

Cross Border Business Law Blog

Maritime Liens and the Automatic Stay: Impact of the Ninth Circuit's Barnes Decision

on 4.13.18 | Posted in Admiralty Law, Bankruptcy Court, Maritime

Can a Bankruptcy Court order the sale of a vessel “free and clear” of a seaman’s maritime lien for maintenance and cure under Bankruptcy Code § 363? According to the Ninth Circuit’s recent ruling in *Barnes v. Sea Hawaii Rafting*, No. 16-15023 (Mar. 28, 2018), the answer is no: absent a lienor’s consent, only a court sitting in admiralty has the power to extinguish a maritime lien.

A Shipboard Accident Leads to Litigation and Bankruptcy

In *Barnes*, the plaintiff in the court below was the captain of the vessel M/V Tehani, a 25-foot rigid hull inflatable boat used for sightseeing and snorkeling voyages out of Honokohau Harbor in Hawaii. In July 2012, a faulty fuel tank caused an explosion aboard the Tehani, and the captain suffered serious injuries requiring extensive medical treatment. Lacking insurance through his employer, the captain sued the boat’s owner, Sea Hawaii Rafting, LLC (“Sea Hawaii”), and its owner/manager, Kris Henry for maintenance and cure under federal admiralty law, and also sued the Tehani *in rem*. All three defendants answered the plaintiff’s complaint, and the parties proceeded to litigate for some fifteen months.

Shortly before trial, however, Sea Hawaii filed a petition for Chapter 7 dissolution, while its owner Mr. Henry filed an individual petition for reorganization under Chapter 13. The captain’s lawsuit initially was suspended as a result of the automatic stay, but the Bankruptcy Court later granted partial relief from stay to allow the case to continue – but specifically left the stay in effect to “bar the enforcement of any maritime lien.”

Once the Bankruptcy Court partially lifted the automatic stay and the District Court case resumed, the District Court *sua sponte* dismissed the Tehani as a defendant, on the basis that the court lacked *in rem* jurisdiction over the vessel due to procedural defects in the captain’s lawsuit. The captain appealed the dismissal of the Tehani, but while his appeal was pending, Sea Hawaii’s trustee sought and received permission from the Bankruptcy Court to sell the vessel free and clear of liens under Section 363 – and he did just that, promptly selling the Tehani to a new company formed and owned by none other than Sea Hawaii’s owner and co-defendant, Mr. Henry.

The Ninth Circuit Invalidates the Sale of the Tehani

The Ninth Circuit reversed on appeal, ruling as an initial matter that the District Court's conclusion that it lacked *in rem* jurisdiction over the Tehani was in error, and the vessel should not have been dismissed from the case. Perhaps more importantly, however, the Ninth Circuit further held that the Bankruptcy Court's order authorizing the trustee's sale of the Tehani free and clear of the captain's maritime lien *also* was in error, for three reasons:

- First, the Court noted that the automatic stay provision of the Bankruptcy Code "does not expressly refer to maritime liens," which are "sacred liens" entitled to be protected "as long as a plank of the ship remains." The Ninth Circuit already had held in *U.S. v. ZP Chandron*, 889 F.2d 233 (9th Cir. 1989) that maritime liens for seaman's wages were outside the scope of the automatic stay; effectively extending that doctrine, the Ninth Circuit here held that the automatic stay did not bar enforcement of the captain's lien for *maintenance and cure* during the pendency of the bankruptcy proceeding, either.
- Second, the Bankruptcy Court lacked jurisdiction over the captain's lien because the District Court – sitting in admiralty – already had obtained *in rem* jurisdiction over the vessel. Because the District Court had taken "constructive control" of the Tehani upon the filing of the captain's *in rem* lawsuit some fifteen months prior, the subsequent filing of the Bankruptcy petitions could not vest the Bankruptcy Court with the same jurisdiction.
- Third, most critically, the Ninth Circuit ruled that even if the Bankruptcy did have *in rem* jurisdiction over the Tehani, it nevertheless did not have the authority under the Bankruptcy Code to sell the vessel free and clear of the captain's lien. Reasoning that under admiralty law, a maritime lien follows a vessel even into the hands of a bona fide purchaser, and that a maritime lien can only be extinguished through the application of admiralty law, the court ruled that Section 363 of the Bankruptcy Code does not permit a Bankruptcy Court to extinguish a maritime lien. Instead, it could do so only pursuant to the provisions of admiralty law – in other words, by adjudicating the captain's lien claim on its merits.

Under the holding in *Barnes*, it is clear that if a Bankruptcy Debtor's assets include a maritime vessel, care must be taken both by the Court and the Debtor in determining and effecting its disposition. If the vessel is subject to maritime liens – whether for seaman's wages or, after *Barnes*, maintenance and cure – Section 363 will not be available as a tool to strip those liens to facilitate a sale. Instead, the parties must proceed in admiralty to address those liens prior to any sale of the asset.

Tags: automatic stay, Bankruptcy Code § 363, Bankruptcy Court, debtor, federal admiralty law, maritime liens, sale of asset