaction. Furnishing fuel to a vessel through an agent in a foreign port is a maritime transaction. The issue is whether the transaction gives rise to a maritime lien and, if so, where would that lien rank. *Exxon Corp. v. Central Gulf Lines, Inc.*, 500 U.S. 603 (1991)

26. **A FISHING PERMIT IS AN APPURTENANCE OF THE VESSEL**

Federal fishing permit deemed to be an appurtenance of the vessel and subject to a maritime lien and therefore subject to sale together with the vessel. Often the fishing permits have more value than the vessel and are an attractive target for those with maritime lien claims. *Gowen Inc. v. F/V Quality One*, 244 F.3d 64 (1st Cir. 2001)

27. **AN AGENT CLAIMING A MARITIME LIEN**

Vessel charterer engaged agent to provide fuel for vessel through a third party. Court found that the agent had provided necessities to the vessel and, thus, was entitled to a maritime lien against the vessel for the amount it paid to the fuel provider. *Galehead, Inc. v. M/V Anglia*, 183 F.3d 1242 (11th Cir. 1999)

28. **PROFITS OR COMMISSIONS INCLUDED IN A LIEN FOR NECESSARIES**

A maritime lien for necessities can include a profit or commission earned by the beneficiary of the lien. *Galehead, Inc. v. M/V Anglia*, 183 F.3d 1242 (11th Cir. 1999)

29. **SUBCONTRACTOR ENTITLED TO A MARITIME LIEN**

Third party to a transaction may be entitled to maritime lien against the vessel resulting from repairs the third party performed, even though the third party was engaged by a contractor. *Marine Coatings Inc. of Alabama v. United States*, 932 F.2nd 1370, (11th Cir. 1991); *Stevens Technical Services, Inc. v. United States*, 913 F.2nd 1521, (11th Cir. 1990); *Gowen Inc. v. F/V Quality One*, 244 F.3d 64 (1st Cir. 2001)

30. **MARITIME LIEN FOR BREACH OF CHARTER ALLOWS CHARTERER TO ARREST THE VESSEL**

A maritime lien for breach of a charter entitles the charterer to proceed *in rem* directly against the vessel. A maritime lien affords special protection to the party who has been injured by a breach of a maritime contract. *Cardinal Shipping Corp. v. M/S Seisho Maru*, 744 F.2nd 461 (5th Cir. 1984); *Bargecarib Incorporated v. Offshore Supply Ships Incorporated*, 168 F.3d 227 (5th Cir. 1999)

31. **CHARTERER’S BUNKERS ON ONE VESSEL SEIZED FOR FAILURE TO PAY FOR BUNKERS ON ANOTHER VESSEL**
 When charterer of a vessel failed to pay charter hire on one vessel, the owner commenced legal proceedings and had the U.S. Marshall seize bunkers owned by the charterer on another vessel that was also owned by the ship owner. *Casper Marine, Inc. v. Seatrans Shipping Corp.*, 969 F.Supp 395 (E.D. La., 1997)
32. **CANADIAN PREFERRED MORTGAGE PRIMED BY LATER MARITIME LIEN/SISTER SHIP ARREST**
 For vessels that call on Canadian ports, a mortgage holder or owner is particularly vulnerable. A preferred ship mortgage (whether Canadian or US) may be primed by a maritime lien even if it occurred after the date of the mortgage. Also, Canada allows “sister ship” arrests of vessels. Thus, a vessel is subject to arrest and sale for a lien incurred by another vessel commonly owned.
33. **IN BANKRUPTCY, ADMIRALTY COURT HAD JURISDICTION OVER FREIGHTS WHICH WERE DISTRIBUTED TO MARITIME LIEN CLAIMANTS**
 In Bankruptcy of Hellenic American Agencies, which began as a Chapter 11 reorganization and ended as a Chapter 7 liquidation, it was ruled that the admiralty court should exercise jurisdiction over freights due and within the custody and control of Hellenic for the purposes of their distribution to maritime lien claimants. *Morgan Guaranty Trust Company of New York, et al. v. Hellenic Lines Limited, et al.*, 585 F.Supp. 1227, 1984 AMC 2409 (S.D. NY 1984)
34. **FAILURE TO PAY INSURANCE PREMIUMS CREATES A MARITIME LIEN**
 Under United States law, the Federal Maritime Lien Act, 46U.S.C. §§ 31341-43, establishes a maritime lien for the provision of necessities, which include marine insurance. *Equilease Corp. v. M/V Sampson*, 793 F.2d 598, 603 (5th Cir. 1986) (*en banc*); *Liverpool and London Steamship Protection and Indemnity Association Limited v. Queen of Leman, et al.* consolidated with *Liverpool and London Steamship Protection and Indemnity Association Limited v. M/V Abra, et al.*, --F.3d--, 2002 WL 1380876 (5th Cir., June 27, 2002)
35. **FAILURE TO PAY INSURANCE PREMIUMS CREATES A MARITIME LIEN**
 This was a consolidated case involving a conflict of laws as to whether or not there was a maritime lien for failure to pay P & I insurance premium for a vessel. Under English law no lien existed. Under American law a lien does exist. The court found that American law applied and, thus, a maritime lien existed and the vessel was subject to being arrested *in rem* to enforce the lien. "The maritime lien having arisen as a result of the failure to pay a contractual debt, it attaches to the ship and binds subsequent owners..." *Liverpool and London Steamship Protection and Indemnity Association Limited v. Queen of Leman, et al.* consolidated with *Liverpool and London Steamship Protection and Indemnity Association Limited v. M/V Abra, et al.*, --F.3d--, 2002 WL 1380876 (5th Cir., June 27, 2002)
36. **MARITIME LIEN FOR BREACH OF CHARTER PARTY**
 RR Caribbean leased the dredge “Jumby Bay” from Blue Green Marine Ltd. The parties then got into a legal squabble and RR Caribbean filed a claim *in rem* alleging a breach of charter party. The court stated, “A maritime lien may arise in tort or contract, and in contract, it may arise under the Federal Maritime Lien Act or under the general maritime law. Under the general maritime law, a maritime lien arises in favor of a charterer ‘[i]f a vessel owner breaches a charter party that is at least partially performed.’ Blue Green, by delivering the Jumby Bay to RR Caribbean, partially performed its lease agreement, or charter party. Being partially executed, the charter party was capable of giving rise to a maritime lien...” *RR Caribbean, Inc. v. Dredge “Jumby Bay,”* 147 F.Supp.2d 378 (D.Virgin Islands, 2001); 8 *Benedict on Admiralty* § 12.01[C][1][d][iii] (7th ed., rev. 2000)

III. Fraud, Forgery, Incompetency, Etc.:

1. **FORGED, FRAUDULENT, ETC. DOCUMENTS**

A preferred ship mortgage can be unenforceable even if properly recorded when documents in the chain of title are forged or executed under fraud, undue influence, duress or mistake.

2. **UNAUTHORIZED OR FALSE AUTHORIZING DOCUMENTS**

A preferred mortgage can be unenforceable even if properly recorded when documents are executed without authorization and/or pursuant to false authorizing resolutions by corporations, partnerships, limited liability companies, trusts or other entities. *ITT Industrial Credit Company v. M/V Richard C*, 617 F. Supp. 761 (E.D. La. 1985)

3. **FRAUDULENT VESSEL LOAN**

This is a criminal case in which the defendants perpetuated a scheme in which they sought and made \$1,200,000 worth of loans on a non-existent vessel. *United States v. Camaille, et al.*, No. 84-179 (E.D. La.)

4. **FRAUD AND MISREPRESENTATION BY THE MORTGAGOR**

Buyer/Borrower Christophides purchased a vessel for \$2 million that was financed by bank. The conditions of the loan included a personal guaranty, a requirement that the vessel be long term chartered to Levant, and the loan be cross-collateralized with a \$5.7 million loan bank previously made to Levant for the purchase of two other vessels (which loan was then in default). Levant then breached the charter party and Christophides consequently defaulted on his loan. During litigation it was alleged that the Levant financing was secured through misrepresentation because a Levant director bribed two bank officers. The case was remanded back to the district court to unravel and determine whether the bank could collect from Christophides. *Banque Franco-Hellenique de Commerce International ey Maritime, S.A. v. Christophides*, 1997 WL 317398 (2nd Cir. 1997)

5. **FORGED POWER OF ATTORNEY**

An individual wanted to buy a yacht owned by a corporation. One of the requirements of closing was a certified copy by the corporate secretary of a resolution from the corporation's board of directors authorizing the sale. The "seller" showed up at the closing with a power of attorney instead of the resolution. The buyer and lender accepted the power of attorney and the transaction closed. Later it was discovered that the power of attorney was forged. Title insurance would have insured this transaction for the buyer and his lender.

6. **DOCUMENTS EXECUTED BY ONE WITHOUT APPROPRIATE CAPACITY**

A vessel title and mortgage would be in jeopardy (even if properly recorded) if documents are executed by one who does not have appropriate capacity, such as a minor or a person who is insane or mentally incompetent.

7. **ALTER EGO - WHAT AFFECT ON THE MORTGAGE**

Banchory attempted to recover proceeds from the sale of an arrested vessel, "Pride of Donegal," though the amount claimed by Banchory was due from the manager of the vessel for unpaid charter hire for another vessel. The effect of what Banchory wanted would be for Banchory to prime the mortgagee of the "Pride of Donegal." Banchory alleged: that the manager and the record owner of "Pride of Donegal" were alter egos; that because of fraud and misrepresentation, the mortgage was invalid; or that the mortgage should be equitably subordinated to Banchory. After extensive litigation, the court gave priority to the mortgage. *Banchory Shipping v. Banco Wiese Limitado*, 160 F.3d 170 (4th Cir. 1998)

8. **FABRICATING CHARTERS TO INDUCE A LENDER TO LOAN MONEY**

In a claim in the Commercial Court in London involving Berliner Bank, the issue revolved around a vessel buyer fabricating long term charters upon which the lender relied. Title insurance protects against fraud in the transaction.

9. **THE AFFECT OF UNTRUSTWORTHY DOCUMENT BACK-UP**

Documents allegedly supporting ship mortgages lacked basic indicia of trustworthiness and solemnity that reasonable person would normally expect of legitimate records relating to transactions involving

large sums, and thus irregularity of such documents would be considered in determining whether mortgages were gratuitous. *Bergesen d.y. A/S v. Lindholm*, 760 F. Supp. 976 (D.Conn. 1991)

10. BOAT BROKER POCKETED MONEY

A south Florida boat broker has been accused of numerous instances of fraud in conjunction with performing his duties. The *Fort Lauderdale Sun-Sentinel* in two articles reported the following alleged incidences of fraud involving the broker: selling boats and pocketing the money; failing to satisfy liens on vessels he sold; writing a bad check to pay off a lien on a vessel; selling boats with funds borrowed from Deutsche Bank and failing to turn over its share of the proceeds; selling a vessel that did not exist in order to get financing from Bank of the West; using a forged certificate documenting the existence of a vessel. *Fort Lauderdale Sun-Sentinel* "Police: Boat broker pocketed money meant for clients," June 22, 2002; *Fort Lauderdale Sun-Sentinel* "Boat broker accused of fraud," June 9, 2002

11. RECISSION OF VESSEL SALE

Evidence was sufficient to find that under Louisiana law the seller of a ship and the seller's principal were guilty of fraud warranting the rescission of the sale for redhibitory vices. *Lynhaven Dolphin Corp. v. E.L.O. Enterprises, Inc.*, 776 F.2d 538 (5th Cir. 1985)

IV. Errors During the Process:

1. DELAYS OF RECORDATION OF MORTGAGE

Alberto purchased a yacht financed by Maryland National Bank. The mortgage was presented to the U.S. Coast Guard for recordation but it was not recorded or endorsed on the vessel's abstract for 6 ½ months. Meanwhile, Alberto filed for bankruptcy. Can the bankruptcy trustee avoid the bank's interest in the vessel? Does the bankruptcy automatic stay bar recordation of the mortgage? The bankruptcy judge and the district court ruled against the bank. Under the facts, the circuit court reversed and remanded. *Alberto v. Maryland National Bank*, 823 F.2d 712 (3rd Cir. 1987)

2. THE EFFECT OF AN ERRONEOUS VESSEL ABSTRACT

A preferred mortgage can be adversely affected because of administrative issues at the Coast Guard National Vessel Documentation Center (NVDC), including erroneous abstracts resulting from: home port changes in the chain of title; the establishment of the NVDC; the fire at the NVDC; and computer malfunctions at the NVDC.

3. DANGER OF RELYING ON A LEGAL OPINION

Lender pursued claim against owner's attorneys who issued an opinion on which the lender relied, but which contained false assurances. Trial court said there was no privity between the lender and the borrower's attorney and, thus, denied the lender the right to rely on the opinion. *The Prudential Insurance Company of America v. Dewey Ballantine, Bushby, Palmer & Wood, & Gilmartin, Poster & Shafto*, 80 N.Y. 2d. 377, 605 N.E. 2d 318 (1992)

4. ESCROW AGENT ERROR

Commerce entered into an agreement with Beluga to purchase all of the stock of Sando, a subsidiary of Beluga, whose sole asset was a vessel. Beluga would surrender its stock certificates of Sando and new certificates from Sando would be issued to Commerce. The new stock certificates were to be held by an escrow agent who would hold them until the full purchase price was paid. The vessel was to be sold for cash and a promissory note from Sando to Beluga was secured by a mortgage on the vessel. The escrow agent withdrew and turned the stock certificates over to Commerce's attorney who then turned them over to Commerce. Armed with the certificates, Commerce obtained possession of the vessel and sailed off to the Bahamas. Commerce then gave a mortgage to Beluga but refused to make the cash payment. Beluga attempted to foreclose on the mortgage *in rem* and the suits and counter suits started flying. In addition to the basic reasons to acquire title insurance (protection for title problems and against liens and encumbrances), the complexity and structure of the transaction lends itself perfectly to title insurance. No other tool better protects the lender and owner. And if things go bad as happened here, title insurance provides cost of defense and prosecution. Additionally, the title insurer could provide reliable and

legally responsive escrow services. *Beluga Holding, Ltd. v. Commerce Capital Corporation*, 212 F.3d 1199 (11th Cir. 2000)

5. **ERRORS BY THE CLOSING ATTORNEY OR VESSEL DOCUMENTATION AGENT**

The title to a vessel may be defective and the mortgage of the vessel may be in jeopardy if the vessel documentation company, attorney, or closing agent hired to handle the transaction made a mistake: in searching the records; rendering its report; drafting documents; filing documents; releasing documents out of escrow without authorization; etc. Title insurance insures mistakes in the purchase and mortgage processes.

6. **COAST GUARD ERROR**

Two mortgagees were fighting over which mortgage primed. WRT, a party to the litigation, filed its mortgage first, but there is some question over whether there was a transfer of funds. Regardless, the U.S. Coast Guard erred because it reflected in the public record that the WRT mortgage had been terminated. GECC, the other party to the litigation, entered into a mortgage almost ten months later and almost five months after the erroneous record was established. The court said that even though a search of public records could not have disclosed the pre-existing encumbrance due to Coast Guard error, that mortgage (the pre-existing encumbrance) is valid against third parties from the time it was filed. In this case, the court overlooked the Coast Guard error in favor of the WRT mortgage to the detriment of the GECC mortgage. Title insurance would clearly have helped both parties. It would have provided defense costs to each and would have paid the loss of the losing party. *Mayfield v. The Energy VII*, 1999 WL 38163 (E.D LA, 1999)

7. **MISINTERPRETATION OF DOCUMENTS LEADING TO INCORRECT REPORT ON TITLE AND LIEN STATUS**

Misinterpretation of documents of record by the person or company performing the lien search giving an incorrect or misleading report on the status of title, liens, claims or encumbrances against the vessel should be of concern to a vessel buyer or lender. Vessel title insurance would cover these risks.

8. **SUBORDINATION AGREEMENT BECOMES INEFFECTIVE OR FAILS**

If a subordination agreement is part of a transaction and it becomes ineffective or otherwise does not accomplish its purpose, the intended junior interest may be reinstated to priority. Title insurance covering the transaction could insure the issue.

9. **COAST GUARD REFUSED TO RECORD AMENDED PREFERRED MORTGAGE**

Though mortgagor signed an amended preferred ship mortgage before a notary, mortgagee failed to sign the amended mortgage and the National Vessel Documentation Center refused to record the document.

10. **INFORMATION IN COAST GUARD'S ON-LINE VESSEL DATA BASE CALLED "UNTRUSTWORTHY" AND "VOODOO INFORMATION"**

In an injured seaman suit where the defendant claimed that it did not own the vessel at the time of the injury, the plaintiff countered with evidence from the U.S. Coast Guard's internet on-line vessel database. The court rejected that evidence and called it inherently "untrustworthy" and "voodoo information." Needless to say, reliance on the Coast Guard's internet vessel database for vessel ownership, title or related questions is extremely imprudent. *St. Clair v. Johnny's Oyster & Shrimp, Inc.*, 76 F.Supp2d 773 (S.D.Texas)

11. **TRANSACTIONS THAT VIOLATE PUBLIC POLICY**

The buyer does not have legal title and a lender's mortgage on the vessel would be void if the transaction (or possibly if a transaction in the chain of title) violates public policy (e.g. payment of a gambling debt or as part of a crime).

12. **WHAT HAPPENS WHEN LEGAL OPINION IS WRONG? CAN YOU SUE YOUR LAWYER**

"A Minnesota bank, sued its Louisiana lawyers after they gave an opinion letter that turned out to be incorrect. The firm had stated that a fleet mortgage securing the construction of two dockside casinos in Mississippi gave the bank's bondholders a security interest 'superior to all other liens.' This advice ultimately turned out to be wrong: after the mortgagor ran into financial problems, the contractor instituted litigation and a bankruptcy court in Mississippi ruled the fleet mortgage invalid and

unenforceable. On behalf of the bondholders, the bank then filed a malpractice action in Mississippi. The firm responded by filing a motion to dismiss on the ground that personal jurisdiction was lacking. The court, finding this contention to have merit, granted the motion." *Journal of Maritime Law and Commerce*, 31 JMARLC 407, (July, 2000), *The Erring Proctor: Admiralty Lawyers and Malpractice Claims*, Robert M. Jarvis; *First Trust National Association, as Indemnitor Trustee v. Jones, Walker, Waechter, Poitevent, Carrere & Denegre et al.*, 996 F. Supp. 585 (S.D. Miss., 1998)

13. **WAS THE PREFERRED MORTGAGE FOR \$92,000,000 OR \$92,000; OR THE CASE OF THE MOVING DECIMAL POINT**

This case involves a \$92 million typographical error. Prudential Insurance loaned U.S. Lines funds secured by a preferred ship mortgage. A few years later, U.S. Lines restructured its debt and GECC ended up with a second preferred mortgage. Thereafter, U.S. Lines filed for bankruptcy at which time it was discovered that the Prudential corollary ship mortgage amendment contained an inadvertent error; namely, one section stated that the outstanding balance was \$92,885 instead of \$92,885,000. GECC and the other creditors argued that the Prudential mortgage priority was limited to the \$92,885 as, inter alia, a preferred ship mortgage is strictly construed and must comply in every respect without error with the procedures of the Ship Mortgage Act. After considerable litigation, the court moved the decimal back to where the parties originally intended and maintained the priority of the Prudential mortgage. *The Prudential Insurance Company of America v. S.S. American Lancer et al.*, 870 F.2d 867, 1989 A.M.C. 1097 (2nd Cir. 1989)

V. Priority of Mortgage:

1. **POOR BANKING PRACTICES CAN LEAD TO EQUITABLE SUBORDINATION OF MORTGAGE**

The lender bank, in the trial court's opinion, failed to exercise good standard lending practices by doing such things as ensuring that the official number was properly engraved on the vessel. Thus, it was possible for a fraud to be perpetuated by allowing two vessel documents and mortgages to exist against the same vessel. The court then found that the lender bank was equitably subordinated to the second filed mortgage. The appellate court overruled the lower court based on the facts. *Maryland National Bank v. The Vessel Madame Chapel*, 46 F.3rd 895 (9th Cir. 1995)

2. **INSURED CLOSING LESSENS RISK OF EQUITABLE SUBORDINATION**

If a lender utilizes a First American insured closing, the issue of equitable subordination (as described in Section V, No. 1) could become the title insurer's problem and form part of the insurance package. *Maryland National Bank v. The Vessel Madame Chapel*, 46 F.3rd 895 (9th Cir. 1995)

3. **SALE OR MORTGAGE MUST BE RECORDED WITH COAST GUARD TO BE VALID AGAINST THE PUBLIC**

No sale or mortgage, which includes a vessel of the United States, is valid against any person other than grantor or mortgage owner and anyone with actual notice until bill of sale or mortgage is recorded with U.S. Coast Guard at vessel's home port (now the National Vessel Documentation Center at Falling Waters, WV). *Maryland National Bank v. The Vessel Madame Chapel*, 46 F.3d 895 (9th Cir. 1995)

4. **IF A VESSEL IS NO LONGER A "VESSEL," PREFERRED MORTGAGE MAY BE UNENFORCEABLE**

A preferred mortgage can be ruled unenforceable by a judge even if properly recorded if the vessel lacks legal vessel status as defined by 1 U.S.C. §3. *Biloxi Casino Belle Incorporated v. MRA, Ltd. dba Casino Belle of Tunica, et al.*, 176 B.R. 427 (S.D. Miss., 1995); *In the Matter of Treasure Bay Corp.*, 205 B.R. 490, 1997 AMC 2878 (S.D. Miss., 1997); *Daniel v. Ergon, Inc.*, 892 F.2d 403 (5th Cir. 1990)

5. **IF NOT A "VESSEL," MORTGAGE FILED WILL NOT QUALIFY AS PREFERRED SHIP MORTGAGE**

The Biloxi Belle II Casino and the Southern Belle Casino were not "capable of being used as a means of transportation on water" when First Trust filed its purported preferred ship mortgage on the casinos. As a result, the documentation previously issued by the U.S. Coast Guard was invalid. Consequently, the

purported mortgage filed by First Trust did not qualify as a preferred ship mortgage under the Ship Mortgage Act. *In re Biloxi Casino Belle Incorporated*, 176 B.R. 427 (USBC SD Miss, 1995)

6. MARITIME LIEN BREACH OF CHARTER HAS PRIORITY OVER PREFERRED MORTGAGE IF IT ATTACHES BEFORE MORTGAGE IS RECORDED

Rainbow Line, Inc. sought and was awarded damages for a breach of a charter party. Meanwhile, the vessel was sold, mortgaged and then the owner defaulted on the mortgage. The vessel was arrested and sold. The mortgagee argued that it was unjust for a secret lien arising out of a breach of a maritime contract to prime the mortgage. The court ruled that a breach of charter has priority over the mortgage if it has attached before the mortgage was recorded. *Rainbow Line, Inc. v. The Tequila*, 480 F.2d 1024 (2nd Cir. 1973)

7. LIENS FOR NECESSARIES DO NOT HAVE TO BE FILED TO PRIME MORTGAGE

Preferred ship mortgage is primed by a preferred maritime lien that includes those liens arising before the preferred ship mortgage is filed, including liens for necessities. Note that liens for necessities do not have to be filed to be valid and prime the mortgage. *Bank of America v. M/V Pengwin, et al.*, No. 97-36050 (9th Cir. 1999)

8. WHAT IS A RENEWAL OF A MORTGAGE AS OPPOSED TO A NEW MORTGAGE

The bank had two mortgages that predated a lien for necessities. After the lien for necessities attached, the bank amended, renewed and/or entered into three more mortgages each one in an amount larger than the two original mortgages. In a facts driven case, the court found that the three subsequent mortgages were renewals or amendments of the original two mortgages, which did not lose their priority to the extent of the amount of debt existing on the date the lien holder perfected its lien. *Bank of America v. M/V Pengwin, et al.*, No. 97-36050 (9th Cir. 1999)

9. WHEN DOES PREFERRED MORTGAGE BECOME PERFECTED

Mortgage on debtor's yacht was not perfected until U.S. Coast Guard endorsed and recorded it in accordance with Ship Mortgage Act, though mortgage had been delivered to Coast Guard by mortgagor approximately three months earlier; accordingly, trustee could exercise rights as judicial lien creditor and avoid mortgage, where debtor had filed for bankruptcy in interim. *Matter of Alberto*, 66 B.R. 132 (D.N.J. 1985)

10. THE IMPUTATION OF MORTGAGEE'S BAD FAITH

The court ruled that the filing of a false certificate that the vessel's official number was affixed to the vessel, when the lender did not have knowledge that the vessel was not marked, would not affect the status of the preferred mortgage. However, the mortgagee's bad faith will defeat the preferred status. Query, what does it take for knowledge to be imputed to the mortgagee? *Maryland National Bank v. The Vessel Madame Chapel*, 46 F.3rd 895 (9th Cir., 1995)

11. THE APPLICATION OF THE MORTGAGE RENEWAL RULE

The Mortgage Renewal Rule generally is that in the absence of an indication of contrary intent, execution of a new mortgage in renewal, or amendment of a former one, does not extinguish priority of the former one. However, it only applies to the amount of debt remaining on the date of renewal. (emphasis added) *Bank of America v. M/V Pengwin et al.*, No. 97-36050 (9th Cir. 1999)

12. MARITIME LIEN FOR AN OVERPAYMENT OF FREIGHTS

The issue before the U.S. Supreme Court was whether a maritime lien was created for an overpayment of freights. The Court ruled that it did. They found it arose out of a contract of affreightment. Whether it was mistakenly done or fraudulent, a maritime lien still resulted and it could prime a preferred mortgage entered into after the event occurred. *The Pacific Cedar*, 290 U.S. 117 (1933)

13. EFFECT OF STATE LAW SECURITY ON U.S. DOCUMENTED VESSEL

Once a vessel has become a "vessel of the United States" (which is a vessel federally documented with the U.S. Coast Guard), the validity of security interests is determined by federal law. State law security interest in yacht that became "vessel of the United States" upon issuance of its certificate of documentation was nullified by statute, which invalidates mortgage on vessel of United States as to third parties without notice, unless recorded in office of collector of customs at home port of vessel (now the

U.S. Coast Guard National Vessel Documentation Center in Falling Waters, WV). This is true even though security interest and mortgage preceded issuance of certificate of documentation by U.S. Coast Guard. Recording procedures were applicable to all mortgages on vessels of United States regardless of when mortgages were made. *In re Alberto*, 823 F.2d 712 (3rd Cir. 1987)

14. WHEN DOES A VESSEL MORTGAGE BECOME PREFERRED

In this dispute before the U.S. Supreme Court, the question was which party was entitled to priority; the party alleging a lien for necessities or the vessel mortgagee. The Supreme Court reversed the lower courts and found in favor of the necessities lien holder (whose lien actually arose after the mortgage was in existence but before it was endorsed). The court noted that the mortgage becomes preferred only upon compliance with the conditions specified. *Morse Dry Dock & Repair Co. v. The Northern Star*, 271 U.S. 552 (1926)

15. PROTECTING THE LENDER DURING THE CONSTRUCTION PERIOD

The buyer of three boats that were to be built defaulted on payment for the second and third boats. The boats were resold by the builder who recovered his damages from the breach. A creditor of the buyer who furnished funds sought the excess proceeds from the sale. There were no maritime liens as the boats were not yet "vessels." The creditor asserted it had an unperfected security interest. Because the buyer did not attain rights in the collateral sufficient to meet the requirements for attachment of a security interest, the creditor is not entitled to distribution of the proceeds under Article 9 of the U.C.C. Instead, the rights of the buyer and seller are governed by Article 2, which puts the creditor in a less favorable position. First American offers a program of combined UCC and vessel title insurance for vessels under construction that protects lenders throughout the construction period and after when the vessel is documented and becomes a "vessel" eligible to become security under a preferred ship mortgage. *Connister Trust Ltd. v. Boating Corporation of America and Villas-Afloat, Ltd.*, 2002 WL 389864 (Tenn. Ct. App., 2002)

16. EQUITABLE SUBORDINATION

Preferred mortgage can be adversely affected by doctrine of equitable subordination. *Wardley International Bank v. Nasipit Bay Vessel*, 841 F. 2d 259 (9th Cir. 1988)

17. WHEN MARITIME LIENS OUT RANK THE PREFERRED MORTGAGE

Silver Star held two preferred ship mortgages on the M/V Saramaca. Trans Ocean, who furnished containers to the vessel Silver Star, commenced an *in rem* action against the vessel. The vessel was seized and sold, and the proceeds were deposited in the court to be distributed among the claimants depending on priority. The trial court ruled that Trans Ocean outranked the mortgagee, Silver Star, for a portion of Trans Ocean's claim. Based on the facts of this case, the appellate court reversed. *Silver Star Enterprises v. M/V Saramaca*, No. 94-30747 (5th Cir. 1996)

18. EFFECT OF SUBORDINATION OF PREFERRED SHIP MORTGAGE

In a bankruptcy, if a secured claim such as a maritime lien (which includes a preferred ship mortgage) is subordinated, it becomes part of the debtor's estate and, thus, is unsecured. 59 *Tulane Law Review* 1401, 1419, *Liens and Liquidation: Preferences, Strong Arm Clause, Fraudulent Transfers, Equitable Subordination, Priorities and Other Limitations on Liens Claims*

19. SUBORDINATION OF THE MORTGAGE TO MARITIME LIENORS

"(I)t is likely that courts will continue to look with disfavor on mortgagees who prop up insolvent shipowners to the detriment of other maritime lienors" and, under theories such as equitable subordination, subordinate the mortgage to the maritime lienors. 59 *Tulane Law Review* 1401, 1422, *Liens and Liquidation: Preferences, Strong Arm Clause, Fraudulent Transfers, Equitable Subordination, Priorities and Other Limitations on Liens Claims*; *Israel v. Nili*, 435 F.2d. 242 (5th Cir. 1970)

20. WHEN A VESSEL IS NOT A "VESSEL" PREFERRED SHIP MORTGAGE LOSES ITS PRIORITY

First Trust was the indenture trustee for mortgage notes secured by preferred ship mortgages on two casinos. The casinos went into bankruptcy and the other creditors attacked the preferred ship mortgages claiming that the casinos were not vessels for purposes of the Ship Mortgage Act. The court agreed

ruling against First Trust, and the mortgages, thus, lost their priority. *In the Matter of Treasure Bay Corp. et al.*, 205 B.R 490, 1997 AMC 2878 (B.C.S.D. Miss. 1997)

21. MISREPRESENTATION OF LIEN STATUS AND WEAKNESS OF RELYING ON U.C.C. FOR SECURITY FOR A VESSEL TRANSACTION

In a case involving a state-registered vessel, NBS purchased a yacht in Minnesota and financed the purchase through Richfield Bank. The lender held a U.C.C. perfected security interest in the yacht. Ultimately, the yacht was sold by NBS through TBY, the original yacht dealer, to Ichelson and moved to Iowa. Borg-Warner financed that purchase and filed a U.C.C. financing statement on the vessel in Iowa. TBY represented at the time of the sale to Ichelson that no liens existed on the yacht and that representation was relied upon. TBY told NBS that it would pay off the Richfield Bank loan with the proceeds of the sale. TBY reneged and instead filed for bankruptcy. The court applying U.C.C. principles of law held that the Richfield security is superior to Borg-Warner's. Additionally, it disallowed Borg-Warner and Ichelson's claims against NBS for breach of the warranty of title. Title insurance was the simple answer to this unfortunate situation. It would have protected both Ichelson and Borg-Warner by insuring the title and the priority of the security interest. It would have insured that the sale funds were used to pay off the prior loan. And, the expertise that a title insurer would have brought to the table would have recognized and, probably required, that the vessel be U.S. Coast Guard documented and that a preferred ship mortgage be placed on the vessel. *National Business Systems, Inc. et al. v. Borg-Warner Acceptance Corporation, et al.*, 792 F.2d. 710 (8th Cir. 1986)

22. CHARTER PRIMES PREFERRED SHIP MORTGAGE

A maritime lien attaches for a vessel when the charter commences and the vessel is placed at the disposal of the charterer. In this case, a tug owned by Offshore Supply Ships, Inc. was time chartered to BargeCarib; the tug was sold and the new owner financed the purchase with Bank One which placed a preferred ship mortgage on the vessel as security. Subsequent to the mortgage, the owner of the tug breached the charter party, then defaulted on its loan to Bank One. Bank One arrested the vessel. The 5th Circuit found that a maritime lien attached at the commencement of the charter party even though the actual breach of the charter occurred much later and, thus, found that the maritime lien that resulted from a breach of the charter had priority over the preferred ship mortgage. *Bank One Louisiana, N.A. v. M/V Mr. Dean, et al.*, 293 F.3d 830 (5th Cir., June 10, 2002)

23. UNPAID INSURANCE PREMIUMS MAY PRIME PREFERRED MORTGAGE

Failure to pay for vessel insurance premiums usually creates a maritime lien. If the insurance policy predates the preferred mortgage, the maritime lien for failure to pay premiums probably primes the mortgage even if the failure to pay arises after the date the mortgage went into effect. In the case of a P & I policy or other retrospective insurance premium schemes in which premium comes due well after the policy terminates, calls and additional premiums due may very well be included in the maritime lien. *Liverpool and London Steamship Protection and Indemnity Association Limited v. Queen of Leman, et al. consolidated with Liverpool and London Steamship Protection and Indemnity Association Limited v. M/V Abra, et al.*, --F.3d.-- 2002 WL 1380876 (5th Cir., June 27, 2002)

VI. Failure of Mortgage:

1. VESSEL HAD TWO DOCUMENTS AND TWO MORTGAGES

An owner documented a vessel with the U.S. Coast Guard, filed a preferred ship mortgage, and then registered the vessel with the state. The state-registered vessel was sold and then documented with the Coast Guard under a new official number, then resold, and another preferred ship mortgage was filed. Thus, there were two documents outstanding both of which had mortgages filed against them. Which mortgage was valid and which primed? *Maryland National Bank v. The Vessel Madame Chapel*, 46 F.3rd 895 (9th Cir., 1995)

2. VIOLATING COMMUNITY OR JOINT PROPERTY RIGHTS

A preferred mortgage can be unenforceable even if properly recorded when documents are executed in violation of community or joint property rights. *Heidi Morcher v. Merry Nash*, 1999 AMC 1413 (D.V.I. 1998)

3. **A VESSEL CEASES TO BE A “VESSEL”**
A preferred mortgage can be unenforceable even if properly recorded when the vessel ceases to be a vessel triggered by an event that automatically invalidates the documentation of a “vessel” pursuant to 46 C.F.R. Sec. 67.23-9.
4. **VALID CERTIFICATE OF DOCUMENTATION AT TIME OF FILING IS ESSENTIAL FOR VALID PREFERRED MORTGAGE**
In order to possess first preferred ship mortgage under Ship Mortgage Act, vessel must have valid certificate of documentation outstanding at time purported first preferred ship mortgage was filed. *In re Biloxi Casino Belle Inc.*, 176 B.R. 427 (S.D.Miss. 1995)
5. **PROOF OF VESSEL OWNERSHIP NECESSARY FOR VALID PREFERRED MORTGAGE**
Mortgagee must prove mortgagor's ownership of vessel as part of its burden of establishing valid preferred ship mortgage. *Chase Manhattan Financial Services, Inc. v. McMillian*, 896 F.2d 452 (10th Cir. 1990)
6. **PROVISIONS OF SHIP MORTGAGE ACT ARE STRICTLY CONSTRUED**
Provisions of Ship Mortgage Act relating to perfection of ship mortgages must be strictly construed. *Matter of Alberto*, 66 B.R. 132 (D.N.J. 1985)
7. **MORTGAGEE’S BAD FAITH AND OTHER MORTGAGEE BREACHES**
When vessel was arrested and sold pursuant to a preferred ship mortgage, the owners of the vessel, in defense of the deficiency judgment against them, alleged that the bank breached its fiduciary duty, breached the duty of good faith and fair dealing by damaging the vessel and allowing it to deteriorate, and failed to provide proper notice. While under the particular facts of this case the court found for the bank, the result could have been different. The case is illustrative of the innovation and creativity of those who attack the priority and sanctity of the preferred mortgage. *Maryland National Bank v. Traenkle*, No. 00-1746, 10 Fed Appx. 194 (4th Cir. 2000)
8. **OPINION THAT MORTGAGE WAS VALID WAS WRONG**
Law firm was sued for malpractice by trustee for bondholders because a legal opinion letter opining on the validity and priority of a preferred fleet mortgage on casino vessels was found by the bankruptcy judge to be erroneous. The opinion stated that the fleet mortgage constituted a legal, valid, binding and enforceable obligation superior to all other liens. The judge found the mortgage to be invalid and unenforceable. The malpractice case was dismissed on jurisdictional grounds that did not touch upon the merits. *First Trust National Association, as Indemnitee Trustee v. Jones, Walker, Waechter, Poitevent, Carrere & Denegree et al.*, 996 F. Supp. 585 (S.D. Miss., 1998)
9. **TO BE PREFERRED SHIP MORTGAGE REQUIRES STRICT COMPLIANCE WITH STATUTE**
The ship mortgage is made preferred only upon compliance with all the conditions specified in the statute. "Obviously the statute taken literally may work harshly..." Justice Holmes then stated, "We see no room for construction, and there is nothing for the courts to do but to bow their heads and comply." *Morse Dry Dock & Repair Co. v. The Northern Star et al.*, 271 U.S. 552, 46 S.Ct. 589 (1926); *The Prudential Insurance Company of America v. S.S. American Lancer et al.*, 870 F.2d 867, 1989 A.M.C. 1097 (2nd Cir. 1989)

VII. Cost of Defense and Prosecution:

1. **INABILITY OF MORTGAGEE TO COLLECT ATTORNEY FEES**
The court refused to award attorney fees as part of an *in rem* claim against a vessel even though the written agreement that was the basis for the claim provided for the awarding of attorney fees. **(In title disputes, the First American vessel title policy provides for costs of defense and prosecution.)** *Bradford Marine, Inc. v. M/V Sea Falcon*, 64 F.3d 585 (11th Cir. 1995)

2. **COST OF DEFENSE/PROSECUTION ATTORNEY FEES DISALLOWED**

The court would not award attorney fees to preferred ship mortgagee in a dispute in which the mortgagee prevailed against a third party seeking priority over the mortgagee. The award of attorney fees in this type of litigation is discretionary by the court and infrequently granted. **(First American, under its vessel insurance policy, is responsible for costs of defense and prosecution.)** *Banchory Shipping v. Banco Wiese Limitado*, 160 F.3d 170 (4th Cir. 1998)

VIII. When is a Vessel a "Vessel":

1. **WHEN DOES A VESSEL BECOME A "VESSEL"**

Deepwater pipe-laying barge built in Korea was sailed under its own power to the U.S. Gulf Coast to install J-Lay Tower (which was essential to its use as a pipe-laying barge), but court found that it was not yet an existing vessel and thus no maritime liens (including preferred ship mortgage) would attach. *Hyundai Heavy Industries v. M/V Saibos*, 163 F.Supp.2d 1307 (ND Ala., 2001)

2. **A HOUSEBOAT IS A "VESSEL" AND SHOULD BE TREATED ACCORDINGLY**

The court found that a houseboat is a boat. "That she has no motive power and must, as would the most lowly of dumb barges, be towed, does not deprive her of the status of a vessel." Thus, she is subject to maritime liens and a mortgagee should utilize a preferred ship mortgage, which is the best protection for a lender when lending money on a vessel. *Miami River Boat Yard, Inc. v. 60' Houseboat, Serial No. SC-40-2860-3-62*, 390 F.2d 596 (C.A. Fla., 1968)

3. **WHEN DOES A VESSEL BECOME A "VESSEL"**

A casino engaged a shipyard to build a casino vessel. After engines were installed in the vessel and it was near completion, it was removed from the shipyard and sailed up the Mississippi River on its own power, but with assist tugs, to a yard where the finishing touches were to be performed. The original shipyard went into bankruptcy and the unpaid contractors and workmen in that yard alleged they had maritime liens for their claims that attached to the vessel and could be enforced *in rem*. The contractors in the up river facility alleged that the vessel was not yet a vessel at the time it left the original yard and those claims could not be the subject of a maritime lien, and an *in rem* proceeding was invalid; therefore priority favored their state liens. The matter was the subject of mediation and ultimately the claims were settled with both sides significantly compromising.

4. **CERTIFICATE OF DOCUMENTATION IS NOT DETERMINATIVE OF BEING A "VESSEL"**

Issuance of a U.S. Coast Guard Certificate of Documentation is not determinative of whether subject of the Certificate of Documentation constitutes a "vessel" as defined by 1 U.S.C. §3. The documentation process is not intended to be, nor is it, conclusive as to the issue of what constitutes a "vessel" for purposes of federal admiralty and maritime matters and the Ship Mortgage Act. *Daniel v. Ergon, Inc.*, 892 F.2d 403 (5th Cir. 1990); *In re Biloxi Casino Belle Incorporated*, 176 B.R. 427 (USBC SD Miss, 1995)

5. **WHEN IS A VESSEL A "VESSEL"**

When deciding Jones Act status for a seaman, court found that floating production platform was not a vessel. *Fields v. Pool Company*, 182 F.3d 353 (5th Cir. 1999)

6. **WHEN IS A VESSEL A "VESSEL"**

The court found that based on the facts in this case, the casino and other vessels in this case were vessels for purposes of seeking to foreclose *in rem* on preferred ship mortgages on the vessels. *Credit Suisse First Boston Mortgage Capital LLC v. Doris, Official No. 566240 et al.*, consolidated with *Credit Suisse First Boston Mortgage Capital LLC v. Bayou Caddy's Jubilee Casino et al.*, 120 F.Supp.2d 709 (N.D..Miss, 2000)

7. **“VESSEL” MUST BE INTENDED TO BE USED AS A MEANS OF TRANSPORTATION ON WATER**

The U.S. Coast Guard issued Certificates of Documentation on two casinos constructed on barges. Following bankruptcy, the preference of the preferred ship mortgages on the casinos was attacked. The court held that a first preferred ship mortgage granted pursuant to the Ship Mortgage Act may only be perfected on a "vessel," as defined by 1 U.S.C. § 3. The bankruptcy court found that “the casinos were not designed or intended nor were they realistically capable of being used as a means of transportation on water in the business of maritime commerce and thus did not constitute “vessels” for purposes of federal admiralty and maritime matters and the Ship Mortgage Act” and, thus, the mortgagee did not possess a first preferred ship/fleet mortgage. *In re Biloxi Casino Belle, Inc.*, 176 B.R. 427 (U. S. B. C. Miss, 1995)

8. **TRUCK MOUNTED RIG ON A BARGE IS A “VESSEL”**

Plaintiff was injured on a workover rig that consisted of a portable truck-mounted rig driven onto the deck of a leased barge and bolted into place. It had been bolted to the barge for two years. The barge transported the rig from well head to well head over navigable waters to service wells located in navigable waters. The court concluded that the rig was a vessel as a matter of law. Thus, presumably, it is subject to maritime liens.

9. **CASINO WAS CONSIDERED A “VESSEL” WHILE BEING TOWED**

Casino was towed from the shipyard to a place where it was to be permanently moored. The casino owner failed to pay for towage and the tug owner, pursuant to an alleged maritime lien for towage, sought to assert an *in rem* claim against the vessel. The debtor claimed that a floating casino had been found to not be a vessel for purposes of federal admiralty and maritime matters. The court ruled in favor of the tug owner and held that, though it was a floating casino, and in other cases a floating casino was found not to be a “vessel,” while the casino was being towed, it was a "vessel," such as could be made subject to maritime liens. *In re Amgam Associates*, 239 B.R. 737 (USBC S.D. Miss 1999)

IX. The "Gap":

1. **LIENS ARISING DURING THE “GAP” PERIOD**

The bank entered into a preferred ship mortgage with its customer and the mortgage was timely filed and recorded. When an abstract of title was received immediately after the closing of the mortgage, it was discovered that a notice of claim of a maritime lien had been filed against the vessel two days before the closing and, thus, was undetectable from the public record at the time of closing. Title insurance would cover this gap period.

2. **EXPOSURE DURING THE “GAP” PERIOD**

Preferred mortgage outranked by documents recorded by another during the gap period between the date of an abstract and the recordation of the mortgage.

3. **DID NOT PERMIT PERFECTION OF MORTGAGE BACK TO DATE MORTGAGE FIRST DELIVERED TO COAST GUARD**

Section of Ship Mortgage Act, providing that mortgage is perfected only when endorsed and recorded by U.S. Coast Guard, did not allow for perfection relating back to date mortgage was first delivered to Coast Guard for endorsement and recording; accordingly, where owner of vessel had filed for bankruptcy in interim, Bankruptcy Code did not permit post-petition perfection of mortgage. *Matter of Alberto*, 66 B.R. 132 (D.N.J. 1985)