

## **Chilean courts start accepting Letter of Undertaking as sufficient guarantee in case of vessel arrest.**

### **Introduction**

In Chile there are no specific regulations regarding the nature of the securities that may be requested by claimants in case of a vessel arrest. For long time P&I clubs letters of undertaking (“LOUs”) were accepted only if agreed by the arrest petitioner mainly due to the fact that Chilean courts were not used to them.

Having said this, in a recent arrest following a pollution case occurred in Quintero Bay, the court hearing the arrest accepted a LOU with no prior approval from the arrest petitioner.

### **Legal framework**

The International Convention Relating to the Arrest of Sea-Going Ships (Brussels, 10 May 1952) has not been ratified by Chile, although its principles were taken into account by Chilean domestic law.

The fundamental regulations applicable to ship arrest are found in Paragraph 5 of Title VIII of Book III of the Chilean Code of Commerce (the “Code of Commerce”) denominated "*About the Procedure to Arrest Vessels and its Release*" (articles 1,231 *et seq.*) as well as in the common rules contained in Title IV and Title V of Book II of the Code of Civil Procedure, respectively denominated "*About the Pre-Judicial Measures*" (articles 280 *et seq.*) and "*About the Precautionary Measures*" (articles 290 *et seq.*), which are subsidiary to those of the Code of Commerce. The arrest regulated under the Code of Commerce is triggered in case that the arrest petitioner has one or more “maritime privileges”, which are listed in the Code of Commerce under articles 844 to 846.

With respect to the regulations applicable to the judicial sale of vessels, they are found, on the one hand, at Paragraph 2 of Title II of Book III of the Code of Commerce, denominated '*About the Naval Property*' (Articles 831 *et seq.*) in conjunction with the common law rules contained in Paragraph 2 Title I of Book III of the CCP, denominated '*About the Administration of Arrested or Attached Goods and the Foreclosure Procedure*' (Articles 479 *et seq.*), and the regulations contained in Title XVIII of Book III of the same Code, denominated '*About the Action of Dispossession Against Third Parties who Possess a Mortgage Property*' (Articles 758 *et seq.*).

In connection to maritime disputes, Article 1203 of the Code of Commerce establishes the general principle that in Chile the resolution of any maritime dispute, including those related to marine insurance, is subject to mandatory arbitration.<sup>1</sup>

#### **TYPES OF CLAIM FOR WHICH ARREST OR ATTACHMENT CAN BE REQUESTED**

Under Chilean law a vessel may be arrested if the requesting party has a credit that entitles it to do so. These credits may be of two types, namely:

- (a) *Privileged credits* as set forth by Articles 844, 845 and 846 of the Chilean Code of Commerce; and
- (b) Credits other than those mentioned in (a) above.

Under Chilean practice it is unusual to petition an arrest which is not based on a *privileged credit* maritime, as it faces more technical problems than an arrest based on the special system established by the

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<sup>1</sup> One of the relevant exceptions to this rule is cases that are related to oil pollution regulated by the Chilean Navigation law, which are heard in first instance by a minister of the court of appeal of the place where the facts occur.

Code of Commerce. Accordingly, we will focus this presentation on the last one.

Under Chilean law there is no statutory definition for *privileged credits*. However, they may be defined as those which give rise to a maritime lien and allow the request of an arrest as per the special rules set forth by Paragraph 5 of Title VIII of Book III of the Code of Commerce, denominated '*About the Procedure to Arrest Vessels and Its Release*' (Articles 1231 *et seq.*). Articles 844, 845 and 846 of the Code of Commerce establish and distinguish the following groups of *privileged credits*:

A. Credits of Article 844:

- 1° Legal costs and other disbursements caused by reason of a suit, in the common interest of the creditors, for the preservation of the vessel or for its forced alienation and distribution of the yield;
- 2° The remuneration and other benefits arising from the contracts of embarkation of the vessel's crew, in accordance with labour regulations and civil law which regulate the concurrence of these credits, together with the emoluments paid to the pilots at the service of the vessel. This privilege applies to the indemnities which are due for death or bodily injuries of the servants who survive ashore, on board or in the water, and always provided that they stem from accidents related directly to the trading of the vessel;
- 3° The charges and rates of ports, channels and navigable waters, together with fiscal charges in respect of signaling and pilotage;
- 4° The expenses and remunerations due in respect of assistance rendered at sea and general average contribution. This privilege applies to the reimbursement of expenses and sacrifices incurred by the authority or third parties, in order to prevent or minimize pollution damages or hydrocarbon spills or other substances contaminating the environment or third party property, when the

fund of limitation of liability has not been constituted as established in Title IX of the Chilean Law of Navigation; and

5° The indemnities for damage or losses caused to other vessels, to port works, piers or navigable waters or to cargo or luggage, as a consequence of the collision or other accidents during navigation, when the respective action is not susceptible to be founded upon a contract, and the damages in respect of bodily injury to the passengers and crew of these other vessels.

B. Credits of Article 845:

Mortgage credits on large vessels (i.e., vessels over 50 gross tons) and secured credits on minor vessels (i.e., vessels up to 50 gross tons).

C. Credits of Article 846:

1° Credits in respect of the sale price, construction, repair and equipping of the vessel;

2° Credits in respect of supply of products or materials, which are indispensable for the trading or conservation of the vessel;

3° Credits arising from contracts for passage money, affreightment or carriage of goods, including the indemnities for damage, lack and short deliveries of cargo and luggage, and the credits deriving from damage in respect of contamination or the spilling of hydrocarbons or other contaminating substances;

4° Credits in respect of disbursements incurred by the Master, agents or third parties, for account of the owner, for the purpose of trading the vessel, including agency service, and

5° Credits in respect of insurance premiums concerning the vessel, be they hull, machinery or third-party liability.

The *privileged credits* of Article 844 enjoy privilege over the vessel in the order enumerated in 'A' above with preference over mortgage credits and the *privileged credits* of Article 846. Mortgage credits are

preferred to those of Article 846, which in turn follow the rank indicated in 'B' above.

In this respect, it is noteworthy that the *privileged credits* established by the above-mentioned provisions have preference and exclude all other general or specific privileges regulated by other legal bodies, when referring to the same goods and rights. However, the rules regarding priorities and privileges in matters of pollution or for avoiding damage from spills of hazardous substances, which are established in international treaties in force in Chile and in the Navigation Law, have preference over the provisions of Title III of Book III of the Code Commerce (*'About Privileges and of Naval Mortgage'*) in the specific matters to which they refer.

#### **OTHER SPECIFIC PRECONDITIONS TO ARREST OR ATTACHMENT**

The arrest is subject to the following preconditions:

- (a) The arresting party must invoke one or more of the *privileged credits* enumerated in Section 5 above. In this respect it is noteworthy that, except for the regulations related to pollution or for avoiding damage from spills of hazardous substances, the maritime privileges preclude any other general or special privilege regulated by other laws in connection with the same goods. The maritime privileges also confer upon the creditor the right to pursue the vessel in whomsoever's possession she may be.
- (b) The arresting party must attach antecedents that constitute presumption of the right being claimed.
- (c) If the court estimates that the antecedents attached are not sufficient (court's discretionary faculty) or the petitioner states they are not yet available to him, the court may require that counter security be provided for the eventual damage that may be caused if, subsequently, it is found that the petition lacked basis.

## **SISTER SHIPS**

The lien on the ship granted by a *privileged credit* can be exercised not only against the actual ship to which the *privileged credit* relates but also on a ship in the same ownership or a ship in the same administration or operated by the same person.

## **FORM OF APPLICATION**

Arrest of a vessel is commenced by filing an arrest petition at any of the competent courts as per Section 3 above. The complaint which initiates the proceedings must comply with the following requirements:

- (1) Compliance with all formal requirements related to the presentation of a suit as per Chilean general procedural regulations, which implies (i) to specify the court; (ii) to identify the claimant, his representatives and the nature of such representation; (iii) to state the facts surrounding the case and the applicable laws, and (iv) to make precise and clear petitions for the court's decision.
- (2) In the case of an arrest based on *privileged credits*, when the arrest is requested as a *preliminary precautionary measure*, the petitioner must indicate the substantive action he intends to file later on and briefly state his grounds for such an action. If the action does not concern the holding or possession of the vessel but rather the collection of some pecuniary service, the petitioner must indicate the amount and form of guarantee he considers sufficient to secure the outcome of the action. If the petition is filed simultaneously with, or during the course of, the substantive suit, the petitioner must indicate in such a petition his claim in respect of the amount of the guarantee and the manner of its constitution.
- (3) As pointed out in Section 6.1 above, in the case of an arrest based on *privileged credits*, the arresting party must attach antecedents that constitute presumption of the right being claimed and eventually of counter-security.

## **REPRESENTATION BY COUNSEL AND POWER OF ATTORNEY**

Under Chilean law the general rule is that either individuals or corporations are required to be represented by counsel. Depending on the circumstances, a power of attorney is not necessarily required but security may be requested.

### **BAIL OR SECURITY BY DEFENDANT**

As regards security for lifting the arrest, the amount of security is usually established by the court based on the petition of the arresting party. Such amount cannot exceed the value of the arrested vessel and can be reviewed subsequently through incidental proceedings.

Regarding the form of security, there are no specific rules and it will depend on the court's resolution, but the guarantee usually requested and granted is a bank guarantee issued at the order of the court. As soon as the requested guarantee is provided, the court shall lift the vessel arrest without delay.

For a long time, protection and indemnity insurance (P&I) club letters of undertaking were accepted only if agreed by the arrest petitioner, mainly due to the fact that the Chilean courts were not accustomed to them. However, in a recent arrest following a pollution case, the court hearing the arrest accepted a letter of undertaking with no prior approval from the arrest petitioner. This is a positive development, as Chilean courts seem to finally be aligned with international practice, whereby a letter of undertaking is accepted by the courts as sufficient security.

### **COURT HEARINGS AND PROCEEDINGS SUBSEQUENT TO ARREST**

In the case of an arrest based on a *privileged credit* and provided that the conditions mentioned in section 6.1 above are met, the court must grant the petition without any formality. In doing so, the court must analyze quickly the antecedents submitted, granting the petition without hearings or service of the arrest order on the affected party. The court's

analysis for granting an arrest usually takes from a few hours up to one day. However, if the arrest is petitioned with a credit other than a privileged one and under the general rules of the CCP, which is seldom, the corresponding grant may take several days due to several procedural technicalities that are necessary to follow. These obstacles are not found under the special arrest system set forth by the CODE OF COMMERCE for *privileged credits* and thus in practice this is the system normally followed and used.

Having said that, in the case of an arrest based on *privileged credits*, the person who establishes the guarantee or is affected by it may at any time request, for good reasons, that the guarantee be modified, reduced or lifted. The procedures for lifting the arrest do not impair the right of the petitioner to later allege or enter the motions or defenses he sees fit. They are also not considered a waiver of the right to limit responsibility according to the provisions of Article 889 *et seq.* of the Code of Commerce. The motion objecting to a retention or arrest, as well as the motion objecting to the amount or form of the guarantee, are considered incidental motions which do not suspend the effects of the contested resolution. The request for modification, reduction or lifting of a guarantee substituting for an arrest shall also be treated as incidental. In this respect it is noteworthy that the general rules on preliminary and precautionary measures set forth by Titles IV and V of Book II of the CCP apply in respect of anything not provided for by the special regulations related to arrest based on *privileged credits* or in the absence of agreement by the parties. It must be noted that these special provisions do not exclude the exercise of other precautionary measures in common law that may be available to a creditor to secure the outcome of his action or in cases which do not deal with a credit that enjoys privilege over a vessel.

## **COSTS AND ADVANCES FOR COURT PROCEEDINGS AND CUSTODY**

Except for the costs related to the fees of the service processor who informs the Maritime Authority of the arrest and performs service of process on the person against whom the arrest is requested, as per



Section 18 below, there are no court fees to be paid. In cases where it is anticipated that the vessel will remain under seizure for a substantial period of time, it may be necessary to request the court to appoint a depositary, which may imply additional costs.

### **ENFORCEMENT OF ORDER OF ARREST**

The arrest or retention of a vessel is carried out by service on the maritime authority in the place where the vessel is, or by official letter to or notification of the Director General of the Maritime Territory and the Merchant Marine, should the vessel not be within the jurisdiction of the court that decreed such a measure. Previous service on the person against whom the measure is requested is not necessary.

In urgent cases, the court may communicate the arrest via telegram, telex or other reliable means. In the case of a preliminary proceeding, the person against whom the arrest is requested must also be notified within a period of 10 days counted from the resolution that granted such a measure. This period may be extended by the court for good reason. The lack of service within the aforesaid period or the last of its extensions shall cause the automatic forfeiture of the decreed arrest, which is communicated by the court directly to the maritime authority.

### **CLAIMS FOR DAMAGES BY THE OWNER OF AN ARRESTED VESSEL**

First, it is noteworthy that when an arrest has been decreed as a *prejudicial precautionary* measure, the petitioner is obliged to file his complaint requesting that the decreed arrest remain in force within a time period which, in principle, is 10 days, but which may be extended for up to a total of 30 days, provided there is a sound basis to do so. The non-fulfillment of this obligation means the cancellation of the arrest and liability for the damages which may have been caused, on the irrefutable presumption that the proceedings for the arrest were fraudulent. This applies both to an arrest based on *privileged credits* as well as other credits.

In addition, if the arrest was wrongful, fraudulent or lacked a legal basis, the defendant may claim damages in separate ordinary proceedings subject to the general rules set forth by the CCP.

### **SPECIAL REMARKS / B. *Extinction of maritime privileges***

Regardless of the extinction of the credits that originated them, maritime privileges terminate when:

- 1° More than one year has passed from the date of the origin of the credit. Such a period is not susceptible to any interruptions or suspensions except in favor of the creditor who may have obtained the legal retention or judicial seizure of the good subject to privilege, or by the creditor that could not previously enforce his *privileged credit* because of a legal impediment;
- 2° The vessel is sold judicially, either voluntarily or involuntarily, after the registration thereof in the pertinent registry, or after 30 consecutive days have passed from the date of the auction, whichever period is shorter, and
- 3° In the case of the voluntary conveyance of the vessel, after 90 consecutive days have passed from the date of the registration of the transfer.

The provisions in numbers 2° and 3° above do not preclude the right of the privileged creditors to exercise their preference upon the unpaid balance of the price, should there be one.

### **Recent developments**

In a recent arrest relating an alleged claim for damages arising from pollution at Quintero Bay, the court of Quintero accepted a P&I club letter of undertaking without the agreement of the arrest petitioner.

These are good news as Chilean courts seem to be finally aligned with the international practice whereby LOUs are accepted by courts as sufficient guarantee.