

On the Ownership of Ships under Construction in Chinese Law

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Abstract: In the face of increasingly complex legal issues, the Chinese shipbuilding industry still requires robust legal and policy support to strengthen its core competitiveness. Presently, the provisions concerning the ownership of vessels under construction and related matters in China's Maritime Law are ambiguous, leading to varying claims regarding the legal nature of shipbuilding contracts and inconsistent conclusions in judicial practice. This article suggests employing the principle of autonomy of the will as a guiding framework, acknowledging the intricacy of shipbuilding contracts and the distinct nature of vessels under construction. By doing so, it aims to uncover the genuine intentions of the parties involved in shipbuilding contracts and ascertain the ownership of vessels under construction. This clarification would not only be beneficial for the involved parties, but also help advance China's policy objective of becoming a "marine power".

Keywords: Ownership of Ships Under Construction; The Principle of Autonomy of Will; The Shipbuilding Contracts

1. Introduction

Although China's Maritime Code clearly outlines the mortgage rights of ships under construction, there is a notable absence of explicit regulations concerning ownership and related matters for such ships^[1]. Thus, the objective of this article is to examine various theories pertaining to the nature of shipbuilding contracts, comprehend the distinctiveness of the shipbuilding process, and propose recommendations for determining the ownership of ships under construction based on the principle of autonomy of will.

2. Judicial Practices on the Attribution of Ownership for Ships under Construction

The Maritime Law of the People's Republic of China lacks specific provisions and clear determinations for shipbuilding contracts. In the judicial process, courts primarily determine the nature of the shipbuilding contract, whether it is a contract of sale or a contract for work, in order to ascertain the ownership attribution. Historically, Chinese shipyards have often chosen to apply the English Sale of Goods Act 1979 in international shipbuilding contracts, considering them as sales contracts, and opted for London arbitration to resolve disputes^[2].

3. Different Theories on the Nature of Shipbuilding Contracts

3.1 The Doctrine on the Contract for Work and its Evaluation

The primary objective of determining the contractual legal nature is to establish the extent to which contractual provisions and mandatory rules apply. The doctrine on the contract for work asserts that a shipbuilding contract encompasses not only the transfer of ownership but also emphasizes the completion of work results, such as specifying ship parameters and adjusting prices. Its essence lies in the construction work rather than solely the transfer of ownership, thereby categorizing its nature as a contract for work. In some countries within the continental legal system, such as Germany, shipbuilding contracts are categorized as contracts for work. Consequently, when addressing associated disputes, the applicable provisions are those outlined in Article 651 of the German Civil Code.

In China's legal system, judicial practice typically addresses such matters based on the provisions outlined in Article 770 of the Civil Code. A contract for work refers to an agreement aimed at achieving specific work results. In this type of contract, the party commissioning the work (referred to as the "Commissioning Party") requests the contractor to provide materials and requires the contractor to carry out inspections and remedies as agreed. Simultaneously, the contractor is obligated to accept the Commissioning Party's supervision and inspection.

When a shipbuilding contract is categorized as a contract for work, if the builder provides the materials, they retain ownership of the constructed object. However, if the Commissioning Party supplies the materials, and the builder adds value through craftsmanship and labor,

the determination of ownership is based on the rules of processing. Specifically, if the value of the processed product is lower than the value of the materials, ownership belongs to the Commissioning Party. Conversely, if the value of the processed product exceeds the value of the materials, ownership belongs to the builder.

Although the doctrine on the contract for work has certain advantages in explaining the nature of shipbuilding contracts, there are also some shortcomings. In cases where the employer and contractor jointly provide materials, particularly when it is difficult to differentiate the attribution of the main components, the attribution of ownership of the resulting product still needs to be determined based on agreements and interpretations. Solely emphasizing the view that the builder possesses ship ownership may not fully reflect the intent and background of the contract and may lead to the employer's inability to effectively protect their rights after delivery.

3.2 The Doctrine on the Contract of Sale and its Evaluation

Another perspective classifies shipbuilding contracts as sale contracts, where the shipyard, acting as the seller, holds ownership of the ship under construction until delivery is completed, at which point the buyer acquires ownership. English law distinguishes the legal provisions applicable to sale contracts from those governing contractor contracts. Contracts involving the provision of goods and services are governed by the Sale of Goods and Services Act and common law rules, while sale contracts are regulated by the Sale of Goods Act and its amendments^[3]. Building on this rationale, Lord Justice Romer of the English Court of Chancery concluded in a case that shipbuilding contracts fall within the purview of contracts defined in the Sale of Goods Act 1983, thereby possessing the characteristics of sale contracts^[5].

Considering shipbuilding contracts as contracts for the sale of goods is a relatively specific viewpoint within English law. However, in the unfortunate event of the builder's bankruptcy without a mortgage or third-party guarantee, the buyer's claim against the builder is treated as an ordinary claim in the bankruptcy proceedings. Consequently, the buyer can only recover a proportionate amount, resulting in an inability to fully recoup their investment. Unless explicitly stipulated prior to vessel delivery, ownership during the construction period remains with the builder. This signifies that even if the buyer has covered the construction costs, the vessel remains the property of the builder, and the buyer lacks the right to reclaim ownership or exercise control over the vessel's use and operation. Such implications can lead to substantial economic losses for the buyer and increase uncertainty and risk in commercial and operational aspects.

4. The “Agreement Theory” of Shipbuilding Contracts

4.1 The “Agreement Theory”

Theoretical distinctions between contracts of sale and contracts for work, although provided, cannot be directly applied in judicial practice due to the complexities inherent in shipbuilding contracts. When determining ship ownership during the construction of a vessel in a shipbuilding contract, the primary consideration should be the expressed intentions of the parties involved.

Therefore, this paper proposes the “agreement theory”, which upholds the principle of autonomy of will and emphasizes the significance of specific contractual provisions that reflect the genuine intentions and commercial considerations of the parties involved. Particularly in commercial activities, in order to uphold autonomy, the law must exhibit greater respect for the agreed-upon content^[5].

The parties' intent holds substantial weight when interpreting contract terms. Courts are tasked with inferring the parties' intentions through an analysis of their communications, negotiation records, the background and purpose of the contract, and other relevant factors. This may entail reviewing oral agreements, written correspondence, email communications, as well as examining the parties' actions and statements prior to and following the contract's signing. This approach helps strike a balance between the interests of both parties.

4.2 Comparative analysis of different theories

Classifying shipbuilding contracts strictly as either contracts for work or contracts for work fails to resolve issues and instead introduces new complexities. Compared to the perspectives of the doctrine on the contract of sale and the contract for work, the “agreement theory” prioritizes the legal agreement, genuine intent, and protection of the parties' rights within a contract, avoiding rigid interpretations. Uphold-

ing the principle of freedom of contract, parties have the autonomy to enter into agreements that align with their own desires and negotiate contract terms that reflect their intentions. In judicial practice, courts typically rely on the parties' authentic expressions of intent, rather than the contract's name and terminology, to classify or determine the nature of specific contracts. They consider whether the contract fits into a particular type of typical contracts or combines elements from multiple typical contracts to establish the applicable legal norms^[6]. The content of contractual provisions carries greater significance than the classification of contract nature. Recent Chinese court cases demonstrate a noticeable shift towards analyzing the contractual content directly to ascertain the parties' agreement on ship ownership, rather than overly focusing on the classification of shipbuilding contracts. This approach has garnered support from numerous scholars as well.

5. Conclusion

In practice, the key factor to consider is whether the parties have reached a consensus regarding ship ownership. Once the parties have clearly established agreements regarding the ownership of the ship under construction, their agreement should be upheld based on the principle of autonomy of will.

Dragon Pearl Night Club Restaurant Ltd v. Leung Wan Kee Shipyard Ltd, exemplifies this principle. In this case, the court determined that in the absence of explicit provisions regarding ship ownership in the contract, it is essential to interpret the contract reasonably and establish ownership based on the parties' expressed intentions. In situations where there is no explicit expression of intention, the parties' intentions can be inferred through various means, such as examining relevant materials, ship design, and overseeing the construction process, which aid in determining the purpose and essential characteristics of the contract.

In conclusion, the determination of ship ownership in a shipbuilding contract hinges upon the explicit provisions and agreed-upon conditions outlined within the contract. If the contract unambiguously stipulates the ownership of the vessel, it should be adhered to accordingly. However, in cases where the contract lacks explicit provisions regarding ownership, additional factors such as the parties' intentions and industry customs come into play to establish the most reasonable attribution.

References

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