

## Federated States of Micronesia Admiralty Law

The Federated States of Micronesia (FSM) adopted its Admiralty Law in 1997 and it became Title 19 of the Federated States of Micronesia Code. The government recently amended to 19 FSMC 302 which removed the requirement that a majority of the voyages of a registered vessel must begin or end in the Federated States of Micronesia. The government has also issued maritime regulations, which incorporate and place into effect the provisions of the various international maritime conventions. There have been over 120 ships registered in the FSM.

### *International Conventions*

The FSM has acceded to the SCTW and is on the IMO “White List” and has been found to provide full force and effect to the SCTW provisions.

Although the FSM has not acceded to all the various IMO conventions, the detailed regulations of the FSM Maritime Act have incorporated some of those conventions and instruments which have the force of law in the FSM, such as the following:

1. International Convention for the safety of Life at Sea (SOLAS) 1974, and the 1978 and 1988 protocols;
2. International Load Line Convention (Load Line), 1966
3. International Convention on Tonnage Measurement (Tonnage) 1969
4. International Regulations for Prevention of Collisions at Sea (COLREG) 1972
5. International Convention for Standards of Training, Certification and Watchkeeping of Seafarers (STCW) 1978, as amended in 1995<sup>1</sup>;
6. ILO Convention No. 92 Crews Accommodation
7. Code of Safety for Fishermen and Fishing Vessels, Part B; Safety and Health Requirements for the Construction and Equipment of Fishing Vessels, International Maritime Organization, and the provisions of MARPOL;
8. Voluntary Guidelines for the Design, Construction and Equipment for Small Fishing Vessels;
9. International Convention for the Unification of Certain Rules of Law relating to Bills of Lading, 1924, as amended by the 1968 Protocol; relating thereto, commonly known as the Hague-Visby Rules.

These regulations are patterned after the texts of the various conventions and instruments mentioned above. The regulations themselves are at least five hundred pages in length and cover all details of the system. The proposed ISPS regulations for Maritime Security have been published for public comment.

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### ***FSM Constitution***

The 1997 National Maritime Act is codified in Title 19 of the FSM Code. The national law was enacted by the FSM Congress pursuant to the fact it is a national power described and delegated in the FSM Constitution to the national government.

The FSM Constitution provides in Article I, Section 1 that:

“the territory of the Federated States of Micronesia is comprised of the Districts of the Micronesian archipelago that ratify this Constitution. Unless limited by international treaty obligations assumed by the Federated States of Micronesia, or by its own act, the waters connecting the islands of the archipelago are internal waters regardless of dimensions, and jurisdiction extends to a marine space of 200 miles measured outward from appropriate baselines, the seabed, subsoil, water column, insular or continental shelves, airspace over land and water, and any other territory or waters belonging to Micronesia by historic right, custom, or legal title.”

And Article IX, Section 2(h) expressly delegates to the FSM National Congress the power to “regulate navigation and shipping except within lagoons, lakes, and rivers”. The issue of internal lagoons, lakes and rivers would be governed by state laws to the extent allowed.

The FSM Maritime law is patterned after the established maritime law of nations, as opposed to simply following the statutory precedent from United States jurisdictions. The FSM is a party to and signatory to 1982 Law of the Sea Convention. The FSM has a special maritime agreement with the United States in the treaty commonly known as the Compact of Free Association.

### ***The FSM Supreme Court***

The FSM Supreme Court has jurisdiction over admiralty and maritime disputes and has promulgated “Supplemental Rules for Certain Admiralty and Maritime Claims” which govern the procedures to be used with respect to: maritime attachment and garnishment; actions in rem; possessory, petitory and partition actions; and actions for exoneration from or limitation of liability. These rules provide the applicable rules of procedure to use before the Court for these specific actions.

The FSM Supreme Court has expressly defined the extent of its jurisdiction over maritime disputes, early in the history of this country, specifically rejecting a limited view of only using United States precedent:

The "maritime law" over which this Court has jurisdiction, then, like that of the courts in the United States, is that which has its origins in the codes of seafaring nations of the world and which still is a part of the law of nations. Because the United States courts look to that body of essentially international law in order to define their "admiralty and maritime" jurisdiction, the framers' use of similar language in the FSM Constitution suggests that this Court should employ that same frame of reference. In other words, the maritime jurisdiction conferred on this Court by the Constitution is not to be decided with reference to the details of the United States' holdings in that area, but rather on the basis of this Court's understanding of the general maritime law to which the constitutional provisions, both of this country and of the United States, direct the respective courts of the two nations.

We find therefore that this Court has jurisdiction over all cases which are maritime in nature, or, as Justice Story put it: all maritime contracts, torts and injuries. The latter branch is necessarily bounded by locality; the former extends over all contracts, (wheresoever they may be made or executed, or whatsoever may be the form of the stipulations,) which relate to the navigation, business or commerce of the sea. DeLovio v. Boit, 7 F. Cas. at 444.

Not only is the conclusion of DeLovio appropriate here, but also its underlying policy aims are quite relevant to the Federated States of Micronesia, an island nation with a heavy stake in fishing and shipping. Placing maritime jurisdiction in the national courts ensures uniformity in the development and application of maritime law, an important feature of both national and international shipping and navigation systems. 1 S. Friedell, *Benedict on Admiralty*, § 105, at 7.10 through 7.15 (7th ed. 1988). Story saw the need for uniformity as a strong factor calling for a liberal construction of the jurisdictional grant:

The advantages resulting to the commerce and navigation of the United States, from a uniformity of rules and decisions in all maritime questions, authorize us to believe that national policy, as well as juridical logic, require the clause of the constitution to be so construed, as to embrace all maritime contracts, torts and injuries, or, in other words, to embrace all those causes, which originally and inherently belonged to the admiralty...." *Id.* at 443." Federal Business Development Bank v. S/S Thorfinn, 4 FSM Intrm. 367 (App. 1990).

### ***The Pacific Foods Case***

In addition, the FSM Supreme Court has acted to enforce the rights and obligations of parties under the FSM Maritime Act in a consistent fashion. There was one case in which competing banks with ship mortgages had a dispute over priority. The Court was quick to point out a mistake made by the FSM Registrar in the recording of the mortgages, and explained as follows:

“The statutory scheme sets up a system for the registration of FSM vessels, the recordation of ownership interests in those vessels, the priority of liens and claims against those vessels, and the methods of enforcing those claims. 19 F.S.M.C. 301 *et seq.* The statute provides for a Registrar, appointed by the Secretary of the Department of Transportation and Communications, who will keep a Register of FSM vessels and the instruments that must be deposited with the Registrar. 19 F.S.M.C. 309(1). A transfer of any interest, including a mortgage, in a registered vessel is not valid with respect to that vessel against any person other than the grantor or mortgagor "until the instrument evidencing such transaction is recorded in the Register." *Id.* § 310(1). The Registrar is required to record the particulars in such instruments "as soon as they are received," *id.* § 310(2), including "the amount and date of maturity of any mortgage," *id.* § 310(3)(e). Once a ship is registered, the Registrar must issue a Certificate of Registry for it. *Id.* § 318(1). Once a mortgage has been properly recorded with the Registrar, the Registrar must endorse on the Certificate of Registry the mortgagor's and mortgagee's names, the mortgage's amount and date of maturity, and the time and date the mortgage was recorded. *Id.* § 324. By statute, an earlier recorded mortgage has priority over one recorded later.

Where there is more than one mortgage recorded in the Register in respect of the same vessel, the mortgages shall, notwithstanding any expressed, implied, or constructive notice, be entitled in priority one over the other according to the time and date on which each mortgage was recorded in the Register and not according to the date of each mortgage itself. *Id.* § 326(7). The question of priority is important because if a ship has to be sold either as forfeiture or to satisfy its or its owner's debts, the mortgagees will be paid from the proceeds according to their priority. *Id.* §§ 327(3), 330(2). A mortgagee with a higher priority will thus be paid in full before a subsequent mortgagee with a lower priority is paid one cent. Thus the lower the mortgage priority the more likely it becomes that the mortgage will not be paid in full or perhaps not at all.

As stated above, the priority of the mortgages should be immediately apparent because they will all be recorded on the same Certificate of Registry. If the Department had not performed so poorly in issuing a separate Certificate of Registry listing just the Bank of the FSM's mortgages, that bank would have realized when it went to register its mortgages that they did not have first priority because the Development Bank had registered its mortgage first, and perhaps then taken some other course of action to protect its interests. Protection of creditors

(or of someone contemplating the purchase of the ship) is a purpose of the ship registration system.

The Bank of the FSM acknowledges that the Development Bank's mortgage was first filed but contends that defects, specifically that Pacific Foods actual indebtedness to the Development Bank was for \$100,000 more than the recorded mortgage, in its filing make it invalid. There is no principle of law that prohibits a lender from securing with a mortgage a sum less than the full amount of what it has lent. It merely does so at its own risk. The Development Bank's \$337,184.38 mortgage was properly registered, and it was registered first. The FSM Development Bank's \$337,184.38 mortgage is therefore entitled to the first priority as a matter of law. 19 F.S.M.C. 326(7).

The Bank of the FSM also asserts that the equities of the situation favor it because of what it terms the debtors' fraud in executing mortgages on the vessel *Lady Mae* while claiming that there were no other liens or encumbrances on the vessel. If the Bank of the FSM wishes to pursue a civil fraud charge against any defendant, it may, if it is so advised, move to amend its complaint. Any proposed amended complaint must comply with Civil Procedure Rule 9(b) and state the circumstances constituting fraud with particularity. See Medabalmi v. Island Imports Co., 10 FSM Intrm. 32, 35 (Chk. 2001).

The Development Bank cites cases where minor discrepancies concerning the amount and the maturity date between a mortgage as executed and as recorded did not cause that mortgage to lose its priority. The Development Bank also contends that the "renewal mortgage rule" allows a mortgagee with a first preferred mortgage to rewrite or renew its first mortgage and still retain its priority over subsequent mortgagees because those mortgagees were on notice of the prior mortgage and therefore knew it might be renewed, and the debt and the security were the same. Under this "rule," renewing a mortgage would not extinguish its priority and subordinate it to subsequent mortgages. The Development Bank contends that the court should apply this "rule" and hold that the Development Bank has first priority not only for the \$337,184.38 it registered on December 6, 1999, but also for the full \$437,184.38, which it tried to register on February 3, 2000 as a "correction ship mortgage." This cannot be so. With one exception, all of the United States cases that the Development Bank cites for the validity of the "renewal mortgage rule" involved mortgages that were renewed or rewritten for principal amounts either equal or less than the original mortgage amount. In the exception, Prudential Insurance Co. of America v. S.S. American Lancer, 686 F. Supp. 469 (S.D.N.Y. 1988), *aff'd*, 870 F.2d 867 (2d Cir. 1989), a typographical error caused the first preferred ship mortgage to be recorded for \$92,885 instead of \$92,885,000. However, in S.S. American Lancer, the second mortgage holder at all times, including before and during its loan negotiations, knew of the true amount of the first mortgage and in its own second mortgage specifically subordinated its mortgage to the Prudential Insurance Co.'s first mortgage. Both mortgages were part of a joint refinancing arrangement in which both lenders

participated together. It was not until after the shipowner had been in bankruptcy for over a year that the typographical error was noticed. The court refused to let the second mortgagee to receive a \$92 million windfall for what the second mortgagee knew was a clerical error and when it knew all along that the first mortgage was for \$92,885,000, and had extended its credit based on that knowledge and in the terms of its own mortgage subordinated its mortgage to the \$92,885,000 first mortgage. That is not this case. Not only was the Bank of the FSM unaware of the Development Bank's prior mortgage, or its amount, before it executed its mortgages, but also, because of the Department's failure to properly endorse and issue the *Lady Mae's* Certificate of Registry, was not aware of it until sometime later. (The Bank of the FSM could have been more diligent in searching the records and the *Lady Mae's* file at the Department to determine on December 9, 1999, before it executed the mortgages, whether any prior mortgages were filed there, but considering the Department's failure to properly handle issuance of the Certificate of Registry even that might not have been fruitful and revealed the other mortgage's existence. The Department, however, quite properly refused to register the \$437,184.38 "correction ship mortgage" with a December 6, 1999 date.)

In this case, the Development Bank asks that it be given priority for an additional \$100,000. To do so would destroy the statutory scheme created by Congress. It would mean that anyone contemplating issuing a second mortgage on a vessel could never be sure of the extent of the registered first mortgage's priority ) whether it was actually greater than the recorded amount (and how much greater) and whether it was so large as to make any second mortgage worthless from the start. For example, if a vessel worth about \$400,000 had a recorded first mortgage for \$150,000, the vessel owner might easily obtain more financing, but, if the court followed the interpretation the Development Bank urges it to, a second lender, contemplating lending \$100,000 on the vessel's security could never be sure that the first priority was only for \$150,000 and not for some higher sum, such as \$350,000 that would make its loan insecure. Such a result would destroy one of the goals of the ship registry system) that all ownership interests be recorded on the ship's Certificate of Registry. It would also hinder another purpose and goal) enhancing the ability of ship owners to obtain needed financing. Code provisions must be construed with a view to effect their object. 1 F.S.M.C. 211. Thus, without deciding if the FSM statutory scheme for ship registration would ever allow the application of the "renewal mortgage rule," the statute prohibits its application in the manner the Development Bank wants it to be applied in this case. A mortgagee cannot assert that its registered mortgage has priority over a subsequent mortgagee for a principal amount greater than the principal amount registered.

The Development Bank therefore has first priority only for its \$337,184.38 mortgage registered December 6, 1999. The Bank of the FSM has second priority for its three mortgages registered December 10, 1999. The Development Bank may, if it so chooses, register Pacific Foods's additional \$100,000 indebtedness to

it, but such registration shall not cause that indebtedness to take priority over the Bank of the FSM mortgages registered December 10, 1999.

Bank of the FSM v. Pacific Foods & Services., Inc. 10 FSM Intrm. 327 (Pon. 2001).

This case demonstrates that the FSM Supreme Court will step in and correct any deficiencies and will enforce the rights and obligations of competing interests with regard to FSM registered vessels. Since that case was decided, the FSM has upgraded its Registry, appointed a Registrar with extensive training and capabilities, and has registered over 100 ships.

***Report of one Attorney working in Micronesia:***

“I have represented lending institutions and vessel owners from Singapore, the Solomon Islands, the United States, France, Spain, Venezuela, China, Korea, Taiwan and Panama with regard to vessel registration and deletion, recordation of mortgages and discharges of mortgages, and maritime collisions at sea. I have deleted vessels from registries in Panama, Solomon Islands, Belize, Mauritius, and the United States for flagging here in the FSM at various times over the last eight years. I have represented a Chinese vessel involved in a maritime collision and death of a seamen with a Japanese flagged vessel in international waters. I have represented maritime insurers and insureds in handling of foreign crew claims on FSM flagged vessels. I have also represented the State of Pohnpei in a major oil spill from a foreign flagged vessel in the internal waters of the State of Pohnpei. As in most jurisdictions, the clients usually try to avoid engaging these matters into the courts. But in those matters that I have handled before the courts of the FSM, I can provide the legal opinion that the courts here view the maritime law as a priority and see the enforcement of the maritime laws in a consistent and fair manner as a priority for this nation. This nation is a maritime nation, a nation of a million square miles of ocean. The courts here will properly and consistently enforce the rights and obligations of the parties to any maritime dispute by applying the FSM maritime law and applicable international law.”

***Summary***

The maritime registration system currently in place has integrity and is reliable in its management and implementation.