

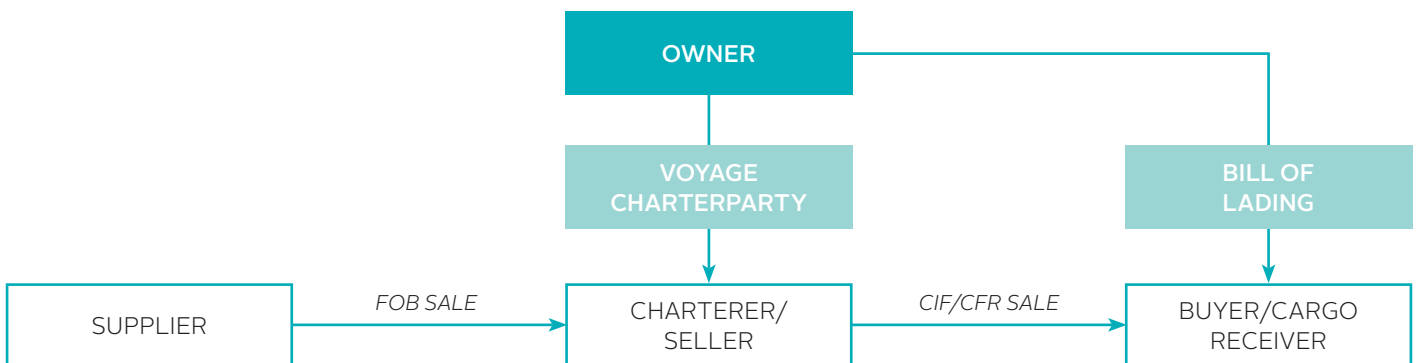
## SHIPPING

### OWNERS' LIENS ON CARGO FOR UNPAID FREIGHT IN CHINA

A shipowner client comes to us with a problem. The charterer has defaulted on freight payments and/or will not pay freight due and payable under the Charterparty. The charterer has also gone incommunicado.

The vessel is en route to discharge its cargo in China. The Bill of Lading is held by the buyer/cargo receiver to whom the charterer had sold the cargo. The shipowner wants to know whether he can exercise a lien on the cargo against the lawful holder of the Bill of Lading, until he has been paid the freight due to him from the charterer.

The following diagram sets out the basic framework:



Ince & Co opened its Beijing office in late 2012, and since then we have continued to encounter this type of dispute with increasing frequency. This article sets out some basic guidance and tips for the shipowner who finds himself in a similar scenario<sup>1</sup>.

#### The charterparty must contain a lien clause

The first question the shipowner should ask himself is whether the charterparty contains a lien clause. Many charters give the shipowner an express contractual lien on cargo in respect of unpaid freight. A typical lien clause wording might look something like this:

*"Owners shall have a lien on the cargo for freight incurred at the port of loading to the extent of amount due to Owners."*

The shipowner should be careful to consider the scope of the lien clause. If a lien clause refers only to a lien for unpaid demurrage, for example, it would not entitle the shipowner to exercise a lien in respect of unpaid freight.

#### The lien clause must be validly incorporated into the Bill of Lading

The receiver will come into a contractual relationship with the shipowner via the Bill of Lading. For the lien to be effective

against the receiver the shipowner will also have to prove that the Bill of Lading contract is also subject to the lien clause, and gives the shipowner the same rights as he has under the lien clause in the charterparty.

This is satisfied if the Bill of Lading expressly incorporates the terms and conditions of the charterparty. Under English law, the shipowner must prove that the wording of the incorporation provision in the Bill of Lading is sufficiently clear to incorporate the charter lien clause into the Bill of Lading. Although general words may suffice, to best protect himself the shipowner should try to ensure that the Bill of Lading makes express reference to the lien clause in the charterparty. Typical wording might look something like this:

*"This shipment is carried under and pursuant to the terms of the Charterparty dated XXX, and all the terms whatsoever of the said charter, including the lien under clause XX on freight, are hereby incorporated and shall apply to and govern the rights of the parties concerned in this shipment."*

There are additional requirements in China, where the Bill of Lading must state "freight payable as per charterparty" and must identify the charterparty in question expressly by having the date of the charterparty annotated on the Bill of Lading.

<sup>1</sup> This is not intended to be legal advice on Chinese law. We are not qualified to advise on Chinese law. The views expressed are simply our understanding of Chinese law based on our experience.

The requirements may also depend on the particular local maritime court. Some maritime courts in China even require that the relevant lien clause in the charterparty be expressly identified.

**TIP:** To protect himself, the shipowner should make sure that the Bill of Lading states the date of the relevant charterparty whose clauses are sought to be incorporated into the Bill of Lading.

### The lien must be recognised by the local courts in China

Even if the charterparty and the Bill of Lading provide the shipowner with a specific contractual lien over the cargo which would be enforceable under English law, and even though the charterparty may be subject to English law and arbitration, the lien may not be exercisable in China.

The shipowner must look to the law of the jurisdiction in which the lien is sought to be exercised (for present purposes, China) to see whether Chinese law also recognises a right to a lien, and whether the shipowner can fulfil the requirements in order to exercise the lien under Chinese law.

Article 87 of the Chinese Maritime Code provides that the shipowner is entitled to a lien over the cargo of the debtor for freight and other amounts outstanding, but this right is subject to a number of limitations. We briefly highlight below what we understand to be the prevailing Chinese maritime courts' practice.

First, the shipowner must ask the charterer to provide security before exercising the lien. The shipowner can only exercise a lien if no security has been voluntarily provided by the charterer.

Secondly, the shipowner can only lawfully exercise a lien over the freight if the cargo is owned by the party who is liable to pay the overdue freight, i.e. the charterer. In other words, at the time the shipowner seeks to exercise the lien, the charterer (defaulting party) must also be the owner of the cargo upon which the lien is to be exercised.

This will give rise to a difficulty to the shipowner where the charterer is no longer the owner of the relevant cargo and is no longer the holder of the Bill of Lading. In that case, the shipowner is not able to lawfully exercise a lien over the freight under Chinese law.

In such event, upon the application of the holder of the Bill of Lading, the local court would issue an order to release the cargo. In our experience, these court orders can be obtained and enforced quite quickly.

### What can the Shipowner do?

Even if the shipowner believes he stands in a position to lawfully exercise a lien on the cargo, he cannot rule out the possibility that the cargo receiver (or any other party who claims to be the owner of the cargo) will apply to the court for an order to release the cargo.

The shipowner finds himself stuck between a rock and a hard place. He is unable to obtain payment for the freight from the charterer. Neither is he able to avail of the protection he would like to rely on, since he cannot validly exercise the lien in China.

Some shipowners choose to try and force the charterer's hand by refusing to proceed to the discharge port or by doing so but refusing to discharge the cargo, in the hope that this will force the charterer to pay freight.

By doing so, the shipowner may be in breach of his obligation to proceed to the discharge port with due despatch, and be exposed to liability to the holder of the Bill of Lading for interference with the Bill of Lading holder's right to the cargo.

Further, this is a commercially unrealistic solution (how long will the shipowner be prepared to wait?), and in circumstances where the charterer is in genuine financial difficulty it is unlikely to have the desired impact.

Shipowners would do well to bear in mind the wise old saying that "*prevention is better than cure*". The shipowner's best hope is to avoid this unfortunate situation by paying careful consideration to choosing commercial partners. Shipowners must be careful to conduct the appropriate financial due diligence on counterparties, especially when embarking on new commercial relationships with charterers who do not have an established reputation in the market.

Every situation is unique and depends on the precise facts, so shipowners are encouraged to seek legal advice if they have any doubts about the legal position.



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