Lessons of O.W. Bunker

Interpleader – Enjoining in Rem Proceedings
Good or Bad Idea?

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Lessons of OW Bunker (Again)

Interpleader – Enjoining in Rem Proceedings

Is an Interpleader action a good idea or a bad idea? Depends on which side of the fence you are on!

Introduction

OW Bunker was never supposed to collapse, just like all the other major shipping and bunker companies around the world; it was too big, too powerful, too smart. But it did, and unfortunately left a lot of people holding the bag. But to whom did the (money in the) bag belong?

We had the usual cast of characters, the usual suspects: shipowners and charterers (vessel interests), bunker suppliers, middlemen and physical suppliers. So when OW Bunker filed for Chapter 11 bankruptcy protection in the District of Connecticut, those who were supposed to pay for bunkers previously supplied, but were not sure who to pay, filed interpleader actions in the Southern District of New York.[1]

Physical suppliers – who never get respect – wanted to be paid by OW as the actual bunker supplier. OW, as the direct supplier in contract with vessel interests wanted to be paid, and the bank ING (to whom OW had assigned their maritime lien rights) also wanted to be paid.

On the other hand, vessel interests had received, consumed and not paid for the bunkers, and so their vessels were at risk of *in rem* arrest for a maritime lien for "necessaries" under US maritime law. So while everyone was lining up as a creditor in the bankruptcy, they decided to pay (interplead) the money into court to avoid being at risk to pay more than once for the same bunkers. This left the competing interests to fight over the funds. Nice and easy, and they could walk or sail away.

These interpleader actions filed in the SDNY (over 25-cases) have kept New York lawyers quite busy addressing novel bankruptcy, maritime and interpleader issues.

Interpleader Analysis

1. **Purpose**

The use of an interpleader action [Rule 22 of Federal Rules of Civil Procedure] by vessel interests was to enjoin "completing claimants" from commencing actions *anywhere* against the vessel; in other words, the strategy was to "enjoin" (prohibit someone from performing a particular action by issuing an injunction) all *in rem* proceedings.

However, this move was predictably met with resistance from parties within the supply chain.

2. **Supply Chain**

A typical transaction before OW collapsed involved a contract between vessel interest, an OW entity, a chain of subcontracts with local OW entities, and ultimately a physical supplier:

First, vessel interests would contract with an OW entity for supply of bunkers. Second, that particular OW entity would procure the bunkers by subcontract with another entity (often, another OW entity operating locally to the place of supply). Third, the local OW entity would contract with a physical supplier (either another OW entity or an independent supplier) to physically provide the bunkers to the vessel.

When OW collapsed, many suppliers in the chain were left holding the bag, each standing varying degrees of contractual separation from the vessel and vessel interest. The litigation that followed has focused on the rights of bunkers suppliers at the extremes: the **direct supplier** who contracted with the vessel interests and the **physical supplier** who contracted with an intermediary.

[1] Along with the interpleader actions, they also filed anti-suit injunctions to prevent various filed *in rem* arrests from going forward on the US West Coast.

3. Interpleader Jurisdiction

Vessel interests received competing claims for payment by various suppliers, direct and physical (as well as the bank by assignment), and clearly did not want to pay more than once for the same bunkers. As a tactical move, they relied on 28 USC §1335 (Interpleader Statute) or FRCP 22 (Interpleader Rule), to protect themselves from facing multiple claims.

An interpleader action allows a plaintiff to deposit funds into the court registry and let defendants fight over who is entitled to the proceeds. The funds become the *res*. Also, under 28 USC §2361, a court can enjoin competing claimants from filing claims relating to the same interpleader case in any other forum.

Of course, suppliers questioned whether the court (1) had subject matter jurisdiction, and (2) could issue a restraining order, essentially arguing vessel interests could not satisfy the Interpleader Statute's requirements because suppliers *in rem* maritime lien claims were separate and distinct from other competing claimants' *in personam* contract claims.

These novel bankruptcy, maritime and interpleader issues, never been decided by a US court, came into focus in the 2nd Circuit case of *Hapag-Lloyd v. U.S. Oil Trading* (Feb 24th 2016 & May 6th 2016):

The 2nd Circuit acknowledged that the competing claims by suppliers had different legal origins, but found it immaterial to an interpleader action. For a supplier to prove its *in rem* lien claim under CIMLA,[2] the Court stated the supplier would have to show the bunkers were provided "on the order of the owner or a person authorized by the owner," which in turn required an analysis of the contractual relationships of other competing claimants' *in personam* contract claims.

It held that the competing claims, however, were "inextricably intertwined;" and based on the broad and remedial nature of 28 USC §1335, the Court had interpleader jurisdiction.

Further, the 2nd Circuit questioned the geographic scope of the District Court's restraining order and remanded the case back to the District Court for reconsideration, with instructions to enter an order that eliminated or retained the foreign scope of the injunction under *China Trade & Dev. Corp. v, m/v Choong Yong* (2nd Cir. 1987). Shortly thereafter, following defendant's decision not to challenge the scope of the injunction, the 2nd Circuit confirm that the foreign scope of the injunction was appropriate. [3]

Bunker Supplier Rulings

1. Direct Suppliers

The direct supplier has traditionally been in the best legal position to establish an enforceable maritime lien due to being in "privity of contact" with vessel interests. But there has been some dispute on this issue within the SDNY, where Judge Valerie E. Caproni is presiding over multiple OW interpleader cases:

In Jan 2017, Judge Caproni issued an Order in 4-test cases, decided on a full evidentiary record (summary judgment motions), confirming OW **does have** an enforceable maritime lien (under element 3, direct supplier accepted order for bunkers directly from vessel interests; elements 1 & 2 do not require direct supplier itself to deliver bunkers to a vessel). Therefore, the bank (ING) as OW assignee could enforce those liens. *O'Rourke Marine Services, L.P., L.L.P. v. M/V COSCO HAIFA* (Apr 8th 2016).

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[2] Under the Commercial Instruments and Maritime Lien Act (CIMLA), a bunker supplier has a maritime lien enforceable in a civil action *in rem* if it (1) furnished necessaries/bunkers, (2) to the vessel, (3) "on the order of the owner or a person authorized by the owner." 46 USC 31342.

[3] The Court stated that if the foreign scope of the injunction were eliminated, "defendants with maritime lien claims could race to arrest vessels overseas" and extract payment, potentially resulting in "inconsistent judgments" and exposing them to "double or triple liability for a single obligation."

District courts in Alabama and Texas agree OW has an enforceable maritime lien. Barcliff, LLC v. MV DEEP BLUE (SD Ala. Sept 28th 2016); *NuStar Energy Services, Inc. v. COSCO AUCKLAND* (SD TX, Dec 1st 2016).

In the meantime, Judge Katherine Forrest, newly assigned in the SDNY, vacated *O'Rourke* in part as to OW's maritime lien. (Aug 24th 2016). She issued another ruling adding a requirement of "risk of financial loss," concluding OW did not have maritime lien because it was not exposed to real risk and did not "provide" bunkers to the vessel. *ING Bank N.V. v. TEMARA* (SDNY, Oct 21st 2016.)

Then in Jan 2017, presiding Judge Caproni held that necessaries can be provided to a vessel indirectly, that OW had exposed itself to "real risk of financial loss," since physical providers might not deliver the bunkers and the vessel might not pay. She concluded OW *did* provide bunkers to the vessels and had maritime liens. See e.g. *Nippon Kaisha Line Ltd. v. O.W. Bunker USA, Inc.* (Jan 9th 2017).

Judges singing off different sheet music?

2. Physical Suppliers Searching in Vain

Physical suppliers often had no direct contract with vessel interests or the initial OW contracting party, and their remoteness to the initial transaction complicated efforts to recover bunker costs.

So far, physical suppliers have been unable to establish the 3rd element for a maritime lien (that bunker supply to vessel was "on the order of the owner or person authorized by the owner"). Courts have held:

- *Knowledge does not equal direction*: a vessel's knowledge that a physical supplier would provide bunkers did not establish the supply was on "order of the owner or person authorized by the owner." *Valero Marketing & Supply Co. v. M/V ALMI SUN,* 2016 WL 475905 (E.D. La., Feb 8th 2016)
- *No agency*: no evidence so show direct supplier or intermediary acted as vessel's actual or apparent agent in selecting the physical supplier. *O'Rourke Marine Services, L.P., L.L.P. v. M/V COSCO HAIFA* (SDNY, Apr 8th 2016)
- *No Ratification by Signature*: signing bunker certificate and vessel's acceptance of bunkers did not mean ratification of maritime lien in favor of a physical supplier, and maritime liens cannot be created by contract. *Valero Marketing and Supply Co. v. M/V ALMI SUN,* 2016 WL 475905 (E.D. La., Feb 8th 2016); *O'Rourke Marine Services, L.P., L.L.P. v. M/V COSCO HAIFA* (SDNY, Apr 8th 2016).

Other districts have also rejected a physical supplier's maritime lien claim on the same grounds. See *Bunker Holdings* (WD Wa. Jun 6th 2016); *ING Bank N.V. v. M/V Clipper Iyo* (SD Tx, Dec. 29th 2016); *Barcliff*, LLC v. MV DEEP BLUE (SD Ala. Sept 28th 2016).

3. What can Physicals Do?

First, keep trying: some district courts may not follow other court rulings + appeals are pending in some cases. Second, depending on its bargaining position, a physical supplier may be able to require express (a) contract approval of the bunker supply by vessel interests prior to delivery, and (b) disclaimer of any no-lien clause. Third, contract with the direct supplier that (a) the physical retains title to supplied bunkers, and (b) the direct supplier assign its maritime lien until the physical has been paid for the bunkers.

Interpleader is Definitely Bad for Suppliers

So why is an interpleader action a bad idea?

1. It messes with traditional maritime law because its intent is to stop bunker suppliers from enforcing a long valued *in rem* maritime lien against a vessel for bunker supply (after all, a ship is highly mobile, here today and in Timbuctoo tomorrow, or modern day Port Royal or Tortuga, where pirates rule); it therefore takes away a supplier's *in rem* arrest as a weapon-of-choice against recalcitrant payers.

2. It fails to adequately take into account difference between an *in rem* procedure, and an *in personam* action, i.e. *in rem* claims for maritime lien against a vessel are distinct/separate from suppliers with *in*

personam claims for breach of contract (but 2nd Circuit held in *Hapag-Lloyd* that even though *in rem* and *in personam* claims have a different legal basis, it was immaterial as they are "inextricably intertwined.").

Question:

> **First**, would it be possible for a court to "carve out" *in rem* rights in an interpleader action to the extent a direct supplier (such as OW/the bank) is entitled only to its "margin" or "delta" in the bunker transaction, leaving other parties in the supply chain to pursue any lien claims for the balance?
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> **Second**, would it be possible, based on specific facts, for a bunker supplier to enforce its *in rem* lien against a vessel, whereby the court analyzes the contractual relationship (and possibly makes a factual ruling in that regard) in a way that does not "negatively affect" any contractual *in personam* claim? If it could do so, then why would any "intertwining" negate or void *in rem* rights?

3. It forces a bunker supplier to subject itself to a US court's jurisdiction just to file its claim to the funds (the funds now representing the *in rem* property).

4. The interpleader statute grants the right to recover attorney's fees, which forces a supplier to incur vessel interest fees if it opposes the interpleader action and loses, whereas this exposure is usually not on a supplier's radar (assuming of course it has sufficient legal basis to avoid a wrongful *in rem* arrest claim).

Question:

Since the SDNY cases involve mainly US physical suppliers and bunker supply within the US, would there be a different result in an interpleader action involving a foreign supplier and a foreign stem? What if the foreign supplier did not consent to personal jurisdiction (US court may have no power to enjoin foreign enforcement proceedings)?