

MARINE
M O N E Y

ACADEMY

PRESENTED BY:
Holland & Knight

NEW YORK
2022

Documenting a Ship Financing Transaction

Jovi Tenev, Partner, Holland & Knight
Gerald Morrissey, Partner, Holland & Knight
Rich Furey, Partner, Holland & Knight

THE TYPICAL CHAIN OF EVENTS AND CONTRACTS



• LETTER OF INTENT

- Confirmation by parties to be interested to enter into a transaction
- Binding or non binding? Obligation to act in good faith?
- Exclusivity element
- Jurisdiction Clause and Governing Law Clause

Exchanging
first ideas



NON-DISCLOSURE AGREEMENT

(sometimes called a confidentiality agreement)

- Binding Agreement to keeps things confidential
- Addressees
- Consequences in case of breach
- Term
- Jurisdiction Clause and Governing Law Clause

Legal negotiations
of NDA



TERM SHEET

- Summary of major terms
- Please, not too many details (5 - 10 pages)
- Binding or “subject to contract”?
- Timeline

Commercial
negotiations

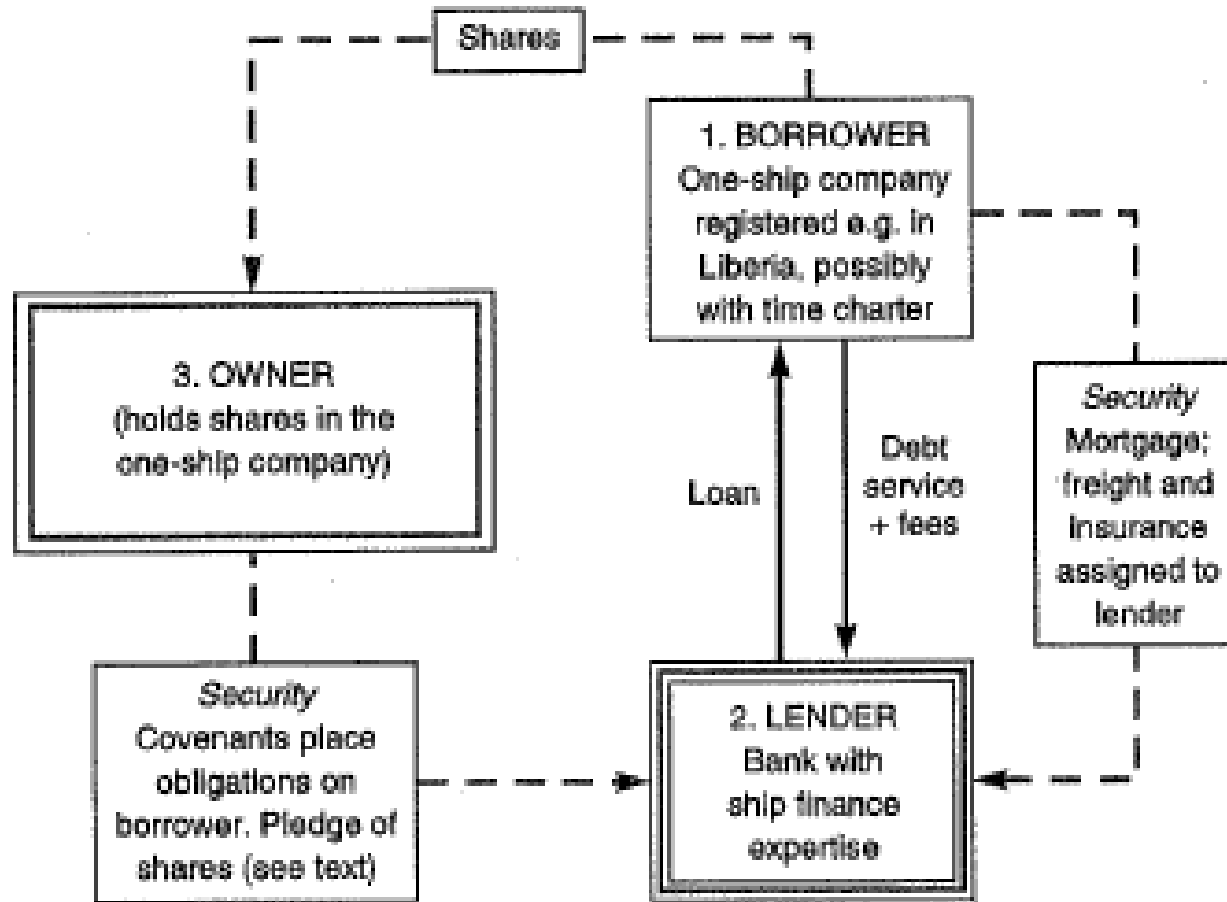


DOCUMENTATION

- Binding, detailed contracts
- Security documents and exhibits

Detailed commercial and
legal negotiations

MORTGAGE BACKED LOAN



Single Ship Financing

- Relies on ship and other collateral for security
- Borrower owns one ship (Special Purpose Co.)
- Parent guarantees loan and pledges shares
- Vessel flagged in legally acceptable jurisdiction

Multiple Ship Owning Borrower

- Parent company or an intermediate subsidiary acts as borrower
- Ship-owning SPCs grant ship mortgage and “upstream” guarantees

LOAN AGREEMENT – BASIC ANATOMY

- Economics: Amount; Term; Interest Rate; Fees
- Amortization; Prepayment (Mandatory Events; Voluntary) & Commitment Cancellation
- Conditions Precedent and Utilization
- Market Disruption; Increased costs; Taxes and Indemnities
- Events of Default; Acceleration & Remedies
- Proceeds Waterfall
- Agent/Security Trustee Role; Protection and Appointment
- Transfer Provisions
- Choice of Law (typically English or NY); Dispute Resolution (Courts or Arbitration)

SHIP MORTGAGE

- In US: normally a unilateral instrument; shipowner grants to mortgagee a mortgage covering the ship
- US legal requirements: (i) identify vessel; (ii) mortgagor name/address; (iii) amount of debt; (iv) signed, etc.
- Description of indebtedness/obligations secured?
- Attach as exhibits the promissory note/loan agreement?
- Representations & Warranties: (i) shipowner's existence and good standing; its status as a U.S. citizen; its power and authority to own and mortgage the vessel; authorization to enter transaction; no liens other than "Permitted Liens"
- Covenants: Maintenance of Insurance including:
 - Marine risk hull & machinery – amounts to be paid in the event the ship suffers a partial/total loss
 - Protection and indemnity insurance - coverage against claims asserted by third parties for damages suffered (including collision) not covered by hull insurance

SHIP MORTGAGE (Con't)

- Covenants: Liens
 - Crew members, repairmen, suppliers of bunkers and other necessities and others who deal with ship on routine business acquire maritime liens on the ship as a matter of law; several provisions deal with this to preserve mortgagee's preferred status:
 - 1. Restrict mortgagor's authority restricted of liens for crew wages or salvage:
 - *"None of the Shipowner, any charterer, the Master of the Vessel or any other person has or shall have any right, power or authority to create, incur or permit to be placed or imposed or continued upon the Vessel any lien whatsoever other than for crew's wages and salvage and the lien of this Mortgage."*
 - 2. Notice to potential lienholders:
 - *"The Shipowner will place, and at all times and places will retain, a properly certified copy of this Mortgage on board the Vessel with her papers and will cause such certified copy to be exhibited to any and all persons having business therewith which might give rise to any lien thereon other than liens for crew's wages and salvage, and to any representative of the Mortgagee;..."*

SHIP MORTGAGE (Con't)

- Covenants: Liens (Con't)
 - 3. Covenant against liens over 30 days; notify mortgagee of court proceeding:
 - *“Except for the lien of this Mortgage, the Shipowner will not suffer to be continued any lien, encumbrance or charge on the Vessel, and in due course and in any event within thirty (30) days after the same becomes due and payable or within fourteen (14) days after being requested to do so by the Mortgagee, will pay or cause to be discharged or make adequate provision for the satisfaction or discharge of all claims or demands, or will cause the Vessel to be released or discharged from any lien, encumbrance or charge therefor.”*
 - *“If a libel or complaint be filed against the Vessel or the Vessel be otherwise attached, levied upon or taken into custody by virtue of any legal proceeding in any court, the Shipowner will promptly notify the Mortgagee thereof by cable or telex, confirmed by letter, at its address, as specified in this Mortgage, and within fifteen (15) days will cause the Vessel to be released and all liens thereon other than this Mortgage to be discharged and will promptly notify the Mortgagee thereof in the manner aforesaid. The Shipowner will notify the Mortgagee within forty-eight (48) hours of any average or salvage incurred by the Vessel”*

SECURITY INTEREST IN EARNINGS

Ships are employed under a variety of types of charters and contracts:

- bareboat / demise charter – possession/control transferred to charterer who crews and operates the ship during the charter period
- time charter -- use of the ship for an agreed period of time and hire is paid on a periodic basis, usually monthly or semimonthly (no transfer of possession/control)
- voyage charter -- ship engaged to carry cargo on a specific voyage and the basic earnings are in the form of freights (no transfer of possession/control)
- A consecutive voyage charter or a contract of affreightment, under which payments are based on movement of agreed quantities of cargo, may also be assigned as collateral

Assignment of Earnings and Charters:

- the borrower assigns to the lender, all its right, title and interest in and to the charter party;
- ***“including the right of the owner to perform the charter”*** -- requires the consent of the charterer

SECURITY INTEREST IN INSURANCE PROCEEDS

- Lender will require that it be named as a *loss payee* in the insurance policies
 - Loss payee clause names a person to whom the insurance proceeds are to be paid if a loss occurs
 - subject to the proviso that until the lender notifies the underwriter to the contrary, all or certain losses may be paid directly to the shipowner
- If possible, Lender will want to be a named *assured* (with a waiver of premium liability) as well as a loss payee. By becoming a named assured, the lender becomes a party to the insurance contract, a status that is higher than that of a loss payee or third party beneficiary
- Another means by which the lender obtains rights in insurance is by taking an assignment of insurance.
 - Similar to being named an assured, under an assignment the assignee is entitled to sue on the policy in its own name
 - An assignment particularly may be useful with respect to insurances not in place at the time the loan is made.

SECURITY INTEREST IN REQUISITION PROCEEDS

- In US, Merchant Marine Act of 1936 provides that the government may requisition title to, or use of, vessels owned by United States citizens, during any national emergency, or following proclamation by the President that the security of the national defense makes it advisable
- Shipowner is entitled to "just compensation" for the title to or use of the property
- Statute provides for the recognition of valid mortgage claims against the ship and a means for securing the payment of such claims to the mortgage holder

OTHER COMMON COLLATERAL & CREDIT SUPPORT

- Guarantees – upstream; downstream
 - Frequent component in ship financings but not collateral;
 - An unsecured obligation of guarantor unless pledges its assets to support the guaranty
 - Enforcement of guaranty is open to variety of defenses
- Share pledges
- Account control agreements
- Assignment of shipbuilding contracts and related documents

LEASE FINANCING DOCUMENTATION

- “Bareboat charter” or “Demise charter”
 - Ship owner transfers to bareboat charterer use, control, crewing, maintenance, operation, insurance, and all other aspects of vessel operations
 - Owner reserves rights to receive hire ("rent") payments during the bareboat charter period and to have possession of the vessel returned to it at the end of the bareboat charter period
- Key provisions
 - Hell-or-high-water Clause
 - Operational control
 - Maintenance
 - Operational and tax indemnification by charterer
 - Regulatory & legal compliance
 - Assignments by owner

CHOICE OF LAW & FORUM; DISPUTE RESOLUTION

- US vs English vs Local Law
- Forum selection
- Recognition of foreign judgments
- Courts vs Arbitration
 - Speed vs. Compromise / Public vs. Private
 - Recognition of foreign arbitration awards

FLAG & REGISTRATION

WHY MUST SHIPS FLY THE FLAG OF A STATE?

- Art 87 UNCLOS (Freedom of the High Seas)
 - Freedom of navigation
 - Legal vacuum on the high seas

“The high seas are open to all States, whether coastal or land-locked...”

- Art 94 UNCLOS (Duties of the Flag State)
 - Flag determines which law applies on board of a ship

“Every State shall effectively exercise its jurisdiction and control in administrative, technical and social matters over ships flying its flag.”

- Art 91 para 1 UNCLOS (Nationality of Ships)

“There must exist a genuine link between the State and the ship.”

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WHICH FLAG TO CHOOSE?

Two types of ship registers: operated by the State or operated by a private organization for a State

LEGAL ASPECTS

- Safe legal environment
- Tax aspects
- Contractual aspects (lenders' requirements)

COMMERCIAL ASPECTS

- Registration fees
- International treaties re port dues

OPERATIONAL ASPECTS

- Internationally accepted flag
- Well functioning registry
- Customer orientated
- Ideally 24/7 reachable

POLITICAL ASPECTS

- Politically accepted and acceptable state and flag

CONCLUSION

QUESTIONS?

Jovi Tenev, Partner, Holland & Knight, +1 212 513 3218 Jovi.Tenev@hklaw.com

Gerald Morrissey, Partner, Holland & Knight, +1 202 469 5497 Gerald.Morrissey@hklaw.com

Rich Furey, Partner, Holland & Knight, +1 212 513 3439 Richard.Furey@hklaw.com