

SHIP FINANCE

United Kingdom



Ship Finance

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Quick reference guide enabling side-by-side comparison of local insights into ship finance issues, including in each jurisdiction due diligence; repayment; registration of vessels; ship mortgages and other liens over vessels; collateral; tax considerations for vessel owners; insolvency and restructuring considerations; and recent trends.

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DUE DILIGENCE

Demonstrating title or legal ownership

How does one demonstrate title to or legal ownership of a vessel registered under the laws of your jurisdiction?

For a standard fee of £29, or £79 for the premium service with 24-hour turnaround, a transcript of a vessel's entry in the registry is available from the Registry of Shipping and Seamen. This transcript will show details of the ship, the name and address of the current ownership and division of ownership of shares in the ship, and details of any mortgages over the ship.

Law stated - 21 April 2023

Liens

How can one determine whether there are any liens recorded over a vessel?

The transcript of registry only shows any mortgages registered over a ship. Liens do not need to be registered under English law.

Law stated - 21 April 2023

How does one determine whether there are any security agreements, liens, charges or other encumbrances granted by a vessel owner or affiliated party who might be a borrower, guarantor or other credit party in connection with a vessel finance transaction?

A transcript of registry will demonstrate whether a mortgage has been granted over the ship and registered. However, unregistered mortgages are possible.

If the shipowner is a company registered in the UK (references throughout this chapter to companies registered in the UK will, in most cases, also apply to UK incorporated limited liability partnerships), a search of the Companies House register for the relevant part of the UK will reveal any fixed or floating charges granted by the shipowner and registered.

A writ search can be carried out at the Admiralty and Commercial Court for a fee of £11 to determine whether any claims have been commenced against the ship. This will demonstrate any encumbrances over the ship.

Law stated - 21 April 2023

Public registry searches

Can one determine whether an obligor registered in your jurisdiction is duly organised and in good standing from a search of a public registry?

A search on the Companies House website will show key information such as the registered office, date of incorporation, insolvency actions registered against the company and key future filing dates. Company accounts and annual returns can also now be accessed free of charge. However, the accuracy of Companies House data is reliant on companies making filings.

Good-standing certificates can be ordered from Companies House. A good-standing certificate will state that a company has been in continuous, unbroken existence since its incorporation and that no action is currently being taken

to strike the company off the register. An incorporation certificate can also be requested, certifying the names of directors, the secretary and company objects. You can no longer order certificates with information on shareholders, shareholdings or statement of capital.

A search of the Insolvency and Companies List (formerly known as the Bankruptcy and Companies Court) will determine whether any proceedings have been lodged against a company. This can be done online (although an account must be created) or by telephone.

Law stated - 21 April 2023

Can the shareholders or other equity interest holders, directors and officers or other authorised signatories of an obligor organised in your jurisdiction be determined from a search of a public registry? If not, how are these parties customarily identified?

Details of a company's directors, officers, secretary and shareholders will be listed on the company's confirmation statement, which can be requested from Companies House. Companies House also maintains an accessible register of company secretaries and directors, and companies are required to make filings upon a change of any director or secretary for the purposes of this register. However, the accuracy of Companies House data is reliant on companies making the required filings in a timely manner.

Companies are also required to keep a register of directors and a register of shareholders, which must be kept at the company's registered office or at a single alternative inspection location. Any person is entitled, on payment of a prescribed fee (currently £3.50 per hour), to inspect these registers. Since 30 June 2016, a private company has been able to choose to send information usually kept in all or any of certain statutory registers to the registrar of companies to be kept on the public registrar at Companies House rather than keep the statutory registers at its registered office.

The register of shareholders maintained by the company and the annual return will identify only the registered shareholders. They will not identify whether the registered shareholder is holding them as a nominee for another, nor describe any equitable interests that exist. However, on 6 April 2016, legislation came into force to facilitate transparency as to the ultimate beneficial owners of UK companies whereby most companies (with certain exceptions) must keep a register of 'persons with significant control' (PSC) over that company, and, from 30 June 2016, it also became necessary to file such details with Companies House. For newly incorporated companies, a statement of initial significant control must now be filed at Companies House as part of the application for registration. As from 26 May 2015, the use of bearer shares in UK companies was prohibited. Any person is entitled to review a company's PSC register free of charge and companies must provide copies on request – at a maximum charge of £12 for each copy.

Law stated - 21 April 2023

Debt obligation

What corporate or other entity action is necessary for an obligor to enter into or guarantee a debt obligation? When is action by the board of directors or other governing body required? Must shareholders approve a guarantee?

Entry into a debt obligation or guarantee must be duly authorised by the appropriate corporate action. Typically, this will be by means of a resolution of the board of directors, although the board may delegate powers to individual directors or others to enter into such obligations on behalf of the company. A shareholders' resolution is not usually required for either guarantees or loans unless the loan is made to a director or the guarantee is given on his or her behalf. Shareholder approval may also be appropriate if the directors have doubts as to whether a transaction is of benefit to the company and, therefore, if the transaction would be a proper exercise of their powers.

The company's articles of association or other constitutional documents may place restrictions on the giving of guarantees or impose procedures that must be followed in order to authorise the entry into a debt or guarantee obligation, but (subject to exceptions relating to transactions involving directors) in favour of a person dealing with a company in good faith, the power of the directors to bind the company, or authorise others to do so, is deemed to be free of any limitation under the company's constitution (section 40, Companies Act 2006).

Law stated - 21 April 2023

Obligations of foreign lenders

Must foreign lenders qualify to do business in your jurisdiction to extend credit to a borrower organised in your jurisdiction? Will foreign creditors be deemed resident as a consequence of making a loan or other extension of credit to an obligor within your jurisdiction?

Foreign banks or other lenders do not need to seek UK regulatory approval to extend credit to a UK company, and there are no exchange controls in place that would restrict payments from a UK company to such foreign lenders. Corporate lenders will not be deemed UK-tax resident unless they are incorporated in the UK or are centrally managed and controlled here. A non-resident company that trades through a UK permanent establishment is liable to pay UK corporation tax on the profits arising from that permanent establishment. Payments of principal are not subject to UK withholding tax. However, payments of interest by a UK-based borrower to a foreign lender are subject to a 20 per cent withholding tax at source.

Law stated - 21 April 2023

REPAYMENT

Central bank and regulatory approval

Is central bank or other regulatory approval required for repayment of a loan in foreign currency?

Regulatory approval is generally not required for repayments of a loan in foreign currencies. This is subject to any international sanctions that may be applicable to the currency in question. Anti-money laundering and antiterrorism regulations will also need to be complied with.

Law stated - 21 April 2023

Usury laws

Do usury laws limit the interest payable to a lender in respect of a vessel financing?

Lenders granting loan facilities governed by English law need to exercise caution when setting the rate of interest payable if the borrower is in default of its obligations. General English law contractual provisions will apply, including common law rules on clauses deemed to be a penalty and, therefore, unenforceable. Whether a clause setting out the default rate of interest would be deemed to be a penalty would be decided by the courts on a case-by-case basis; however, there are established case law principles to follow, for example:

- the courts have recognised that a lender has a legitimate commercial interest in applying a higher rate of interest to a borrower who is in default because of the increased credit risk which that borrower represents (Cargill International Trading PTE Ltd v Uttam Galva Steels Ltd [2019] EWHC 476 (Comm));
- default interest can only be charged while the default is continuing unremedied (see Lordsvale Finance plc v Bank

of Zambia [1996]);

- the rate must not be obviously extravagant, exorbitant or unconscionable (relevant factors would include whether the rate is too high by comparison with market rates or any applicable statutory rates and the extent to which the parties are sophisticated or experienced commercial persons bargaining with the benefit of legal advice) (see *Cavendish Square Holding BV v El Makdessi* [2015] and *ParkingEye Ltd v Beavis* [2015]); and
- as a rough rule of thumb, a default rate of twice the normal contractual rate where the lender has the benefit of security for the loan, would be likely to shift the evidential burden on to the lender to demonstrate that the default rate was justifiable (see *Ahuja Investments Ltd v Victorygame Ltd* [2021]).

Default rates of between 1 and 2 per cent per annum above the contractual rate of interest applicable to the loan facility in question are common market practice in English law ship finance loan agreements.

Law stated - 21 April 2023

Withholding taxes

Are withholding taxes payable on principal or interest payments to non-resident lenders?

Payments of principal are not subject to UK withholding tax. However, payments of interest by a UK-based borrower to a foreign lender are subject to a 20 per cent withholding tax at source.

This withholding tax rate may be eliminated or reduced under the terms of a double taxation treaty, and the lender would need to make a formal application to the UK tax authority (HMRC) for approval to receive interest gross. If HMRC has not yet approved the payment of interest without withholding tax, the borrower must continue to deduct 20 per cent from its interest payments (although if the application is granted, this can be reclaimed). Post-Brexit, the UK has a double taxation agreement with every EU member state. The terms of the UK's double taxation agreements can be found in the Double Taxation Manual, published by HMRC.

Previously, the EU Interest and Royalties Directive may have been relied on to eliminate or reduce the rate in respect of payments to EU lenders. However, the directive ceased to apply following the expiry of the Brexit transition period on 31 December 2020. Legislation that continued to exempt relevant payments of interest after the end of the Brexit transition period was repealed by the Finance Bill 2021 on 1 June 2021. As such, there is now no exemption to withholding taxes on payments of interest by a UK-based borrower to a foreign lender (unless covered by a double taxation agreement).

In ship finance transactions, lenders will typically require that a tax gross-up clause be included in the loan documentation.

Law stated - 21 April 2023

REGISTRATION OF VESSELS

Eligibility for registration

What vessels are eligible for registration under the flag of your country? Are offshore drilling rigs or mobile offshore drilling units considered vessels under the laws of your jurisdiction? What is the effect of registration?

The UK Ship Register (the Register), which is maintained by the Maritime and Coastguard Agency (MCA), is split into four parts depending on the type of ship:

- Part I – merchant vessels and pleasure vessels or large yachts over 24 metres;
- Part II – fishing vessels;
- Part III – Small Ships Register for ships under 24 metres; and
- Part IV – bareboat charters of foreign-flagged vessels that are chartered on bareboat charter party terms by a charterer.

A ship may not be registered in more than one part of the Register and the MCA does not permit the registration of ships under construction.

The Merchant Shipping Act 1995 provides that 'ship' includes every description of ship used in navigation (section 313). It is unclear under English law whether offshore drilling rigs or mobile offshore drilling units would be classified as 'ships'. It is important whether such structures are classified as ships or not because the regulatory regimes that apply to ships are different from those that apply to non-ship structures.

There are no age restrictions on ships registered with the Register. However, ships over 15 years old must be approved by the MCA's technical experts before they can be registered.

The MCA has the power to refuse to register or terminate the registration of a ship, even if it is eligible for registration, on the grounds that 'having regard to any relevant requirements' it would be inappropriate for the ship to be or to remain registered (section 9 of the Merchant Shipping Act 1995) – for example, if the ship does not comply with environmental or safety requirements.

There is no legal requirement to register a ship under the UK flag. However, an owner will usually register a ship so that jurisdiction can be established over the ship. International law provides that all ships using the high seas must possess a national character. Registration will also provide evidence of the ship's nationality, confer the right to fly the national flag and provide the right to naval protection, diplomatic protection and consular assistance. It will also provide prima facie evidence of the title of the registered owner and of registered mortgages. From a lender's perspective, registration is required in order to ensure that a mortgage can be registered against the ship on the Register, thereby enabling mortgagees to protect their interest.

Law stated - 21 April 2023

Who may register a vessel in your jurisdiction?

The ownership of a UK ship is divided into 64 shares. The Merchant Shipping Act 1995 provides that, in order to be registered as a UK ship under Part I of the Register, at least 33 of the shares (the majority interest) in the ship must be owned by persons or a company qualified to own UK ships (a qualifying owner). Following the enactment of the Merchant Shipping (Registration of Ships) (Amendment) (EU Exit) Regulations 2019, eligibility to register a ship on the UK Registry has been extended to include Commonwealth citizens and countries, to persons settled in the UK and to citizens and companies of a specific selection of countries (as listed in Schedule 6 to the regulations). To be a qualifying owner the persons or company must fit into one of the following categories:

- British citizens;
- British Dependent Territories citizens;
- British citizens living overseas;
- citizens of an EU member state exercising their rights under articles 48 or 52 of the European Economic Community Treaty or article 28 or 31 of the Agreement on the European Economic Area in the UK;
- persons who under the British Nationality Order 1981 are British subjects;
- persons who under the Hong Kong (British Nationality) Order 1986 are British Nationals (Overseas);

- companies incorporated in one of the European Economic Area (EEA) countries (including UK-incorporated limited liability partnerships) with a place of business in the UK;
- companies incorporated in a British overseas possession having their principal place of business in the UK or in that overseas possession; and
- European economic interest groupings registered in the UK immediately before EU exit day (UKEIGs);
- Commonwealth citizens;
- a UK local authority;
- bodies corporate incorporated in a Commonwealth state;
- non-British nationals who are settled in the United Kingdom; and
- citizens of and bodies corporate incorporated in any of the Schedule 6 countries: Argentina, Aruba, Bahrain, Brazil, the Canary Islands, China, the Faroe Islands, Haiti, Israel, Japan, Liberia, Madeira, the Marshall Islands, Monaco, Panama, South Korea, Switzerland, Suriname, the United Arab Emirates and the United States of America.

Where more than one qualifying owner of the ship is resident in the UK, one of the qualifying owners will be appointed the managing owner of the ship and will receive all correspondence from the MCA.

If none of the qualified owners are resident in the UK, a representative person must be appointed who may be either an individual resident in the UK or a company incorporated in one of the European Economic Area countries with a place of business in the UK.

There are additional requirements for registration of fishing vessels and small ships.

All applications for registration shall be made to the Registrar at the Registry of Shipping and Seamen. Registrations can be made in person or by post and must be supported by a declaration of eligibility in the approved form, which shall include a declaration of British connection, a declaration of ownership by every owner setting out his or her qualification to own a British ship, and a statement of the number of shares in the ship, the legal title of which is vested in each owner.

Law stated - 21 April 2023

Registry for international shipping operations

Is there an alternate registry for international shipping operations?

There is no alternative registry for international shipping operations that allows for foreign ownership of ships registered in the UK.

However, if an overseas company opens an establishment in the UK or has some degree of physical presence in the UK – for example, a place of business or a branch through which it carries on business – the overseas company must register with Companies House. See Part 34 of the Companies Act 2006 and the Overseas Companies Regulations 2009/1801 for further information.

Law stated - 21 April 2023

SHIP MORTGAGES AND OTHER LIENS OVER VESSELS

Types of ship mortgage



What types of ship mortgages exist and what obligations may a ship mortgage secure? Can contingent obligations, including swap obligations, be secured? Are there standardised forms?

The UK statutory forms of mortgage generally fall into two categories, those securing 'principal sum and interest' only and those securing an 'account current or other obligation'.

Ship mortgages can be granted by an owner to secure their own obligations whether as principal debtor or as guarantor of another party's obligations, although where a third party granting a ship mortgage is a UK company, lenders should ensure that the English law corporate benefit tests are met. Because principal sum and interest mortgages will not secure contingent or other liabilities beyond principal and interest payable under the loan, it is 'account current or other obligation' mortgages that are usually used in ship finance transactions.

The current pro forma UK statutory mortgages are issued by the Maritime and Coastguard Agency (MCA). These contain limited information, and, although English statute and common law provide mortgagees with a number of general rights if the owner defaults (such as the right to take possession of the ship, the right of sale, the right to appoint a receiver, the right to foreclose and the right to arrest the ship), it is usual that a lender will also require that a deed of covenants 'collateral' to the ship mortgage be executed. This will set out the lender's rights and powers in more detail.

Law stated - 21 April 2023

Required form

Give details of any required form for ship mortgages in your jurisdiction.

The Merchant Shipping Act states that a registered ship mortgage must be in one of the forms prescribed by or approved under registration regulations and published on the MCA website.

Law stated - 21 April 2023

Registration of mortgages

Who maintains the register of mortgages? What information does it contain and where are such filings to be made? What is the effect of registration?

The register of mortgages over UK ships is the responsibility of the centralised Registry of Shipping and Seamen in Cardiff, Wales (the Registry). Filings are made to the Registry.

A mortgage creates a fixed security over the ship, which attaches to the ship in rem. The mortgage will survive a change of ownership. It entitles the lender to sell the ship and use the sale proceeds to pay off the amount owing to it if the owner is in default. Under the Merchant Shipping Act every registered mortgagee shall have power, if the mortgage money or any part of it is due, to sell the ship or share in respect of which he or she is registered, and to give effectual receipts for the purchase money.

Mortgages are registered in the order in which they are produced to the registrar for the purposes of registration. Registration gives the mortgagee higher priority over unregistered mortgagees. This is irrespective of whether the unregistered mortgage was created first and is irrespective of knowledge. Where more than one mortgage is registered against the same ship or share, the priority of the mortgages between themselves shall be determined by the order or time in which the mortgages were registered, the earliest registered mortgage having priority.

Failure to register a mortgage at the Registry does not render the mortgage void. However, an unregistered mortgage

will be an equitable mortgage and an unregistered mortgagee will not have priority over a subsequently registered mortgagee.

Under English law, any person who is an intending mortgagee under a proposed mortgage may notify the registrar of the intended interest, and the registrar shall record that interest. This is known as a 'Notice of Mortgage Intent' (form MSF 4739). A priority notice has effect for a period of 30 days. If the mortgage is executed and registered within 30 days and during that time another mortgage has been registered, the mortgagee with the priority notice will take priority over the other mortgage even though it has been registered first.

Where the shipowner is a UK company, the mortgage and deed of covenants should also be registered with Companies House within 21 days of the creation of the charge. A copy of the security document will be placed on the register at Companies House and will be open to inspection by a search against the company. A failure to register with Companies House within this time limit renders the charge void against a liquidator, administrator or any creditor of the company.

Law stated - 21 April 2023

Must the total amount of the mortgage be stated therein? Must the mortgage contain a maturity date? Must the underlying debt instrument be filed with or attached to the recorded mortgage?

In rare circumstances where the 'principal sum and interest' statutory mortgage is used, it is necessary to state the amount of the loan. Neither the total amount of the mortgage nor the maturity date need be stated in the 'account current' mortgage.

It is only the original mortgage instrument that must be presented when registering the mortgage with the Registry – neither the underlying debt instrument nor the deed of covenants needs to be filed or attached to it. The Registry will endorse the mortgage with the date and time of its registration and it will then be returned to the mortgagee.

Law stated - 21 April 2023

Can a mortgage be registered in the name of an agent or trustee for the benefit of multiple lenders?

Yes, the Registry will accept for registration of a mortgage in favour of an agent or trustee (or, under English law, more commonly known as a 'security trustee') for the benefit of multiple lenders.

Law stated - 21 April 2023

Filings on transfer

If the mortgagee is an agent or trustee for a lending syndicate, must any filings be made upon transfer of a portion of the underlying debt among existing lenders or to a new lender?

English law has well-established principles of trust and agency. If a syndicate of banks have put a trust structure in place whereby one of those lenders acts in a separate capacity as security trustee for itself and the other syndicate members, then for as long as the security trustee remains appointed in this capacity, security will not need to be amended if any of the syndicate banks (including the security trustee in its separate capacity as lender) sells or otherwise transfers its loan commitment to another lender.

If the mortgagee transfers its interest to a new lender, agent or trustee what filings are required?
Is the mortgagor's consent required?

The UK statutory form of mortgage can be transferred to a new mortgagee if the outgoing mortgagee completes and signs the form of transfer contained in the statutory mortgage and lodges this with the Registry. The Registry would not require evidence that the mortgagor has consented to this transfer. However, the loan documentation may have been negotiated in such a way that the lender or lenders may have to seek the borrower's consent to any transfer of commitment or of the underlying security. If the lenders in question also benefit from a deed of covenants this will need to be transferred to the new security trustee. Depending on how the transaction is effected, if the mortgagor is a UK company, new charge registrations may also be required at Companies House.

Maritime liens

What other maritime liens over vessels are recognised in your jurisdiction? Do these claims give rise to a right to arrest a vessel? In what circumstances may associated ships be arrested?

Under English law, there are five main categories of maritime lien:

- salvage remuneration;
- damage done by a ship;
- master and crew wages;
- master's disbursements; and
- bottomry and respondentia (largely redundant).

These claims give rise to an action in rem against a ship and a right to arrest a ship.

Maritime liens operate as a charge on the ship that will follow the ship notwithstanding a change of ownership. This is so even where a purchaser is a bona fide purchaser for value without notice of the claim. As maritime liens survive the sale of a ship, this may operate to allow the arrest of a ship even if it has changed ownership. This is because the lien attaches to the ship at the time the cause of action arises and will remain attached until satisfied or time-barred.

It is also possible to arrest a sister ship of a ship that is subject to a maritime lien if the owner of the sister ship was the owner or demise charterer or bareboat charterer, or in possession or control of that ship, when the cause of action arose in relation to the defendant ship, and that person or entity is also the beneficial owner of all the shares in the sister ship when the claim is commenced.

The Senior Courts Act 1981 sets out a list of maritime claims that give rise to a statutory right of action in rem against a ship. These are commonly referred to as 'statutory liens' and these also give rise to a right to arrest a ship.

What maritime liens rank higher than a mortgage lien?

Claims for maritime liens will rank higher than a registered mortgage, even if they arise after the mortgage has been created or registered. A possessory lien (eg, a shipowner's right to retain possession of cargo until money owed to it by the ship's charterer have been paid) will also rank higher than a mortgage lien.

Typically, a mortgage will have priority over statutory liens, unless a claim has been made and a writ in rem has been issued against the ship prior to the date of the mortgage.

Law stated - 21 April 2023

Non-mortgage liens

May non-mortgage liens be recorded over a vessel?

Non-mortgage liens may not be recorded or registered over a ship under English law.

Law stated - 21 April 2023

'Foreign' flag vessels

Will mortgages on 'foreign' flag vessels be recognised in your jurisdiction? If so, do they share the same priority as those on vessels registered under the laws of your jurisdiction?

Yes, in the UK, mortgages on 'foreign' flag ships are recognised. The priority of the foreign mortgage will be the same as if it had been a similar mortgage over a UK-flagged ship.

Law stated - 21 April 2023

Enforcement of mortgages

What is the procedure for enforcing a mortgage in your jurisdiction by way of foreclosure? Are interlocutory sales permitted? How long does a judicial sale take? What are the associated court costs and how are they calculated?

If the owner is in default under the mortgage documents, the mortgagee has the right to apply to the court for the arrest and sale of the ship if it is located within UK territorial waters. The Admiralty Court in England and Wales has jurisdiction over all ships in UK territorial waters irrespective of their flag.

To arrest the ship, the mortgagee must issue its claim in the Admiralty and Commercial Court Registry. The claim form must then be served by fixing it on the ship. Usually, the mortgagee will apply for the issue of a warrant of arrest at the same time as issuing its claim. For the court to issue a warrant of arrest the mortgagee must file an affidavit setting out, among other things, the details of the mortgage and the default in payment by the owner. The mortgagee must also provide an undertaking to meet the costs of the Admiralty Marshal. Upon receipt of the application and the payment of the fees, the warrant of arrest will be issued and the Admiralty Marshal will serve the warrant of arrest. After the arrest, the ship remains in the custody of the Admiralty Marshal until it is released or sold by the court.

The mortgagee may make an application to the court for an order for sale. Once the order has been made, the ship will be valued and shipbrokers will be instructed to advertise the sale in the trade press. Potential buyers will usually inspect the ship and make sealed bids. The ship will then be sold for the highest bid (if the mortgagee finds a buyer

privately, the court may, in exceptional circumstances, allow for the ship to be sold to that buyer, though recent case law has further limited the scope of such 'private' sales). Once the ship is sold, the proceeds of the sale are paid into the court. The Admiralty Marshal will submit his or her expenses and apply for leave to pay these expenses from the fund in court. The mortgagee will then apply for judgment for an order for the payment out of the proceeds of the court.

Law stated - 21 April 2023

Sale by mortgagee

May a vessel be sold privately by a mortgagee? Will the sale discharge liens over the vessel?

Yes, under English law a ship may be sold through the court or privately by the mortgagee pursuant to the powers given to it under the mortgage documents. The private sale by the mortgagee will not discharge liens over the ship unless they are discharged from the proceeds of sale.

Law stated - 21 April 2023

Default under mortgage

Will the courts of your jurisdiction enforce mortgage provisions stipulating the appointment of a receiver on default under the mortgage?

Yes; however, this method of enforcement is very rarely used in practice.

Law stated - 21 April 2023

Limitations on rights of self-help

What are the limitations on rights of self-help by a mortgagee?

The current pro forma UK statutory mortgages issued by the MCA contain limited information, and, although English statute and common law provide mortgagees with a number of general rights if the owner defaults (such as the right to take possession of the ship, the right of sale, the right to appoint a receiver, the right to foreclose, and the right to arrest the ship), it is usual that a lender will also require that a deed of covenants 'collateral' to the ship mortgage be executed.

Law stated - 21 April 2023

Duties to owner or third-party creditors

What duties does a mortgagee owe to an owner or third-party creditors?

With regard to a private sale of a ship by the mortgagee, it will owe a duty to the owner to act in good faith, with reasonable skill and care and must take all reasonable steps to obtain the best price reasonably obtainable for the ship. Mortgagees do not owe duties to unsecured creditors.

Law stated - 21 April 2023

COLLATERAL

Finance leases

May finance leases or other charters be recorded over vessels flagged under the laws of your jurisdiction?

The only interests that can be registered against a UK-flagged ship are mortgages. Therefore, there is no way to record a finance lease or charter against a ship on the Register unless obligations under those documents were secured by a mortgage against the ship, which, generally, is unlikely.

Law stated - 21 April 2023

May finance leases be recharacterised by a court as a financing contract? If so, is there any procedure for protecting the lessor's interest against third-party creditors?

Where the party that has sold the asset and leased it back has a right against, or an obligation to, the buyer or lessor to retake title to the asset at the end of the lease, for example, by paying an option price, it is possible that a court may recharacterise the lease as a secured financing contract or loan. However, English courts are unlikely to do this unless there is evidence that the sale and finance lease documents do not record the parties' true commercial motivations. The lessor may seek indemnities from the lessee to guard against such a risk.

Law stated - 21 April 2023

Security interests

How is a security interest created over earnings of a vessel, charter contracts, insurances, etc?
How are these security interests perfected?

Security interests over earnings of a ship, charter contracts and insurances can be created by means of an assignment. To be effective as a legal assignment under section 136 of the Law of Property Act 1925, the assignment must be in writing, signed by the assignor and it must be absolute, and not purporting to be by way of charge only. Only the benefit of an agreement may be assigned. In addition, written notice of the assignment must be given to the debtor (eg, the charterer in an assignment of earnings and the insurer in an assignment of insurances). If the assignment satisfies these requirements, the legal right to the debt, all legal and other remedies for the recovery of that debt and the power to give good discharge without involving the assignor, transfers to the assignee. If the assignment does not fulfil all of these requirements, it does not necessarily fail. It is likely to operate as an equitable assignment. The disadvantages of this are that the lender (the assignee) cannot give a good discharge for the debt without the agreement of the borrower (the assignor) and the lender cannot sue the third-party debtor without joining the borrower into the action.

Alternatively, these security interests can be created by means of a fixed or floating charge.

Any such security interests created by UK companies (whether by way of an assignment or fixed or floating charge) must be registered with Companies House within 21 days otherwise they will be void against a liquidator, administrator or creditor of the company.

Law stated - 21 April 2023

Must security interests against non-vessel collateral be registered to be enforceable? If so, where are such filings made?

The two most common types of security interest against non-ship-related collateral are security over the borrower's shares, and security over a bank account.

Ship finance lenders will often take a charge over the shares in the borrower company. The main advantage of a share charge is that following an event of default the lender will be able to sell the ship-owning company as an alternative to selling the ship itself.

In order to ensure that the charge is not void against a liquidator, administrator or any creditor of the company a share charge created by a UK company should be registered at Companies House. Although some security created over shares may be subject to the Financial Collateral Arrangements Regulations 2003, which would mean that the security does not need to be registered, most practitioners still take a cautious view and register (or attempt to register) the security at Companies House.

Law stated - 21 April 2023

How is a security interest over a deposit account established? How is a security interest perfected?

A security interest over a deposit account opened with the lender is usually taken by way of a fixed or floating charge (or if the borrower's deposit account is held with a third-party bank, by way of an assignment in favour of the lender). In order to do so, written notice of the assignment must be given to the account bank and an acknowledgement obtained in return.

A fixed charge or an assignment gives the security taker control over the charged asset. If the security taker does not have sufficient control over the asset, a court will re-characterise the charge or assignment as a floating charge rather than a fixed charge or assignment, even if this was not how the charge is expressed to be created. For a fixed charge or effective assignment to be taken over a bank account, the account holder must not be able to deal with the money in the charged account without written permission from the security taker. If the account is being used frequently in the course of the account holder's business this restriction may be impracticable.

A floating charge over an account provides the security taker with less robust security than a fixed charge or assignment because a floating charge holder is only paid out of asset realisations after fixed charge holders, the expenses of the insolvent estate and certain preferential creditors have all been paid in full and a percentage of the remaining assets has been ring-fenced for payment to unsecured creditors. Moreover, because the charge holder does not control the account it may find that funds have been withdrawn when it comes to enforce. However, a floating charge is often preferred precisely because it allows the account holder more control over the money in the account in order to operate its business. The account holder is free to withdraw funds from the charged account without the security taker's consent.

A fixed or floating charge (or assignment) granted by a UK company over a deposit account will need to be registered at Companies House within 21 days otherwise the charge will be void against a liquidator, administrator or any creditor of the company.

Law stated - 21 April 2023

How are security interests in non-vessel collateral enforced?

Ship finance loan agreements will set out the circumstances, usually named collectively as 'events of default', upon the occurrence of which the lender can accelerate the loan and enforce its security. Depending on how the documents are drafted or negotiated, the borrower may have a number of days' grace to remedy the default before enforcement action may be taken by the lender.

The lender's security documents will often contain detailed enforcement provisions setting out the steps the lender is entitled to take following an event of default; for example, dating the signed stock transfer form provided as collateral to a share charge to transfer ownership of the shares in the borrower away from its parent, or (though infrequent in shipping transactions) by appointing a receiver in respect of the charged assets. If the borrower or other obligor disputes the lender's enforcement action (eg, a guarantor refuses to pay overdue amounts that the borrower has failed to pay), the lender will need to enforce its rights either through the English courts, or if the borrower or other obligor is insolvent and unable to pay, as a secured creditor in the relevant insolvency regime to which the borrower or other obligor is subject.

Law stated - 21 April 2023

Share pledges

How are share pledges for vessel financings established? Are share pledges or share charges common in your jurisdiction?

Security over shares is common in ship finance transactions as the borrower will often be a limited liability company or special purpose vehicle with no assets other than the ship itself. Under a share charge, all of the shares in the borrower are charged to the lender, who, following a default by the borrower under the loan, will ultimately be able to step in and take ownership of the borrowing company or, alternatively, sell the shares to a third party. This gives the lender the ability to sell the ship-owning company, as an alternative to selling the ship itself.

A share charge does not legally depend on the bank having physical possession of the share certificates. However, in the event that the borrower defaults and the lender wishes to sell the shares, the lender will need the share certificates and executed stock transfer forms in order to perfect its security. Therefore, as an ancillary to the share charge, the lender will require the borrower to execute undated stock transfer forms, which, following an event of default by the borrower, the lender will then complete in favour of itself or, more likely, a new arm's-length shareholder.

The lender will also require undated letters of resignation from each of the directors of the borrowing company to enable the lender to replace the directors and officers of the company with its own team in the event of default by the borrower. Irrevocable proxies and directors' undertakings may also be obtained. If the shareholding company that creates the charge is a UK company, the share charge should be registered at Companies House against the shareholding company within 21 days to ensure that it is not void against a liquidator, administrator or any creditor of the shareholding company.

As the use of bearer shares in UK companies has been prohibited since 26 May 2015, share pledges are no longer appropriate when taking security over shares of a company registered in England and Wales.

Law stated - 21 April 2023

Is there a risk that a pledgee, before or after exercise of the share pledge, may be exposed to debts or other liabilities of the pledged company?

It is an established principle of English corporate law that a shareholder of a UK company is only liable for the company's debts up to the value of its shareholding. English courts strictly adhere to the corporate veil principle (whereby a company is recognised as a legal person separate from its shareholders) and will only pierce the veil and look to the members in exceptional circumstances where a number of conditions are met and there is proven impropriety.

Before and after the exercise of share security granted in its favour, a lender will, however, need to be aware of the English statutory concept of 'shadow director' set out in section 251 of the Companies Act 2006, whereby persons (excluding professional advisors) in accordance with whose directions or instructions the directors of the company are accustomed, will be treated as directors and, therefore, be subject to the same legal duties where and to the extent those duties are capable of applying and may be liable in the same way if illegality is proven, such as fraud or misconduct in the winding up of the company in contravention of the Insolvency Act 1986. The Insolvency Act also treats shadow directors as 'connected' to the company and provides liquidators or administrators with significant power to challenge transactions involving shadow directors prior to the onset of insolvency as a preference or at an under value. It should, however, be noted that, to date, a lender has not been proven in the English courts to be acting as a shadow director.

Law stated - 21 April 2023

TAX CONSIDERATIONS FOR VESSEL OWNERS

Domestic taxation

Is the income earned by the owners of vessels registered in your jurisdiction subject to domestic taxation? At what rate?

The mere registration of a vessel in the UK will not cause the income from operation of the vessel to become subject to UK tax. A company is subject to UK corporation tax if it is a UK tax resident or if it is non-resident but carries on a trade through a UK permanent establishment. A ship is not treated as a permanent establishment for this purpose.

As of 1 April 2023, the rate of UK corporation tax payable on taxable profits increased from 19 per cent to 25 per cent.

Law stated - 21 April 2023

Tonnage tax

Is there an optional tonnage tax exempting vessel owners from tax on income?

In addition to the standard corporation tax rules in the UK, there is a separate tonnage tax regime into which companies operating qualifying ships that are strategically and commercially managed in the UK can elect. Those who elect into the regime pay tax based on the net tonnage of the ships operated rather than by reference to the profits earned from such operations. The result is a very low effective rate of tax.

Following the end of the Brexit transition period, certain reforms to the UK tonnage tax came into force on 1 April 2022 including to:

- reduce the lock-in period from 10 to eight years;
- allow HMRC to admit companies to the tonnage tax regime beyond the initial enrolment window, when there is reason to do so;
- remove the requirement for a certain percentage of EU flagged vessels; and
- simplify the rule that allows companies to classify dividends from overseas companies as relevant shipping profits.

Additionally, tonnage tax guidance will be reviewed to include, amongst other areas, consideration of 'net zero' objectives.

To qualify for tonnage tax the following criteria must all be satisfied:

- the company must be within the charge to UK corporation tax, namely, tax resident in the UK or carrying on business through a permanent establishment in the UK;
- the company must 'operate ships'. This means it must own or charter in the ship. It is the operator of a ship that is eligible for tonnage tax, so the owner of a ship will generally not be eligible if it charters out the ship on bareboat terms. In March 2023, the UK government announced further updates to the UK tonnage regime including (1) the opening of an 18-month window commencing on 1 June 2023 for companies that previously left UK tonnage tax to rejoin, and (2) that ship management companies may join UK tonnage tax from 1 April 2024. As of the date of publication, the details of these new regimes were not yet finalised;
- the ships must be 'qualifying ships'. This means they must be 100 gross tons or more, be seagoing and be used for a 'core qualifying activity'. These activities are:
 - carriage of passengers or cargo by sea;
 - towage, salvage or other marine assistance carried out at sea; and
 - transport by sea, in connection with other services necessarily provided at sea.
- qualifying ships must be strategically and commercially managed in the UK. Strategic and commercial management will be assessed by reference to certain specific criteria; and
- the company must not time or voyage charter in on average more than 75 per cent of its net tonnage.

Companies electing to enter and remain within the tonnage tax regime must commit to providing officer or rating-training places in proportion to the number of officers employed by the company on its qualifying ships, or else make a payment in lieu to the Maritime Training Trust.

Tonnage tax-related losses cannot be used to reduce other profits liable to corporation tax. Tonnage tax companies are also not permitted to deduct loan financing interest from other taxable profits or to claim capital allowances (tax depreciation) in respect of vessels within the tonnage tax regime.

Law stated - 21 April 2023

Tax incentives

What special tax incentives are available to shipowners registering vessels in your jurisdiction?

There are no special tax incentives for shipowners registering vessels in the UK. The tonnage tax regime does not require vessels to be registered in the UK.

Law stated - 21 April 2023

Other tax provisions

Are there any other noteworthy tax provisions specifically applicable to shipping, shipping income or ship finance?

Taxable profits generated by shipping activities outside the tonnage tax regime are subject to UK corporation tax in the usual way.

The rate of capital allowances (tax depreciations) on ships stands at 6 per cent. This is partly responsible for a reduction in previously popular tax leasing products provided by ship financiers, where the financier would lease the ship to the customer and use accelerated tax depreciation to reduce the financing costs. In March 2023, the government announced that with effect from from 1 April 2024, the limit on capital allowances on expenditure for businesses that lease ships to UK tonnage tax companies, would be increased from £80 million to £200 million.

Law stated - 21 April 2023

INSOLVENCY AND RESTRUCTURING

General scheme of reorganisation or insolvency administration

Is there a general scheme of reorganisation or insolvency administration in your jurisdiction?

There are general schemes of restructuring and insolvency administration in the UK. The most common process is that of administration, governed by Schedule B1 of the Insolvency Act 1986. Under these rules the administration of a company must achieve one of the following objectives (in order of priority):

- the rescue of the company (the primary objective);
- the achievement of a better result for the company's creditors as a whole than would be likely if the company were wound up (without first being in administration) (the second objective); or
- the realisation of some or all of the company's property to make a distribution to one or more secured or preferential creditors (the third objective).

If a ship mortgagor is subject to insolvency proceedings, all legal proceedings against the mortgagor will be stayed by virtue of an automatic moratorium. However, the mortgagee is still free to enforce its security and retain the proceeds of enforcement in priority to unsecured creditors, provided that the mortgagee does not require the assistance of the courts for such enforcement.

On the other hand, if the ship mortgagor is in the process of administration, the moratorium created by paragraphs 42 and 43, schedule B1, Insolvency Act 1986 is wider. Not only does this moratorium apply to legal proceedings, it does not allow enforcement of security without the consent of the administrator or the court. This moratorium does not alter the substantive rights of any party against a company in administration, but simply suspends the exercise of those rights during the administration. This does not prevent creditors from terminating contracts or from exercising rights of set-off. However, this may be subject to change due to the coronavirus pandemic.

In addition to administration, the 'Restructuring Plan' process was introduced in 2020. The Restructuring Plan is a Court-supervised Companies Act 2006 procedure that may be used in respect of companies in financial distress. The Restructuring Plan is a 'debtor-in-possession' mechanism available to companies in order to eliminate, reduce, prevent or mitigate the adverse effect on a company's ability to carry on business as a going concern caused by serious financial difficulties that the company encounters or is likely to encounter. Under a Restructuring Plan proposed by the debtor company, some or all of the creditors of the debtor are placed in to classes. Different proposals may be proposed to different classes and in order for the proposal to be binding on a class of creditors, at least 75 per cent in value of creditors need to vote in favour. If this requisite threshold is not met for a particular class (or classes) of creditors, the Court may enact a 'cross-class cramdown', allowing the Court to sanction the plan as binding even if a class of creditors did not vote in favour of the proposals applicable to them.

There are other rescue and reorganisation processes available.

Foreign court rulings

Will the courts of your jurisdiction respect the rulings of a foreign court presiding over reorganisation or liquidation proceedings?

The general English common law principle is that a foreign judgment will be enforceable in England and Wales if the defendant was:

- present in the foreign country;
- submitted to the jurisdiction of that court by voluntarily appearing in proceedings; or
- (before the commencement of the proceedings) the defendant had agreed, in respect of the subject matter of the proceedings, to submit to the jurisdiction of that country.

Therefore, at common law, if a defendant was not present in the jurisdiction of the foreign court and did not submit to that jurisdiction, he or she can generally expect that judgment will not be enforceable against him or her in England and Wales.

However, the English common law position has been modified by various statutes, case law and EU regulation.

The EC Regulation on Insolvency Proceedings allocates jurisdiction to the courts of the country in which the insolvent company has its centre of main interests (usually its head office or the place where the majority of its business was conducted). It then provides for automatic recognition of the effects of that insolvency in all member states. This regulation has been replaced by the Recast Insolvency Regulation for insolvencies commencing on or after 26 June 2017 and further clarifies the location of a company's centre of main interests. Following the United Kingdom's exit from the European Union, automatic recognition of insolvency proceedings in member states or the UK no longer applies to those insolvency proceedings commenced after 11pm GMT on 31 December 2020. The EU Regulation still applies to insolvencies commenced before 11pm GMT on 31 December 2020.

The United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border Insolvency, which has been implemented in English law by the Cross-Border Insolvency Regulations 2006, similarly provides for recognition by the English courts of foreign insolvency proceedings brought in the courts of the debtor's centre of main interests. Post-Brexit, recognition of foreign insolvency proceedings in the England is usually obtained using this route.

The Foreign Judgments (Reciprocal Enforcement) Act 1933 also provides for the recognition of judgments from specified jurisdictions, provided those judgments are registered.

In the Supreme Court joined appeals of *Rubin v Eurofinance SA* and *New Cap Reinsurance Corporation v AE Grant*, the issue facing the court was whether the jurisdiction of the English court to assist a foreign insolvency proceedings extended to recognition of foreign judgments that would not otherwise be entitled to recognition due to the lack of submission to the jurisdiction by the defendant.

The Supreme Court held that it would not recognise the judgment of a foreign court unless the defendant was present in or had submitted to its jurisdiction. It made it clear that judgments of courts in foreign insolvency proceedings are not to be accorded special status.

Model Law on Cross-Border Insolvency

Has your jurisdiction adopted the Model Law on Cross-Border Insolvency promulgated by the United Nations Commission on International Trade Law?

Yes. The UNCITRAL Model law has been adopted by virtue of the Cross-Border Insolvency Regulations 2006.

Law stated - 21 April 2023

Order of priority

What is the order of priority among creditors? In what circumstances will creditors be required to disgorge payments from an insolvent company?

The usual order of priority among creditors in the UK is as follows:

- proceeds of fixed-charge assets (less direct realisation costs) to fixed charge-holders;
- fees and expenses of the liquidator or administrator;
- preferential debts paid to preferred creditors – usually limited to employee wages;
- secondary preferential creditors – HMRC (the UK tax authority) in respect of certain outstanding taxes;
- the 'prescribed part' set aside from realisations from floating charge assets for unsecured creditors (up to a maximum of £800,000 for charges created after 6 April 2020);
- proceeds of floating charge assets (less preferential debts and the prescribed part) paid to floating charge holders;
- unsecured creditors (including HMRC in respect of taxes not subject to secondary preferential creditor treatment) rank equally between themselves unless they are subject to a binding subordination agreement;
- interest incurred on all unsecured debts post-liquidation; and
- any surplus paid to shareholders in accordance with the company's articles of association.

A creditor may be required to repay any payments received from an insolvent company where:

- the insolvent company is found to have granted a preference, which occurs where:
 - within six months (or two years if the person being preferred is connected with the company) before the company went into liquidation, the insolvent company took an action that has placed a creditor in a better position than he or she would have been in;
 - the company was influenced by the desire to prefer that creditor; and
 - at the time of the action, the company was unable to pay its debts; or
- the insolvent company is found to have made a transaction at an undervalue. This is where within two years before the administration or liquidation, a transaction was made with a person connected to the company, at below the market value, and at the time of the transaction the company was unable to pay its debts as they fell due.

In either case, an administrator or liquidator may apply to the court for an order avoiding any such action or transaction at undervalue and the creditor may be forced to give back any profit he or she has made as a result.

Law stated - 21 April 2023

Security provision by vessel owner

May a vessel owner provide security on behalf of other related or unrelated companies? What are the requirements for it to be enforceable?

Generally, under English law, a shipowner may provide security on behalf of other related or unrelated companies. In relation to public companies (and private companies with a public parent company), there may be issues regarding the giving of financial assistance that is prohibited under the Companies Act 2006. There may also be issues concerning directors duties under the Companies Act 2006 in circumstances where the security is provided on behalf of an unrelated company.

For the security to be enforceable, the security must be duly executed and perfected, and the party taking the security should be advised to conduct due diligence as to the relevant corporate authorities of the shipowner providing the security.

Law stated - 21 April 2023

Law of fraudulent transfer

Is there a law of fraudulent transfer that permits a third-party creditor to challenge, for example, the grant of a mortgage because of insolvency of the mortgagor or insufficient consideration received by the mortgagor in exchange for the grant of the mortgage?

Under English law, when a company has entered into insolvency proceedings, certain transactions that were entered into by the company before the insolvency began may be challenged by an administrator or liquidator under the Insolvency Act 1986. These transactions are known as 'reviewable transactions'.

The types of reviewable transaction or grounds on which a transaction may be challenged under the Insolvency Act 1986 are as follows (if the criteria in (1), (2) and (3) are satisfied, the floating charge will automatically be invalid and no application needs to be made by the officeholder):

1. if the insolvent company has granted a preference (section 239);
2. an undervalue (section 238);
3. if the insolvent company benefits a creditor by granting a floating charge for existing debt for no new consideration (section 245). A floating charge may be avoided where:
 - it has been created in the 12 months (or in two years if in favour of a person connected with the company) before a company's insolvency to secure past indebtedness (eg, if a floating charge is granted by the company to secure a loan to the company that was previously unsecured);
 - it was given as a preference to a creditor or if it was given in exchange for prior consideration;
 - at the time the floating charge was created, the company was unable to pay its debts or became unable to pay its debts as a consequence of the charge; and
 - if the company entered into a transaction defrauding creditors (section 423). A transaction may be set aside where:
 - the transaction was entered into at an undervalue; and
 - the purpose was to put assets beyond the reach of a creditor or a person who is making a claim or made a claim against the company.

There is no requirement for the company to be insolvent, in liquidation or in administration in order to make a challenge under section 245.

Law stated - 21 April 2023

Petitions by creditors

How may a creditor petition the courts of your jurisdiction to declare a debtor bankrupt or compel liquidation of an insolvent obligor?

Compulsory liquidation is a court-based procedure whereby the assets of a company are realised and distributed to the company's creditors and shareholders before the company is dissolved. The circumstances in which a company may be wound up are set out in section 122(1) of the Insolvency Act 1986.

A creditor wishing to wind up a company should first conduct a search to ensure that no winding-up petition is already pending, search the register at Companies House to check whether the company is already in some insolvency procedure and check with the court to ascertain whether there are any other outstanding winding-up petitions.

Winding-up petitions are usually made in the Business and Property Courts of England and Wales (the Insolvency and Companies List in London or a district registry if outside London). To compel liquidation, the creditor (who will be the 'petitioner') must be able to prove to a court that the company is unable to pay its debts as they fall due. Methods include:

- if a creditor (by assignment or otherwise) to whom the company owes a sum of £750 or more has served a statutory demand that has not been paid within 21 days;
- if a judgment, decree or order of any court in favour of a creditor of the company is returned unsatisfied in whole or in part;
- if it is proved to the satisfaction of the court that the company is unable to pay its debts as they fall due; or
- if it is proved to the satisfaction of the court that the value of the company's assets is less than the amount of its liabilities, taking into account its contingent and prospective liabilities.

Once a winding-up order is made, the official receiver becomes the liquidator and upon the making of a winding-up order the liquidator takes control of the company's assets.

Law stated - 21 April 2023

Model Netting Act

Has your jurisdiction adopted the Model Netting Act of the International Swaps and Derivatives Association (ISDA)? If not, may a swap provider exercise its close-out netting rights under an ISDA master agreement despite an obligor's insolvency?

The Model Netting Act has not been formally adopted into English law due to the widespread acceptance of the enforceability of netting without the need for specific statutory recognition. The Banking Act 2009, however, introduced a special resolution regime for banks and building societies that directly applies to netting transactions with these types of entities

UK company and insolvency legislation also provides a complex regime to protect the market from counterparty insolvencies whereby the gains and losses of a defaulting party are netted out once a swap provider closes out that party's contracts. If a net gain is left, it is payable to the defaulter, with a net loss provable in its insolvency.

UPDATE AND TRENDS

Current developments

Are there any emerging trends or hot topics that may affect shipping finance law and regulation in your jurisdiction in the foreseeable future?

Sustainability

Sustainable shipping initiatives and the drive toward decarbonisation continue to top the agenda for blue-chip shipowners and financiers, who are also embracing environmental, social and governance (ESG) data collation initiatives.

In parallel a strong regulatory push towards decarbonisation has begun. In April 2020, the United States committed to pursuing zero emissions in the shipping industry by 2050. Following the UN Climate Change Conference (COP 26), the International Maritime Organisation (IMO) agreed to begin revising the Initial IMO Strategy on Reduction of Greenhouse Gas emissions from ships so that it promotes a more ambitious approach to reducing carbon emissions. They will debate the final draft of this strategy in Spring 2023 and adopt it at the Marine Environment Protection Committee (MEPC 80) session in July 2023.

On 1 November 2022, amendments to the MARPOL Annex VI came into effect requiring ships to improve their energy efficiency in the short term, and from the beginning of 2023, all ships are mandated to measure their energy efficiency by calculating their attained Energy Efficiency Existing Ship Index (EEXI). This is part of a new data collection and reporting requirement to disclose each ship's annual operational carbon intensity indicator (CII) and CII rating.

At COP 26, the IRFS Foundation Trustees also announced the formation of a new International Sustainability Standards Board (ISSB), which aims to standardise global ESG reporting disclosure requirements. The sustainability bond market is projected to continue to grow year-on-year and the European Commission recently published its proposed (voluntary) Green Bond Standard. However, it remains to be seen whether shipping as a sector will see material investment from sustainability linked funding.

The EU Taxonomy Regulation is also entering into force and sets out criteria for demonstrating sustainability and mitigating against 'greenwashing'. We anticipate further expansion of these types of initiatives in 2023 and beyond.

On the flip side, ESG requirements have led to top shipowners becoming more hesitant in investing their sizeable capital in new tonnage. In turn, the blue-chip ship financiers may well become concerned if loan books are not replenished with new, energy efficient ships.

At the mid to lower end of the market, ESG sits further down the list of immediate priorities, both for owners (who do not have the capital to invest in efficient technologies or newer ships) and the alternative providers that finance those older and/or less efficient ships. It will require further international consensus and intervention to ensure this side of the market does not fall behind in decarbonisation.

Russian sanctions

As a result of wide-ranging global sanctions imposed following Russia's invasion of Ukraine, Russia-flagged ships can no longer enter US, UK, or European Union ports, while Russia-owned, chartered or affiliated vessels are excluded from the UK and North America. These actions have had a major impact on Russia's fleets, in particular tankers, and the maritime industry more widely, with owners, charterers, financiers, insurers and other key stakeholder all scrambled to review sale agreements, charters, loans and policies in order to check sanctions compliance. Enhanced levels of KYC

are now commonplace and all parties involved in the shipping industry need to stay up-to-date with developments as sanctions continue to be updated and expanded.

Switch to RFRs

The US dollar LIBOR panel will cease on 30 June 2023 (although the UK Financial Conduct Authority announced on 3 April 2023 that it will require the LIBOR administrator to continue to publish 1, 3 and 6 month US dollar LIBOR on a synthetic basis until 30 September 2024 to further ease the transition) and ship finance banks and other financiers continue to devote significant time to switching all of their remaining LIBOR based US dollar facilities over to risk-free rates (RFRs) ahead of that deadline. To facilitate this the Loan Market Association has published exposure drafts and various recommended provisions for switching to RFRs or day one use of RFRs and these forms have been widely used by ship finance banks. Although there are still alternatives available, the Secured Overnight Lending Rate (SOFR) is now the go-to RFR for existing facilities switching away from LIBOR and new US dollar loans. SOFR can be applied in a number of ways however in our experience, SOFR compounded in arrears is the most widespread in ship finance, with the switch over intended to produce a neutral result for banks and borrowers. This methodology does have disadvantages however, both for the banks having to calculate a more complex rate and for borrowers who will not know the exact amount of their interest payments until the end of each interest period. We are, therefore, now also seeing a trend towards the use of Term SOFR, which works in a similar way to LIBOR and is linked to derivatives traded in the market.

Law stated - 21 April 2023

Jurisdictions

	Brazil	Basch & Rameh Advogados Associados
	China	KaiRong Law Firm
	Cyprus	Chrysses Demetriades & Co LLC
	Italy	Dardani Studio Legale
	Japan	Yoshida & Partners
	Malta	Dingli & Dingli Law Firm
	Marshall Islands	Vedder Price PC
	Nigeria	Tumba & Tumba
	Panama	Arias, Fábrega & Fábrega
	Singapore	Haridass Ho & Partners
	Sweden	HFW
	Turkey	ECC Law
	United Arab Emirates	HFW
	United Kingdom	HFW
	USA	Seward & Kissel LLP