Brooklyn Journal of Corporate, Financial & Commercial Law

Volume 14 | Issue 1 Article 10

12-27-2019

Between Scylla and Charybdis: Maritime Liens And the Bankruptcy Code

Ian T. Kitts

BETWEEN SCYLLA AND CHARYBDIS: MARITIME LIENS AND THE BANKRUPTCY CODE

ABSTRACT

Federal courts have had trouble fitting maritime law into the bankruptcy scheme created by the Bankruptcy Code (the Code). Particularly troublesome have been vessel-arrest proceedings that are underway when the vessel's owner files for bankruptcy. Prior to the enactment of the Code, courts applied the doctrine of custodia legis *to decide whether the admiralty or the bankruptcy court would administer the vessel. Since the Code was enacted, courts have generally held that the bankruptcy court gained control. A recent Ninth Circuit decision, however, split with other circuits and seems to have revived* custodia legis*. This Note argues that the Ninth Circuit was wrong to do so since the text of the Code addresses the issue, the objectives of the Code are undermined by* custodia legis*, and the Code sufficiently protects maritime lienors. Furthermore, this Note suggests that Congress grant bankruptcy judges Article III status and amend the definitions in the Code so that maritime liens are unmistakably considered 'liens.'*

INTRODUCTION

> *ἀλλὰ μάλα Σκύλλης σκοπέλῳ πεπλημένος ὦκα*
> *νῆα παρὲξ ἐλάαν, ἐπεὶ ἦ πολὺ φέρτερόν ἐστιν*
> *ἓξ ἑτάρους ἐν νηὶ ποθήμεναι ἢ ἅμα πάντας.*[1]

When a shipowner files for bankruptcy, the bankruptcy court will have to navigate the tricky strait between maritime law and bankruptcy. On one side is maritime law, with its ancient customs and jealous protection of all things maritime, while on the other side is the Bankruptcy Code, a modern feat of legal engineering designed to protect both the debtor and *all* of its creditors. One particularly rocky shoal of which the court must be aware is that of maritime liens—charges against a vessel that secure the shipowner's debts.[2]

Maritime liens are treated quite differently under traditional maritime law than how land-based, non-maritime liens are treated under the Bankruptcy Code. Maritime liens are created by certain boat-related transactions.[3] They may be enforced in court by having the vessel arrested and sold, with the proceeds used to satisfy the debt.[4] Courts sitting in

1. Homer, The Odyssey, Book 12 Lines 108–10 ("Sail closer to Scylla's cliff [than to Charybdis] and quickly / drive your ship past, as it is far better / to mourn six men in your ship than all of them together.").

2. 1 Thomas J. Schoenbaum, Admiralty & Maritime Law 683 (5th ed. 2011).

3. *See id.*; *infra* Part I.

4. *Id.* at 721.

admiralty have traditionally been the exclusive forum for enforcing, satisfying, and extinguishing maritime liens.[5] Bankruptcy courts, on the other hand, were created to address virtually all claims—secured or unsecured—against the debtor.[6] To accomplish this, the filing of a bankruptcy petition immediately stops almost all attempts by creditors to collect money from the debtor—including the enforcement of liens[7]—and transfers nearly all the debtor's property into an estate under the jurisdiction of the bankruptcy court.[8] An issue arises when a maritime lienor has arrested a vessel to enforce a maritime lien and the owner of the encumbered vessel then files for bankruptcy: whether the admiralty court or the bankruptcy court has jurisdiction over the vessel.

Courts navigating these murky waters have charted several courses: some toward the side of bankruptcy and others toward maritime law. Under the prior bankruptcy scheme, the Bankruptcy Act of 1898 (the Act),[9] the doctrine of *custodia legis* generally determined whether an admiralty court or a bankruptcy court was to administer a debtor's maritime-lien-encumbered vessel by leaving the vessel to the court that first obtained jurisdiction over it: if the vessel was arrested before its owner filed for bankruptcy, then the admiralty court would generally retain jurisdiction over the vessel through the bankruptcy.[10] Since the passage of the current bankruptcy law, the Bankruptcy Reform Act of 1978 (the Code), courts have reached varying conclusions on whether *custodia legis* continues to apply and how to resolve the issue. The Fifth Circuit has rejected *custodia legis* altogether.[11] At least one court in the Second Circuit has held that *custodia legis* applied to reorganization-type bankruptcies but not to liquidations.[12] Most recently, in 2018, the Ninth Circuit has stated that *custodia legis* continues to apply under any kind of bankruptcy, at least with respect to certain kinds of maritime liens.[13]

This Note will argue that the Fifth Circuit's course is the most prudent and should be adopted by other circuits because it is in accordance with the plain meaning of the Code, follows the legislative intent, best accomplishes the goals of bankruptcy, and does not harm maritime lienors. Part I will provide a background of maritime liens. Part II will give an overview of the treatment of secured creditors under the Code. Part III will examine the

5. *Id.* at 739.

6. 1 Collier on Bankruptcy ¶ 1.01 (Richard Levin & Henry J. Sommers eds., 16th ed. 2019).

7. 11 U.S.C. § 362(a) (2012).

8. 11 U.S.C. § 541; 5 Collier, *supra* note 6, ¶ 541.01; *see infra* Part II.

9. Also known as the "Nelson Act."

10. *See* Ramsay McCullough, *Law Wars: The Battle Between Bankruptcy and Admiralty*, 32 Tul. Mar. L.J. 457, 469–72 (2008).

11. *In re* La. Ship Mgmt., Inc., 761 F.2d 1025, 1025 (5th Cir. 1985).

12. Morgan Guar. Tr. Co. of N.Y. v. Hellenic Lines Ltd. (*Hellenic II*), 585 F. Supp. 1227, 1229 (S.D.N.Y. 1984).

13. Barnes v. Sea Haw. Rafting, LLC, 889 F.3d 517, 532–33 (9th Cir. 2018).

conflicts between the two areas of law and explain the various solutions courts have found. Part IV will argue that the Fifth Circuit correctly interprets the Code and that additional protections for maritime lienors outside the Code are unnecessary. Part V will provide suggestions for how Congress can amend the Code to clarify how maritime liens are to be treated in bankruptcy.

I. MARITIME LIENS

A maritime lien is a claim against a vessel that secures certain debts and may be enforced to satisfy the debt through an admiralty proceeding.[14] In the United States, maritime liens are theoretically grounded in the legal fiction that a vessel is a person who incurs debt and may be called upon to satisfy that debt.[15] Justice Brown explained:

> A ship is born when she is launched, and lives so long as her identity is preserved. Prior to her launching she is a mere congeries of wood and iron—an ordinary piece of personal property—as distinctly a land structure as a house, and subject only to mechanics' liens created by state law and enforceable in the state courts. In the baptism of launching she receives her name, and from the moment her keel touches the water she is transformed, and becomes a subject of admiralty jurisdiction. She acquires a personality of her own; becomes competent to contract, and is individually liable for her obligations, upon which she may sue in the name of her owner, and be sued in her own name. . . . She is capable, too, of committing a tort, and is responsible in damages therefor. She may also become a quasi bankrupt; may be sold for the payment of her debts, and thereby receive a complete discharge from all prior liens, with liberty to begin a new life, contract further obligations, and perhaps be subjected to a second sale.[16]

The transactions that give rise to a maritime lien depend on the laws of the jurisdiction; transactions giving rise to maritime liens in the United States include wages owed to seamen, the supply of "necessaries" like fuel or food, and towage.[17] Involuntary creditors, i.e., victims of maritime torts like collision, allision,[18] and pollution, also receive maritime liens.[19] While the kinds of transactions that give rise to maritime liens were a product of

14. 1 Shoenbaum, *supra* note 2.

15. *Id.* at 683–84.

16. Tucker v. Alexandroff, 183 U.S. 424, 438 (1902).

17. *See generally* William Tetley with Robert C. Wilkins, Maritime Liens and Claims (2d ed. 1998) (cataloguing types of maritime liens and where they are recognized).

18. Allision refers to striking against a fixed object, like a stationary vessel or dock. *Allision*, Black's Law Dictionary (11th ed. 2019). It is opposed to collision, which is striking another vessel that is in motion. *Collision*, Black's Law Dictionary (11th ed. 2019).

19. *See* Tetley, *supra* note 17, at 387–88.

maritime common law, Congress has codified this common law so that the categories of maritime liens are set in the United States.[20]

Maritime liens exist to protect creditors while keeping vessels in commerce.[21] A vessel's basic purpose is to travel from port to port: she is, "of necessity, a wanderer."[22] Over a voyage, a vessel will inevitably incur expenses to keep operating, but its owner will often be in a distant, foreign jurisdiction.[23] Someone extending credit to a vessel may have a hard time enforcing a judgment against a defaulting owner in another jurisdiction. To remedy this problem, certain creditors receive by the operation of maritime law a security interest in the vessel itself—a maritime lien—enforceable *in rem* in any jurisdiction recognizing the maritime lien.[24] The maritime lien prevents the vessel's owner from avoiding its debts by simply moving its vessel away from its creditors and hiding in a foreign jurisdiction.[25] By making it easier for creditors to collect on debt, maritime liens facilitate the extension of credit and thereby encourage maritime commerce.

To enforce a maritime lien, the maritime lienor asks the admiralty court of the jurisdiction, in which the encumbered vessel is located, to have the vessel seized in port.[26] In the United States, Article III district courts have exclusive jurisdiction over admiralty matters,[27] and the seizure process they use is called "vessel arrest."[28] When a vessel is arrested, it may be released from arrest if sufficient cash is filed with the court as security for the vessel.[29] Otherwise, the court will sell the vessel and distribute the proceeds to the maritime lienors.[30] The court prioritizes the maritime lienors in classes based on the underlying transaction.[31] While there are no binding rules an admiralty judge must follow, expenses incurred by arresting and

20. *See In re* Eagle Geophysical, Inc., 256 B.R. 852, 857 (Bankr. D. Del. 2001) ("Congress codified federal maritime lien law which substituted a single federal statute for conflicting state laws. To the extent that any remaining provisions from prior law were not included in the [codification], we . . . conclude that Congress did not intend that they survive. . . . [C]ommon law maritime lien law has been superceded by statute and is not a basis, by itself, for a secured [bankruptcy] claim.") (footnote omitted) (citations omitted); *see also, e.g.*, 46 U.S.C. §§ 31341–43 (2012) (codifying maritime liens).

21. 1 Schoenbaum, *supra* note 2, at 684–85.

22. 2 Benedict on Admiralty § 21 (2018).

23. *Id.* ("[A vessel] visits shores where her owners are neither known nor are accessible.").

24. *Id.*; *see also* Tetley, *supra* note 17, at 1265–1410 (summarizing maritime law and liens in various countries).

25. 1 Schoenbaum, *supra* note 2, at 684–85.

26. *See* Tetley, *supra* note 17, at 933–1026 (describing various types of enforcement procedures).

27. U.S. Const. art. III § 2 ("The judicial Power shall extend . . . to all Cases of admiralty and maritime Jurisdiction . . . .").

28. *See* Tetley, *supra* note 17, at 941–43; *see also* Fed. R. Civ. P. Supplemental Rules for Admiralty or Maritime Claims and Asset Forfeiture Actions R. C (United States procedure for vessel arrest).

29. *See* Tetley, *supra* note 17, at 948–49.

30. *See id.* at 951.

31. *See* 1 Schoenbaum, *supra* note 2, at 721–24.

maintaining the vessel are generally paid off first, then liens held by seamen for wages and maintenance and cure.[32] A properly conducted admiralty sale extinguishes *all* maritime liens against the vessel, whether or not the maritime lienor appeared in court or was paid in full.[33] A maritime lien is only extinguished by such a sale or by satisfaction of the debt, waiver, laches, or destruction of the encumbered vessel.[34]

Article 9 of the Uniform Commercial Code (UCC), which governs liens, does not apply to maritime liens.[35] Maritime liens differ substantially from UCC-governed "land-based" liens.[36] One treatise went so far as to say that maritime liens and land-based liens are "two unlike things . . . called by the same name."[37] First, maritime liens arise automatically, by operation of law, regardless of whether the parties consent.[38] Second, maritime liens do not require recordation to be perfected.[39] Third, maritime liens are not extinguished by the sale of the vessel to a bona-fide purchaser.[40] Fourth, proceeds from a vessel sale are distributed within a class of maritime lienors in reverse chronological order—a maritime lien arising later has priority over a maritime lien of the same class that arose earlier.[41]

II. LIENS IN BANKRUPTCY

The objectives of bankruptcy are to provide the debtor with a "fresh start" and to repay the creditors in a fair and orderly fashion.[42] A debtor may liquidate entirely under chapter 7 or reorganize under chapter 11 to pay off its creditors and continue to do business.[43] There is a strong preference for reorganization when the debtor is a business, as a successful reorganization preserves employees' jobs and the debtor's "going concern" value.[44]

When a debtor files for bankruptcy, several statutes go into effect. For one, an estate is created under the jurisdiction of the bankruptcy court, and

32. *See id.*
33. *Id.* at 721.
34. *Id.* at 728.
35. Walsh v. Placedo Shipping Corp. of Liber (*In re* Pac. Caribbean Shipping (USA), Inc.), 789 F.2d 1406, 1407 (9th Cir. 1986).
36. *See* Grant Gilmore & Charles L. Black, Jr., The Law of Admiralty 586–89 (2d ed. 1975).
37. *Id.* at 589.
38. *In re Pac. Caribbean*, 789 F.2d at 1407.
39. *Id.* The one exception is for preferred ship mortgages, which do require recordation to perfect. *See* 46 U.S.C. § 31322 (2012).
40. Gilmore, *supra* note 36, at 588.
41. *In re Pac. Caribbean*, 789 F.2d at 1407.
42. 1 Collier, *supra* note 6, ¶ 1.01.
43. *Id.*
44. 1 Collier, *supra* note 6, ¶ 1.01. The "going concern" value of a business as a cohesive, operating unit, as opposed to the aggregate value of its individual assets (the "liquidation value"). *See Value (2) – Going Concern Value*, Black's Law Dictionary (11th ed. 2019). Generally, the going concern value of a business is greater than the liquidation value because the business's combination of assets should create goodwill and future cash flows. *Id.*

virtually all of the debtor's property, "wherever located and by whomever held," is transferred into it.[45] Any entity, including a government unit, holding property of the estate must turn it over to the bankruptcy trustee.[46] Property held by a court as the result of a foreclosure on a security interest is part of the estate and must be turned over.[47]

Also upon commencement of a bankruptcy, the "automatic stay" goes into effect.[48] The stay prohibits almost all creditors from attempting to collect any of their debts.[49] Creditors may not sue or enforce judgments against the debtor.[50] They may not attempt to obtain possession of or exercise control over property of the bankruptcy estate,[51] nor may they attempt to "create, perfect, or enforce any lien against property of the estate."[52] The purpose of the automatic stay is not only to protect the debtor from harassment by creditors, but also to protect the creditors by preventing faster-acting creditors from bettering their own positions at the expense of the rest.[53] The stay makes an orderly distribution of the debtor's assets possible.[54]

In the bankruptcy process, creditors' claims against the debtor are classified as either secured or unsecured.[55] A secured claim is a claim secured by a lien on property of the bankruptcy estate, whereas an unsecured claim has no such collateral.[56] To the extent that a claim is secured but the amount owed is greater than the value of the lien—it is considered unsecured and treated as such.[57] The Code defines a lien as a "charge against or interest in property to secure payment of a debt . . . ."[58] The definition is meant to be "very broad."[59] The Code defines three kinds of liens: security interests, judicial liens, and statutory liens.[60] A security

45. 11 U.S.C. § 541 (2012).

46. 11 U.S.C. § 542 (2012).

47. *Id.* (requiring turnover by "an entity . . . in possession, custody or control" of property of the estate); 11 U.S.C. § 101(15) (2012) (including "governmental unit" within the definition of "entity."); *see* United States v. Whiting Pools, Inc., 462 U.S. 198 (1983) (requiring Internal Revenue Service to turn over debtor's property it had seized to satisfy a tax lien).

48. *See* 11 U.S.C. § 362 (2012).

49. *Id.* § 362(a).

50. *Id.* § 362(a)(1)–(2).

51. *Id.* § 362(a)(3).

52. *Id.* § 362(a)(4).

53. H.R. Rep. No. 95-595, at 340 (1977), *reprinted in* Volume C Collier on Bankruptcy app. pt. 4(d)(i) (Richard Levin & Henry J. Sommers eds., 16th ed. 2019).

54. *Id.*

55. *See* 11 U.S.C. § 506(a)(1) (2012). A claim is virtually *any* right to payment from the debtor. *See* 11 U.S.C. 101(5) (2012).

56. 11 U.S.C. § 506(a)(1) (2012).

57. *Id.* This is known as the "bifurcation of claims."

58. 11 U.S.C. § 101(37) (2012).

59. H.R. Rep. No. 95-595, at 314 (1977), *reprinted in* Volume C Collier on Bankruptcy app. pt. 4(d)(i) (Richard Levin & Henry J. Sommers eds., 16th ed. 2019).

60. 2 Collier, *supra* note 6, ¶ 101.51.

interest is a lien "created by an agreement."[61] A judicial lien is a lien "obtained by judgment, levy, sequestration, or other legal or equitable process or proceeding."[62] A statutory lien is a lien "arising solely by force of a statute on specified circumstances or conditions . . . ."[63] A statute describing the characteristics and effects of a lien does not necessarily make that lien statutory.[64] A statutory lien arises automatically and is not based on an agreement.[65] These three categories of liens are meant to be exhaustive, with only "certain common law liens" outside this classification.[66]

Secured creditors are treated quite favorably under the Code.[67] They are entitled to the value of their interest in their collateral and are important to confirming a plan for reorganization.[68] However, secured creditors are prevented from enforcing their liens during a bankruptcy,[69] and if enforcement proceedings are underway when the debtor files for bankruptcy, then those proceedings are immediately stayed and the property securing the debt comes under the jurisdiction of the bankruptcy court.[70] The secured creditor must seek permission from the bankruptcy court to enforce its lien.[71] Otherwise, secured creditors may enforce their liens if the encumbered property is so burdensome to the bankruptcy estate or of such "inconsequential value and benefit" that the bankruptcy trustee chooses to abandon the property.[72]

A secured creditor stayed from enforcing a lien is entitled to "adequate protection" of that lien as a matter of right.[73] Adequate protection guards against the decrease in the value of the creditor's lien. Adequate protection may be provided through cash payments, additional liens, or any other relief.[74] If the debtor cannot provide the secured creditor with adequate protection, then the court *must* lift the automatic stay with respect to the encumbered property.[75] For example, if a secured creditor's collateral is depreciating so that its value will become less than the debt it secures, the

61. 11 U.S.C. § 101(51) (2012).
62. 11 U.S.C. § 101(36) (2012).
63. 11 U.S.C. § 101(53) (2012).
64. 2 Collier, *supra* note 6, ¶ 101.53.
65. H.R. Rep. No. 95-595, at 314 (1977), *reprinted in* Volume C Collier on Bankruptcy app. pt. 4(d)(i) (Richard Levin & Henry J. Sommers eds., 16th ed. 2019).
66. *Id.* at 312.
67. 4 Collier, *supra* note 6, ¶ 506.02.
68. *Id.*
69. 11 U.S.C. § 362(a) (2012).
70. *Id.*; 11 U.S.C. § 541 (2012).
71. 11 U.S.C. § 362(d) (2012).
72. 11 U.S.C. § 554 (2012).
73. 3 Collier, *supra* note 6, ¶ 361.02.
74. 11 U.S.C. § 361 (2012). The only form of relief the statute proscribes is granting the creditor's claim administrative-expense priority. *Id.*
75. 11 U.S.C. § 362(d)(1) (2012) ("[T]he court *shall* grant relief from the stay . . . for cause, including lack of adequate protection . . . .") (emphasis added).

trustee may provide adequate protection through cash payments equal to the depreciation.[76]

As Justice Brown pointed out, an admiralty sale to enforce a maritime lien is similar to a bankruptcy proceeding in that the value of an asset is distributed to creditors and debt is discharged.[77] There are, however, several notable differences in an actual bankruptcy. For one, bankruptcy is not just liquidation of assets but may also be a reorganization of the debtor.[78] Furthermore, bankruptcy liquidation deals with all of a debtor's assets—not just the maritime asset.[79] In either case, when a bankruptcy proceeding is commenced, almost all of the debtor's assets become property of a bankruptcy estate "wherever located and by whomever held."[80]

III. MARITIME LIENS IN BANKRUPTCY

When a shipowner files for bankruptcy, maritime liens must be satisfied before any land-based liens are paid from proceeds of the vessel's sale—in other words, maritime liens have priority over non-maritime liens.[81] Even so, maritime lienors are still clearly stayed from arresting a vessel after its owner files for bankruptcy.[82] However, when a vessel is arrested and then the shipowner files for bankruptcy, courts have charted several courses between the jurisdictions of the bankruptcy and admiralty courts.[83] Prior to the Code, courts generally invoked *custodia legis* to determine that the admiralty court maintained jurisdiction over the vessel.[84] After the Code became law, the Fifth Circuit, which was followed by others, held that the bankruptcy court obtained jurisdiction.[85] The Second Circuit steered a different course by holding that in reorganization the bankruptcy court

76. *See* 3 Collier, *supra* note 6, ¶ 361.03[2].

77. Tucker v. Alexandroff, 183 U.S. 424, 438 (1902).

78. *See* 7 Collier, *supra* note 6, ¶ 1100.01.

79. *See* 11 U.S.C. § 541(a)(1) (2012) ("[The bankruptcy] estate is comprised of all the following property, wherever located and by whomever held: . . . all legal or equitable interested of the debtor in property as of the commencement of the case.").

80. *Id.*

81. *In re* Muma Servs., Inc., 322 B.R. 541, 547 (Bankr. D. Del. 2005) ("Generally, maritime liens must be satisfied before non-maritime liens.").

82. Edward M. Heller & Jan M. Hayden, *Vessel Arrest Before and After Bankruptcy—The Automatic Stay*, 59 Tul. L. Rev. 1212, 1214 (1985) ("Obviously, the arrest of a vessel is prohibited after the owner or charterer has filed a petition under the Bankruptcy Code . . . .").

83. *See* McCullough, *supra* note 10, at 472–90 (describing what the author terms the "six episodes of *custodia legis*").

84. *See* Wong Shing v. M/V Mardina Trader, 564 F.2d 1183, 1188 (5th Cir. 1977) ("When a court of competent jurisdiction takes possession of property through its officers, that property is withdrawn from the jurisdiction of all other courts. Where the jurisdiction of a court, and the right of a plaintiff to prosecute his suit in it, have attached, that right cannot be arrested or taken away by the proceedings in another court.").

85. *See In re* La. Ship Mgmt., Inc., 761 F.2d 1025, 1025 (5th Cir. 1985); *see also* O'Hara Corp. v. F/V N. Star, 212 B.R. 1, 4 (D. Maine 1997) (District Court in the First Circuit following the Fifth Circuit).

obtained jurisdiction, while in liquidation the admiralty court maintained its jurisdiction.[86] Most recently, the Ninth Circuit returned to familiar waters when it held that an admiralty court maintains jurisdiction regardless of the type of bankruptcy.[87] Each Circuit's course is explained in greater detail below.

A. BEFORE THE CODE: *CUSTODIA LEGIS*

Before the current Bankruptcy Code was enacted, courts generally applied the doctrine of *custodia legis* when a vessel was arrested before a bankruptcy commenced.[88] Starting from the premise that only one court can properly exercise jurisdiction over an asset, the doctrine provided that the first court to take possession of property has exclusive jurisdiction over that property.[89] The Supreme Court made an early reference to the doctrine, although not by name, in the 1894 case *Moran v. Sturges*.[90] In this case, a towing company, stating that it did not have sufficient property to satisfy its liabilities, petitioned for voluntary dissolution in state court.[91] The state court enjoined all creditors of the company from taking action.[92] The day after, several holders of maritime liens in the company's steamships had the vessels arrested; a dispute over the legitimacy of the arrest followed.[93] In resolving the dispute, the Supreme Court mentioned "[i]t is a rule of general application that, where property is in the actual possession of one court of competent jurisdiction, such possession cannot be disturbed by process out of another court."[94]

Several years later, in *The Philomena*, a district court sitting in admiralty invoked the doctrine to decide that the court continued to have jurisdiction over a vessel arrested before the owner filed for bankruptcy. In this case, a maritime lienor had a steamship arrested.[95] Several days later, an involuntary bankruptcy petition was filed against the vessel's owner.[96] The bankruptcy receiver petitioned the admiralty court to receive the proceeds from the sale, before the maritime claims were paid out, so the receiver could distribute the funds.[97] The court, noting that bankruptcy courts had no

86. Morgan Guar. Trust Co. of N.Y. v. Hellenic Lines Ltd. (*Hellenic II*), 585 F. Supp. 1227, 1229 (S.D.N.Y. 1984).

87. Barnes v. Sea Haw. Rafting, LLC, 889 F.3d 517, 532–33 (9th Cir. 2018).

88. *See* McCullough, *supra* note 10, at 472–75.

89. *See, e.g.*, Wong Shing v. M/V Mardina Trader, 564 F.2d 1183, 1188 (5th Cir. 1977).

90. *See* Moran v. Sturges, 154 U.S. 256 (1894).

91. *Id.* at 258. Dissolution is part of a non-bankruptcy liquidation process for corporations. *See Dissolution*, Black's Law Dictionary (11th ed. 2019).

92. *Moran*, 154 U.S. at 258–59.

93. *Id.* at 259–62.

94. *Id.* at 274.

95. The Philomena, 200 F. 859, 860 (D. Mass. 1911).

96. *Id.*

97. *Id.*

admiralty jurisdiction, kept the funds to distribute to the maritime lienors.[98] The court relied on *custodia legis*, stating that "[t]he admiralty court . . . cannot refuse to proceed, in an admiralty suit properly before it, wherein its jurisdiction over the property was complete before the bankruptcy proceedings were inaugurated . . . ."[99]

The doctrine continued to be used until the passage of the Code in 1978.[100] Courts, however, recognized an exception to it when the debtor was attempting to reorganize. Reasoning that bankruptcy courts have broader powers in a reorganization than liquidation, the court in *In re J.S. Gissel & Co.* held that the bankruptcy court had the authority to stay an admiralty foreclosure commenced prior to the bankruptcy.[101] Importantly, the Act did not have an automatic stay provision like the current Code. Instead, the bankruptcy court had discretion to enter a stay if the circumstances required, such as protecting assets during a reorganization.[102]

B. AFTER THE CODE: CIRCUIT SPLIT

With the passage of the Bankruptcy Code in 1978, courts had to fix their bearings to the new statutes. It was an open question as to how a pre-petition vessel arrest was to be handled under the new law and whether *custodia legis* was still applicable. Courts in the Fifth, Second, and Ninth Circuits came to different results.

1. The Fifth Circuit: To the Side of Bankruptcy

Several years after the Code went into effect, the Fifth Circuit had a chance to rule on whether *custodia legis* applied under the new law. In *United States v. LeBouf Bros. Towing Co., Inc*, the United States brought an action to foreclose its preferred ship mortgages on vessels owned by a towing company.[103] The vessels were arrested and ordered to be sold.[104] However, three days before the sale, the towing company filed for chapter 11 bankruptcy and moved to revoke the order for sale, citing the automatic stay.[105] The court considered *custodia legis* and found that it was inapplicable under the Code because the plain meaning of automatic stay prevented it from selling the vessels.[106] The court also noted that "Congress certainly intended, and the statute clearly provides, that the automatic stay effected by § 362 prevent all post-petition executions on a debtor's

98. *Id.* at 862.
99. *Id.* at 861.
100. *See, e.g.*, Wong Shing v. M/V Mardina Trader, 564 F.2d 1183, 1188 (5th Cir. 1977).
101. *In re* J.S. Gissel & Co., 238 F. Supp. 130, 133 (S.D. Tex. 1965).
102. *Id.*
103. United States v. LeBouf Bros. Towing Co., Inc., 45 B.R. 887 (E.D. La. 1985).
104. *Id.*
105. *Id.*
106. *Id.* at 889–90.

property; consequently the sale of [the] boats in this action cannot proceed."[107] The court considered, and expressly rejected, applying *custodia legis* differently based on whether the bankruptcy was a liquidation or reorganization.[108]

Shortly after, the Fifth Circuit reaffirmed the rejection of *custodia legis* with a terse, two-paragraph opinion in *In re Louisiana Ship Management, Inc.*[109] It held that an admiralty sale, commenced prior to a bankruptcy but completed after, was null because the bankruptcy court obtained exclusive jurisdiction over the vessel upon the filing of the bankruptcy petition: "Filing of the petition under Chapter 11 automatically stayed the proposed sale to enforce the maritime lien. . . . In addition, it vested exclusive jurisdiction over the vessel in the [bankruptcy] court . . . ."[110] Courts in other circuits have also followed the Fifth Circuit's course.[111]

2. The Second Circuit: Between Bankruptcy and Admiralty

At least one case in the Second Circuit has applied *custodia legis* to liquidations but not reorganizations. In *Morgan Guaranty Trust Co. of New York v. Hellenic Lines Ltd.*, maritime lienors had several of Hellenic Lines' vessels and freights arrested.[112] Hellenic Lines then filed for a chapter 11 reorganization.[113] The bankruptcy court lifted the stay for some, but not all, of Hellenic Lines' maritime assets.[114] A maritime lienor moved that the district court determine whether it retained jurisdiction over freights that had been arrested, or whether they were subject to the bankruptcy court.[115] The district court held that *custodia legis* did not apply and that the bankruptcy court would administer the freights.[116] The court approved of the doctrine generally for its efficiency, but the court declined to apply it because it would frustrate the rehabilitative goal of the chapter 11 reorganization.[117] However, after the bankruptcy was later converted to a chapter 7 liquidation, the same maritime lienors moved for the district court to direct Hellenic Lines to pay the proceeds from the freights to the district court for distribution according to maritime law.[118] Since Hellenic Lines

107. *Id.* at 891.
108. *Id.* at 889–91.
109. *In re* La. Ship Mgmt., Inc., 761 F.2d 1025 (5th Cir. 1985).
110. *Id.*
111. *See, e.g.*, O'Hara Corp. v. F/V N. Star, 212 B.R. 1, 4 (D. Maine 1997).
112. Morgan Guar. Tr. Co. of N.Y. v. Hellenic Lines Ltd. (*Hellenic I*), 38 B.R. 987, 989 (S.D.N.Y. 1984).
113. *Id.*
114. *Id.* at 992.
115. *Id.* at 989.
116. *Id.* at 992.
117. *Id.* at 997.
118. Morgan Guar. Tr. Co. of N.Y. v. Hellenic Lines Ltd. (*Hellenic II*), 585 F. Supp. 1227, 1228 (S.D.N.Y. 1984).

was liquidating instead of reorganizing, the court held that *custodia legis* applied and granted the motion.[119]

No reported decision in the Second Circuit has since reconsidered the issue, but dicta in a 2005 case suggested that whether the bankruptcy is a liquidation or a reorganization would be a factor relevant to deciding whether the admiralty court or the bankruptcy court had jurisdiction over a vessel arrested immediately prior to the filing of a bankruptcy petition.[120] As it stands, the law in the Second Circuit appears to be that admiralty foreclosures are stayed and the bankruptcy court obtains jurisdiction over arrested vessel in reorganizations, but *custodia legis* applies in liquidations so that the admiralty court retains jurisdiction over the vessel and may proceed with the foreclosure.

3. The Ninth Circuit: To the Side of Admiralty

Recently, the Ninth Circuit seems to have returned to *custodia legis*, at least for some types of maritime liens. In *Barnes v. Sea Hawaii Rafting, LLC*, a seaman had been injured in an explosion on a vessel and sued the vessel *in rem* to enforce his maritime lien for maintenance and cure.[121] The procedural requirements to arrest the vessel were met, but the vessel was not actually arrested because the seaman did not want to pay the costs to arrest the vessel.[122] He recognized the vessel's continued operation was the only way for the vessel's owner to earn money to pay him.[123] The vessel's owner, shortly before the trial, filed for bankruptcy under chapter 7.[124] The admiralty court stayed the vessel foreclosure, and the bankruptcy trustee sold the vessel with the bankruptcy court's approval.[125] On appeal, the Ninth Circuit, citing *Moran* and invoking *custodia legis*, held that the sale was invalid because the admiralty court had jurisdiction over the vessel, not the bankruptcy court.[126] The opinion stated "the district court took constructive control of the [vessel] . . . at the time [Plaintiff] filed his verified complaint [to enforce his maritime lien]. [Debtor's] bankruptcy petition, filed nearly two years later, could not have vested the bankruptcy court with the same jurisdiction."[127] Furthermore, the Ninth Circuit held that the automatic stay did not apply to the enforcement of seamen's

119. *Id.*
120. *In re* Millenium Seacarriers, Inc., 419 F.3d 83, 95 n.10 (2d Cir. 2005) ("We . . . need not opine on . . . whether the fact that the pertinent bankruptcy proceeding is a reorganization or a liquidation impacts the role [*custodia legis*] plays . . . .").
121. Barnes v. Sea Haw. Rafting, LLC, 889 F.3d 517, 523 (9th Cir. 2018).
122. *Id.* at 530.
123. *Id.*
124. *Id.* at 524.
125. *Id.*
126. *Id.* at 533.
127. *Id.*

maritime liens for wages or maintenance and cure.[128] The Ninth Circuit expressly stated that the type of bankruptcy—liquidation or reorganization—was irrelevant.[129]

To reach its holdings, the Ninth Circuit relied heavily on an earlier case, *United States v. ZP Chandon*.[130] In *ZP Chandon*, a tugboat company filed a chapter 11 bankruptcy.[131] Prior to the bankruptcy, the Federal Maritime Administration had several of the company's tugboats arrested to enforce its vessel mortgages on them.[132] The boats were released from arrest and permitted to operate along the west coast of the United States.[133] The bankruptcy court soon granted the United States relief from the stay to enforce its mortgages via arrest.[134] Crew members sought to intervene, arguing that they had enforceable maritime liens arising from operating the boats after the automatic stay went into effect and that they were therefore entitled to proceeds from the vessels' sale.[135] The Ninth Circuit held that the crew was entitled to the proceeds because section 362(a)(4) of the Code did not stay the creation of *maritime* liens.[136] The court argued that maritime liens for wages are not statutory liens, since they existed prior to statutory codification.[137] It said that "[m]aritime liens for seamen wages . . . are 'sacred liens' entitled to protection 'as long as a plank of the ship remains . . . .'"[138] The court argued that Congress would not interfere with such an "ancient principle" *sub silentio*, or without explicitly saying so.[139] It found, therefore, that Congress's silence about maritime liens indicated its intent for the section to apply only to "land-based transactions where (1) a recording of a lien interest is required and (2) the creditor first in time is entitled to priority."[140] This rule was expressly reinforced in another case prior to *Barnes*. In *Adams v. S/V Tenacious*, the court held that *ZP Chandon* was irrelevant to maritime liens for preferred ship mortgages, which require recordation to be perfected and are expressly exempt from the automatic stay under certain circumstances.[141]

Building on the language in *ZP Chandon*, the *Barnes* court expanded its holding to find that section 362(a)(4) of the automatic stay also did not

128. *Id.*
129. *Id.* at 533.
130. *See id.* at 532–33.
131. United States v. ZP Chandon, 889 F.2d 233, 234 (9th Cir. 1989).
132. *Id.* at 234–35.
133. *Id.* at 235.
134. *Id.*
135. *Id.*
136. *Id.* at 239.
137. *Id.* at 238.
138. *Id.* (quoting The John G. Stevens, 170 U.S. 113, 119 (1898)).
139. *Id.*
140. *Id.*
141. Adams v. S/V Tenacious, 203 B.R. 297, 298 (D. Alaska 1996).

apply to the *enforcement* of maritime liens for maintenance and cure.[142] As such, the automatic stay did not apply to the vessel foreclosure and *custodia legis* determined which court would administer the boat.[143]

As the law in the Ninth Circuit stands, it seems that maritime liens possessed by seamen—either for wages or maintenance and cure—are not affected by the automatic stay. Other maritime liens that do not require recordation and have inverse-order priority may not be affected by the stay. Maritime liens for preferred ship mortgages, which require recordation, are subject to the automatic stay. Therefore, *custodia legis* applies when the vessel is arrested to enforce seamen's maritime liens and possibly some other maritime liens, but it does not apply to preferred ship mortgages.

IV. THE FIFTH CIRCUIT SHOULD BE FOLLOWED

The Fifth Circuit, and the others that follow it, have properly interpreted the Code with respect to maritime liens. Under the Code, *custodia legis* does not apply in any kind of bankruptcy. The Second and Ninth Circuits' interpretations disregard the plain meaning of the Code, the legislative intent behind it, and its overall objectives.

A. PLAIN MEANING

The plain meaning of the Code renders *custodia legis* obsolete, as the Fifth Circuit recognized. First, the plain meaning of section 541 of the Code—the section creating the bankruptcy estate—unambiguously grants the bankruptcy court jurisdiction over a debtor's vessels, contrary to *custodia legis*. Section 541 creates the bankruptcy estate, comprising "all legal or equitable interests of the debtor . . . ," unless the property falls under one of the enumerated exceptions.[144] Vessels or property in the custody of another court are not excepted.[145] In fact, the Code requires that "an entity . . . in possession, custody, or control, during the case, of property that the trustee may use, sell, or lease . . . shall deliver to the trustee . . . such property."[146] The Supreme Court has specifically held that foreclosed-upon property still comes into the bankruptcy estate, under the jurisdiction of the bankruptcy court.[147] According to these provisions, a vessel arrested and subject to the jurisdiction of an admiralty court becomes property of the bankruptcy estate, where it is administered by the bankruptcy court. This is incompatible with the rule of *custodia legis*.

Second, the plain meaning of section 362 of the Code—the automatic stay provision—prevents an admiralty court from continuing with an arrest

142. Barnes v. Sea Haw. Rafting, LLC, 889 F.3d 517, 532 (9th Cir. 2018).
143. *Id.* at 533.
144. 11 U.S.C. § 541(a) (2012).
145. *See* 11 U.S.C. § 541(b) (2012).
146. 11 U.S.C. § 542(a) (2012).
147. United States v. Whiting Pools, Inc., 462 U.S. 198, 211–12 (1983).

proceeding after bankruptcy is commenced, also contrary to the continued application of *custodia legis*. The stay applies to "any act . . . to exercise control over property of the estate."[148] A vessel—even if encumbered by maritime liens and in the possession of an admiralty court—is property of the estate.[149] Arresting a vessel and selling it is clearly exercising control over it. Therefore, the automatic stay prevents an admiralty court from exercising control over the vessel by continuing an arrest proceeding, thus foreclosing the application of *custodia legis*.

Furthermore, the automatic stay applies to "any act to create, perfect, or enforce any lien against property of the estate."[150] A lien is a "charge against . . . property to secure payment of a debt."[151] A maritime lien is a charge against a vessel that secures a debt; therefore, it is a lien within the meaning of the Code. Although the Ninth Circuit has argued that a maritime lien for wages is not a statutory lien,[152] the automatic stay applies to "*any* lien,"[153] not just statutory. Therefore, the automatic stay also prevents the admiralty court from enforcing maritime liens in an arrest proceeding. In *ZP Chandon*, the Ninth Circuit found it significant that the automatic stay did not "expressly" refer to maritime liens.[154] However, neither does the statute expressly refer to any other particular liens, such as mechanics' liens, mortgages, tax liens, but these are all understood to be within the scope of the stay.[155] The broad language of the statute does not support a reading that includes everything but maritime liens. This is also at odds with *custodia legis*.

B. CONGRESSIONAL INTENT AND LEGISLATIVE HISTORY

The legislative history of the Code indicates that Congress did, in fact, intend for the bankruptcy court to take jurisdiction over an arrested vessel, in contravention of *custodia legis*. One purpose given for the automatic stay is to "prevent dismemberment of the estate. Liquidation must proceed in an orderly fashion. Any distribution of the property must be by the trustee after he has had opportunity to familiarize himself with . . . the property available for distribution."[156] *Custodia legis* does the opposite of Congress' intention

148. 11 U.S.C. § 362(a)(3) (2012).

149. Property of the estate includes the debtor's property "wherever located and by whomever held." *See* 11 U.S.C. § 541(a).

150. 11 U.S.C. § 362(a)(4) (2012).

151. 11 U.S.C. § 101(37) (2012).

152. United States v. ZP Chandon, 889 F.2d 233, 238 (9th Cir. 1989). Courts in other circuits have disagreed. *See, e.g.*, *In re* H&S Transp. Co., Inc., 45 B.R. 233, 238 (Bankr. M.D. Tenn. 1984) ("Since the maritime lien arises automatically and by force of statute, it clearly falls within the Code definition of a statutory lien.").

153. 11 U.S.C. § 362(a)(4) (emphasis added).

154. *ZP Chandon*, 889 F.2d at 238.

155. *See* 3 Collier, *supra* note 6, ¶ 362.03.

156. H.R. Rep. No. 95-595, at 341 (1977), *reprinted in* Volume C Collier on Bankruptcy app. pt. 4(d)(i) (Richard Levin & Henry J. Sommers eds., 16th ed. 2019).

for the Code by separately liquidating the debtor's vessel and paying certain creditors.

Furthermore, the Ninth Circuit's holding in *ZP Chandon* that the stay did not apply to maritime liens depended on its assertion that Congress' failure to mention maritime liens in section 362 evidenced its intent to exclude maritime liens from the provision.[157] The court was incorrect, however, in concluding that Congress never contemplated the issue. In the early 1980s, the maritime industry was in a recession and many maritime companies filed for bankruptcy.[158] The United States Maritime Administration, which guaranteed many ship mortgages, faced increased expenditures as a result of the defaults and bankruptcies.[159] Congress considered various bills to control costs by exempting maritime creditors from the automatic stay.[160] One rejected bill would have amended the Code to allow maritime lienors to enforce their maritime liens despite the stay.[161] Congress ultimately passed a bill that amended section 362 of the Code to add subsections (b)(12) and (b)(13), which allow only the Secretaries of Commerce and Transportation to foreclose on preferred ship mortgages ninety days after the bankruptcy petition is filed.[162] Congress's rejection of a broader exception to the stay for maritime lienors clearly indicates that it intended to have the stay apply to enforcement of maritime liens in other circumstances. With this in mind, the rationale behind the Ninth Circuit's holding in *ZP Chandon* was flawed. The *Barnes* court's reliance on *ZP Chandon* was misplaced, and it should not have been the basis to revive *custodia legis*.

C. *CUSTODIA LEGIS* IMPEDES THE BANKRUPTCY PROCESS

Even if the plain meaning of the Code and the Congressional intent behind it did not displace *custodia legis*, the doctrine would still need to be abandoned because it significantly interferes with the bankruptcy process in both liquidations and reorganizations.

157. *ZP Chandon*, 889 F.2d at 238.

158. *Title XI Bankruptcy Reform: Hearing on S. 1992 and S. 1993 before the Subcomm. on Merch. Marine of the Comm. on Commerce, Sci., and Transp.*, 99th Cong. 12 (1986); *see In re* Prudential Lines, Inc., 69 B.R. 439, 445–48 (Bankr. S.D.N.Y. 1987) (describing history of legislation resulting from the crisis).

159. *Title XI Bankruptcy Reform: Hearing on S. 1992 and S. 1993 before the Subcomm. on Merch. Marine of the Comm. on Commerce, Sci., and Transp.*, 99th Cong. 12 (1986).

160. *See, e.g.*, *To Preserve the Rights of Certain Parties with an Interest in Aircrafts, Aircraft Parts, or Vessel, and for other Purposes*, S. 1993, 99th Cong., 2d Sess. (1985).

161. *See In re Prudential Lines*, 69 B.R. at 445–46.

162. *See* 11 U.S.C. § 362(b)(12)–(13) (2012).

1. *Custodia Legis* Impairs the Bankruptcy Estate in a Liquidation

In a liquidation bankruptcy, the bankruptcy trustee's duty is to "collect and reduce to money the property of the estate . . . ."[163] The trustee seeks to maximize the value of the estate before distribution, and the Code grants the trustee various powers to accomplish this goal.[164] One of those powers is that the trustee may temporarily operate the debtor's business to wind it down if that maximizes the value of the estate.[165] For example, the trustee of a liquidating watch company may "convert watch movements and cases into completed watches which will bring much higher prices than the component parts would have brought."[166] *Custodia legis* would preclude the bankruptcy trustee from being able to wind up the affairs of the debtor, such as completing shipping contracts. This would create additional claims against the estate[167] and make fulfilling the contract for payment into the estate impossible.[168] If, however, the admiralty proceeding is stayed and the bankruptcy court obtains jurisdiction over the vessel, the court may authorize the bankruptcy trustee to operate the vessel to fulfill the debtor's obligations, benefiting both the estate and the creditors.

Furthermore, *custodia legis* does not materially improve judicial economy in a liquidation, and any minimal improvements do not outweigh the benefits of staying the admiralty proceeding. Since bankruptcy liquidation and an admiralty arrest have similar results,[169] it would seem more expeditious to simply apply *custodia legis* and allow the admiralty court to continue to liquidate the vessel. This argument is reinforced by the standard practice in bankruptcy of having the district court conduct the vessel sale.[170] In effect, staying the admiralty court's arrest proceeding only

163. 11 U.S.C. § 704(a)(1) (2012).

164. The most prominent are the trustee's powers to avoid certain transactions the debtor entered into prior to filing for bankruptcy. *See* 11 U.S.C. §§ 544–48 (2012).

165. 11 U.S.C. § 721 (2012).

166. H.R. Rep. No. 95-595, at 380 (1977), *reprinted in* Volume C Collier on Bankruptcy app. pt. 4(d)(i) (Richard Levin & Henry J. Sommers eds., 16th ed. 2019).

167. A claim is a "right to payment," such as damages resulting from a breach of contract. 11 U.S.C. § 101(5)(A) (2012).

168. 11 U.S.C. § 541(a)(6) (2012) (The estate includes "proceeds, product, offspring, rents, or profits of or from property of the estate . . . .").

169. *See supra* Part II.

170. Bankruptcy courts are generally believed to lack the authority to sell a vessel free and clear of maritime liens. 3B Benedict on Admiralty § 43 (2018) ("The only question which remain[s] . . . [is] whether the bankruptcy court had the effective ability to sell a vessel free and clear of maritime liens."); *see*, *e.g.*, Barnes v. Sea Haw. Rafting, LLC, 889 F.3d 517, 533 (9th Cir. 2018). Traditionally, maritime liens are *only* extinguished by an *in rem* proceeding conducted in an admiralty court. Gilmore, *supra* note 36, at 817. The United States Constitution grants admiralty jurisdiction exclusively to Article III courts. U.S. Const. art. III, § 2, ¶ 1 ("The judicial Power shall extend . . . to all Cases of admiralty and maritime Jurisdiction . . . ."); 28 U.S.C. § 1333 (2012) ("The District courts shall have original jurisdiction . . . of . . . any civil case of admiralty or maritime jurisdiction . . . ."). In the current judicial scheme, bankruptcy courts are units of district

delays the admiralty court. However, the potential harm of this delay is mitigated because the Code allows the bankruptcy court to lift the stay "for cause."[171] When the arrest proceeding is stayed and the bankruptcy court takes over, it can allow the admiralty proceeding to continue, or, if it would benefit the estate, allow the trustee to wind up affairs. *Custodia legis* determines the outcome regardless of what is most beneficial to the estate. The stated need to maximize the estate for the benefit of the creditors outweighs the need to sell the vessel quickly, so *custodia legis* is harmful in liquidations.[172]

Additionally, the benefits to judicial economy under *custodia legis* are limited, because maritime lienors will not be entirely kept out of the bankruptcy court. To the extent that the maritime lienors' claims exceed the value of the vessel, their claims will be unsecured.[173] The maritime lienors may still need to file proof of their unsecured claims with the bankruptcy court.[174] *Custodia legis* is only more efficient in terms of allowing the admiralty sale to proceed sooner, which, as previously discussed, is actually detrimental to the bankruptcy process.

2. *Custodia Legis* Makes Reorganization Almost Impossible

Deferring to *custodia legis* and allowing maritime lienors to enforce their liens during a bankruptcy proceeding would make restructuring of maritime companies extremely difficult, if not impossible. Restructuring is preferred to liquidation because restructuring preserves jobs and going concern value,[175] but there is no guarantee that a restructuring will succeed. A maritime company attempting to restructure already faces significant

courts, which refer bankruptcy matters to the bankruptcy court. 1 Schoenbaum, *supra* note 2, at 740. Bankruptcy judges are not Article III judges, since they lack lifetime tenure and pay protection. *See* N. Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 60–61 (1982). Because they are Article I judges, they lack the constitutional authority to adjudicate some claims. *See* Stern v. Marshall, 564 U.S. 462, 485–87 (2011). It has never been decisively settled whether a bankruptcy court has the jurisdiction required to extinguish a maritime lien. *Compare* tetley, *supra* note 17, at 1143 ("No admiralty jurisdiction was bestowed on bankruptcy judges . . . ."), *with* 1 Schoenbaum, *supra* note 2, at 742. ("[T]he bankruptcy judge has full authority to administer the debtor's maritime property, including the power to sell a vessel free and clear of all liens.") (footnote omitted). Another jurisdiction might not recognize the validity of an admiralty sale conducted by a bankruptcy court and arrest a vessel purportedly sold free and clear of maritime liens. This concern lowers the value of the vessel. To maximize the sale price, the general practice is for the district court to withdraw the reference and, sitting in admiralty, sell the vessel itself, delivering it with indisputably clear title. *See* Matthew W. Kavanaugh & Randye B. Soref, Business Workouts Manual § 16:46 (2018) ("The general practice . . . has been to conduct any sales of vessels pursuant to an order of the U.S. District court, sitting in admiralty.").

171. 11 U.S.C. § 362(d)(1) (2012).

172. 11 U.S.C. § 704(a) (2012) ("The trustee shall . . . close [the] estate as expeditiously as is *compatible with the best interests of parties in interest*.") (emphasis added).

173. 11 U.S.C. § 506(a)(1) (2012).

174. 11 U.S.C. § 501(a) (2012).

175. United States v. Whiting Pools, Inc., 462 U.S. 198, 203 (1983).

obstacles, even without the additional difficulty of vessel arrest.[176] If a vessel arrest is not stayed in a restructuring, then the debtor will either be prevented from using the vessel or will have to put up security to release it. To have any chance at reorganization, the debtor needs the ability to use its assets to conduct its business.[177] On the other hand, posting security for the vessel will make restructuring even more expensive and difficult for the debtor, which, by the nature of being bankrupt, will not have much extra cash on hand. Even before the Code, bankruptcy courts recognized that a reorganizing debtor would need to use its arrested vessels and would order the admiralty court to stay a foreclosure.[178] This was also the basis for the post-Code decision *Hellenic I*, which held that *custodia legis* did not apply to reorganizations.[179] Courts can reduce the difficulty of reorganizing a maritime company by recognizing that vessels owned by a reorganizing debtor are not subject to arrest. The Ninth Circuit's rule is therefore undesirable because it makes the socially beneficial restructuring of companies impossible by certain creditors to deprive a maritime debtor of its most important assets.

D. THE BANKRUPTCY CODE PROTECTS MARITIME LIENORS WITHOUT *CUSTODIA LEGIS*

The Code sufficiently protects the interests of maritime lienors so that it is unnecessary to grant them special privileges under *custodia legis* as "wards of the admiralty."[180] In both *ZP Chandon* and *Barnes*, the Ninth Circuit used *custodia legis* to fulfill what it saw as its obligation to protect maritime lienors—namely seamen.[181] However, *custodia legis* provides no

176. *See generally* Mark M. Jaffe, *Chapter 11 Strategies and Techniques—Creditors Committees, Effective Use of a Plan Provisions, Objections to Confirmation, Financing a Chapter 11 Case, Cramdowns and How it Works*, 59 Tul. L. Rev. 1298 (1985) (discussing how the fungibility of services and complicated ownership structure of assets of maritime shipping companies make reorganization particularly difficult).

177. *Whiting Pools*, 462 U.S. at 203 ("The reorganization effort would have a small chance of success . . . if property essential to running the business were excluded from the estate." (citing 6 Collier on Bankruptcy 431 (J. Moore & L. King eds., 14th ed. 1978)). Congress recognized this need in section 362(d)(2) of the Code, where it allows the court to lift the automatic stay for property in which the debtor has no equity *only* if the property is "not necessary to an effective reorganization." 11 U.S.C. § 362(d)(2)(B). In other words, even if the debtor has no ownership interest in an asset, it may continue to use that asset to restructure its business.

178. Gilmore & Black, *supra* note 36, 807–08 ("The powers of the reorganization court to restrain proceedings already instituted when the petition is filed are more extensive than those of the bankruptcy court."); *see In re* J.S. Gissel & Co., 238 F. Supp. 130, 133 (S.D. Texas 1965).

179. Morgan v. Guar. Tr. Co. of N.Y. v. Hellenic Lines Ltd. (*Hellenic I*), 38 B.R. 987, 997 (S.D.N.Y. 1984) (stating "that to employ admiralty procedures and jurisdiction [i.e. *custodia legis*] at all is to deny a shipping line the capacity to reorganize").

180. Barnes v. Sea Haw. Rafting, LLC, 889 F.3d 517, 534 (9th Cir. 2018) (quoting 29 James Wm. Morre et al., *Moore's Federal Practice* § 707.01[12] (3d ed. 2017)).

181. *See* United States v. ZP Chandon, 889 F.2d 233, 238 (9th Cir. 1989) (holding that the automatic stay did not apply to maritime liens because maritime liens were not mentioned and "the drafters of the [the Code] would have casually neglected to express its intention to rewrite a

meaningful protection to maritime lienors that the Code does not. First, *custodia legis* or not, a maritime lienor is entitled to the same priority: under the Code, maritime liens have priority over non-maritime liens, and maritime law is still applied in bankruptcy to determine the priority of the maritime liens against each other.[182] Furthermore, since bankruptcy courts generally refer an encumbered vessel to the district court to sell,[183] the court doing the actual adjudication of maritime lien priority is the same court as when *custodia legis* is used.

Second, the Code includes mechanisms that ensure maritime lienors receive the full value of their collateral, without the extra protection of *custodia legis*. The maritime environment is harsh, and rust and decay can be problems for arrested vessels.[184] In fact, maritime law is so concerned with preserving the value of the vessel that an interlocutory sale of an arrested vessel is permitted when the vessel is "liable to deterioration, decay, or injury."[185] A quick sale of a vessel prevents unnecessary depreciation of its worth as collateral, which at first glance might support the more simple procedure of *custodia legis*.[186] The Code, however, has means to protect maritime lienors from depreciation. Maritime lienors are entitled to adequate protection of their interest in the vessel.[187] If the debtor cannot provide adequate protection, the maritime lienors may have the automatic stay lifted and will be free to continue their admiralty foreclosure.[188] Therefore, maritime lienors will end up in mostly the same position in a bankruptcy as in an admiralty sale.

'sacred' principle of maritime law"); Barnes v. Sea Haw. Rafting, LLC, 889 F.3d 517, 534 (9th Cir. 2018) (applying *custodia legis* after invoking *ZP Chandon* and explaining that "seamen have traditionally been recognized by maritime courts as the 'wards of admiralty'" (quoting 29 James Wm. Moore et al., *Moore's Federal Practice* § 707.01[12] (3d ed. 2017))).

182. *See* Matter of Topgallant Lines, Inc., 154 B.R. 368, 376 (S.D. Ga. 1993); The J.E. Rumbell, 148 U.S. 1, 19 (1893) ("It would seem to follow that any priority given by the statute of a [s]tate . . . is immaterial, and that the admiralty courts of the United States . . . must give [the maritime lien] the rank to which it is entitled by the principles of the maritime and admiralty law.").

183. *See supra* note 170.

184. *See, e.g.*, Merchs. Nat. Bank of Mobile v. Dredge Gen. G.L. Gillespie, 663 F.2d 1338, 1342 (5th Cir. 1981) (noting that with an arrested vessel, "the engine(s) might rust and freeze up, necessitating costly overhaul[,] . . . the electric equipment . . . was susceptible to corrosion, rust and general deterioration[, and] the hulls . . . and most of the superstructures were subject to rusting, and had not been properly painted").

185. *See* Fed. R. Civ. P. Supplemental Rules for Admiralty and Maritime Claims R. E (9)(a)(i).

186. *See* Melissa K.S. Alwang, Note, *Steering the Most Appropriate Course Between Admiralty and Insolvency: Why an International Insolvency Law Treaty Should Recognize the Primacy of Admiralty Law over Maritime Assets*, 64 Fordham L. Rev. 2613, 2638 (1996) (arguing that an admiralty foreclosure should not be stayed by bankruptcy because the vessel will deteriorate).

187. 11 U.S.C. § 361 (2012); *see* Heller & Hayden, *supra* note 82, at 1216–30 (discussing forms of adequate protection in maritime bankruptcy cases).

188. 11 U.S.C. § 362(d)(1) (2012) ("[T]he court shall grant relief from the stay . . . for cause, including the lack of adequate protection. . . .").

Third, the priority status granted to the bankruptcy estate's expenses that arise after the bankruptcy petition is filed ensures that those providing goods and services to a vessel will be paid. The automatic nature of maritime liens creates an apparent problem in ensuring payment to post-bankruptcy-petition maritime creditors in bankruptcies where the debtor continues to operate. If a vessel is operated after the owner files for bankruptcy, either to wind up business in liquidation or to restructure under chapter 11, then transactions giving rise to new maritime liens will likely occur. The Code prevents the "creation" of new maritime liens without court approval.[189] If the court approves the creation of new maritime liens, they would have priority over earlier maritime liens of the same class under the inverse-order priority of maritime law.[190] This would be unfair to the prior maritime lienors because they were stayed from enforcing their liens. If the court does not approve the creation of new maritime liens, people might be unwilling to extend credit to the vessel, since they would not receive the customary protection, or they might do business expecting a maritime lien but not receive one. Doing business on a cash-only basis would be an extra difficulty for the debtor. On the other hand, it would appear unfair to not grant the customary protection of maritime liens to those providing goods or services to a vessel on credit. This is the fundamental problem that the court in *ZP Chandon* faced: how to treat fairly the crew of a vessel operated post-petition.[191]

The solution of the *ZP Chandon* court—holding that the automatic stay did not apply to maritime liens—was, however, overbroad and unnecessary. The Code deems "actual, necessary costs and expenses preserving the estate" to be administrative expenses.[192] Administrative expenses are priority claims entitled to payment before any other except claims for domestic support obligations.[193] Transactions that would create maritime liens absent the automatic stay are "actual, necessary costs and expenses" for the estate—even maritime torts.[194] They would, therefore, be given administrative priority status. Furthermore, if no one was willing to extend credit to the vessel even with priority status, the trustee may grant a creditor super-priority status, i.e., priority over all other unsecured claims, in order to induce them to do business.[195] With these protections for post-petition creditors, they do not need secured status to receive payment. Additionally, the original reason for maritime liens—to prevent the debtor from being

189. 11 U.S.C. § 362(a)(4) (2012).

190. Walsh v. Placedo Shipping Corp. of Liber (*In re* Pac. Caribbean Shipping (USA), Inc.), 789 F.2d 1406, 1407 (9th Cir. 1986).

191. United States v. ZP Chandon, 889 F.2d 233, 235 (9th Cir. 1989).

192. 11 U.S.C. § 503(b) (2012).

193. 11 U.S.C. § 507(a) (2012).

194. *See* Reading Co. v. Brown, 391 U.S. 471, 485 (1968) (holding that damages resulting from negligence are actual and necessary costs).

195. 11 U.S.C. § 364(c)(1) (2012).

able to escape its debts—is irrelevant in bankruptcy because the bankruptcy court is overseeing the estate preventing a debtor from escaping. Therefore, post-petition maritime liens are unnecessary for creditors. Staying their creation does not harm the later creditors, and it does not endanger the maritime liens of the earlier creditors. This apparent problem is actually fully addressed by the language of the Code, and *custodia legis* is not necessary to resolve it. The Bankruptcy Code fully protects maritime lienors without recourse to any special exceptions for them.

V. SUGGESTIONS FOR THE FUTURE

A. AMEND THE CODE TO EXPRESSLY INCLUDE MARITIME LIENS

In order to make Congress's intention to have vessel foreclosures stayed unmistakable, it should amend the Code so that the definition of lien expressly includes maritime liens. Although the plain reading definition of lien already encompasses maritime liens, the Ninth Circuit based its holdings on the Code's silence about maritime liens.[196] If the Code expressly defined maritime liens as liens, it would be impossible to argue that section 362(a)(4), which prohibits any act to "create, perfect, or enforce *any lien*," does not apply to maritime liens.[197]

Congress should be cautious, however, of the canon *expression unius est exclusion alterius*.[198] Expressly including maritime liens within the definition of lien could be interpreted as excluding other kinds of unusual liens. Congress would need to be clear in the amendment that the mention of maritime liens is not meant to exclude any other kinds of liens from the definition.

B. GIVE BANKRUPTCY JUDGES ARTICLE III STATUS SO THEY CAN ADJUDICATE ADMIRALTY CLAIMS

The appeal of *custodia legis* is that it resolves the admiralty foreclosure for the maritime lienors somewhat faster than a bankruptcy, which is a pressing concern.[199] Part of the delay in bankruptcy comes from the bankruptcy court having to refer the matter back to the admiralty court because Article I bankruptcy judges lack the constitutional authority to adjudicate maritime claims. This is inefficient. Congress could amend the law so that bankruptcy judges have the protections necessary to qualify as

196. *ZP Chandon*, 889 F.2d at 238; Barnes v. Sea Haw. Rafting, LLC, 889 F.3d 517, 532 (9th Cir. 2018).

197. 11 U.S.C. § 362(a)(4) (2012) (emphasis added).

198. "The canon that expressing one item of a commonly associated group or series excludes another left unmentioned . . . ." United States v. Vonn, 535 U.S. 55, 65 (2002).

199. *See* Alwang, *supra* note 186, at 2637–38 (arguing that bankruptcy courts should not interfere with vessel arrest because it delays the process).

Article III judges: lifetime tenure and pay protection.[200] Bankruptcy judges could then adjudicate maritime liens in their own courts, without the delay and burden on the district court.

However, Congress seems unlikely to take this step. When the Code was first passed, Congress declined to make bankruptcy judges Article III judges.[201] After the *Marathon* decision, where the Supreme Court held that parts of the Code granted bankruptcy judges unconstitutional authority,[202] Congress passed the Bankruptcy Amendments and Judgeship Act of 1984 to remedy the law.[203] Although granting bankruptcy judges Article III status would have saved the earlier law, Congress instead made the bankruptcy court a unit of the district court to avoid having to give bankruptcy judges lifetime tenure and pay protection.[204] While this issue of maritime lien adjudication may be too small to motivate congressional action, it is one more reason to support granting bankruptcy judges with Article III status.

CONCLUSION

The Ninth and Second Circuits have upheld, in at least some circumstances, the pre-Code doctrine of *custodia legis*. The Fifth Circuit rejects the doctrine as preempted by the Code. This Note has argued that the Fifth Circuit correctly interprets the Code. *Custodia legis* is contrary to the plain meaning of and intention behind the Code. It prevents the bankruptcy court from accomplishing its goals and does not protect maritime lienors more than the Code alone would. Congress should make its intention to treat maritime liens like any other lien clear by amending the definitions of the Code and should grant bankruptcy judges lifetime tenure so they may indisputably have the authority to conduct admiralty sales.

Ian T. Kitts[*]

200. *See* Tetley, *supra* note 17, at 1143–44.

201. *See id.* at 1140.

202. N. Pipeline Const. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 87 (1982); *cf.* Tetley, *supra* note 17, at 1140–41.

203. *See* Tetley, *supra* note 17, at 1141–44.

204. *See id.* at 1141–42.

* B.A. in Classics, University of Oregon, 2015; J.D. Candidate, Brooklyn Law School, 2020. This note is dedicated to the University of Oregon Department of Classics; to Captain Dennis Stokowski, who helped me get my sea legs; and to Professor Michael Gerber, who introduced me to the world of bankruptcy.