

Market Intelligence

SHIPPING 2020

Global interview panel led by Kevin Cooper
of MFB Solicitors

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Bermuda

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1 | What is the current state of the shipping industry in your country?

For over 50 years, the shipping industry in Bermuda has played a key role in placing the island on the international business map. Today, Bermuda is a thriving centre for international ship financing and registration. Over the years, many of the world's leading ship owners, managers and related professionals and financiers have developed close relationships with Bermuda; this collaboration has resulted in the creation of financial structures that are tailored to the specific requirements of the shipping industry.

There have been two major developments in Bermuda over the years in relation to shipping. First, Bermuda has been used increasingly as the base for the shipping industry both in terms of incorporation and management, as well as for registration; and secondly, restructuring of shipping groups (both from a corporate and financial perspective) has utilised Bermuda as the jurisdiction of choice.

There are several reasons why Bermuda is a leading centre and a jurisdiction of choice for the shipping industry. Namely, it has:

- a sophisticated and stable regulatory framework;
- excellent shipping industry expertise;
- advanced IT and communications infrastructure;
- a legal system that is derived from English common law, allowing a final appeal to be made to the House of Lords, sitting as the Privy Council;
- good banking, computer, legal and accounting services;
- an efficient and well-run shipping registry that can operate on a 24-hour basis to accommodate clients, making Bermuda a very user-friendly jurisdiction for the shipping industry;
- low port state control detention figures, as Bermuda ships are considered low-risk vessels and, accordingly, are inspected less frequently than others;
- a government that is committed to the adaptability of Bermuda's laws so that the requirements and demands of international clients are always met;
- no income tax or profits tax, withholding tax, capital gains tax, capital transfer tax, estate duty or inheritance tax is applicable to a Bermuda exempted company; and
- no exchange controls.

The Bermuda Shipping and Maritime Authority (the BSMA) maintains a high quality international ship registry that takes pride in the high standard of its fleet and works to provide support and value to its customers. The BSMA is certified to ISO:9000:2015 standard.

The Bermuda ship registry accepts vessels on the main register, those registered on the demise register with the underlying registry in another jurisdiction and



the ship flying the Bermuda flag (demise 'in') and those registered on the demise register with the underlying registry in Bermuda and the ship flying the flag of another state (demise 'out'). The demise register can be a valuable option for owners as it allows separation between the register of title and encumbrances, and the flag jurisdiction, which can be beneficial for commercial reasons.

The flag of Bermuda has numerous benefits:

- Bermuda is a well-established international flag of high standing with prolonged membership of the Paris and Tokyo MOU Whitelists as well as the United States Qualship 21 programme, which reduces the likelihood of a vessel being inspected in these jurisdictions;
- the Bermuda Ship Registry is a member of the Red Ensign Group of ship registries, the world's ninth largest registry grouping, so vessels enjoy protection of UK and allied navies and ship owners can seek the support of British embassies and consulates;
- Bermuda has a strong and clear legal system based on English maritime law and has comprehensive maritime legislation, and mortgages are registered with a clear position on priority of mortgages;

“With liquidity issues caused by a global pandemic, most financial institutions are proving to be amenable to reasonable requests for refinancing, extensions and holidays.”

- Bermuda registers vessels of any type, age or size provided that they meet the required standards, the registered owner is not required to be incorporated in Bermuda and a streamlined service is provided with fast turnaround available at all times;
- its registry aims to ensure that its fee structure and rates remain competitive;
- statutory surveys can be delegated to classification societies, with audits and inspections carried out by the registry's own experienced surveyors worldwide, thereby ensuring consistency, high standards, continued safety and a rapid response globally;
- the BSMA's in-house expertise across time zones enables it to give timely response to technical queries 24/7, with their focus on assisting the efficient, economic and compliant operation of ships, aware of the commercial and operational requirements of the ship owner; and
- the BSMA's expert surveyors are available 24/7 to assist with port state control matters to avoid delay.

2 | What are the prevailing shipping market trends affecting your country?

The maritime industry as a whole was affected in different ways by the covid-19 pandemic. Some of those companies whose services were required to transport goods around the world found themselves busier than ever. Others, such as the cruise ship companies, have seen their businesses decimated as the tourism industry collapsed and cruises were cancelled en masse.

In Bermuda, we have many listed shipping companies, mostly of Norwegian origin, and on the whole they seem to have weathered the first half of the year in reasonable shape. Those with cash reserves have held onto the funds, and those that are less well financed have sought to go to the banks to extend credit terms or the capital markets to raise funds to bolster their reserves to help to protect against what may be an extended economic downturn.

The cruise ships, of which a number are registered in Bermuda, suffered greatly owing to the pandemic, with many rushing to the financiers to renegotiate financial arrangements and seek debt holidays to enable them to survive the year and look towards a return to their normal schedule in late 2020/early 2021.

With liquidity issues caused by a global pandemic, rather than any failure to operate the business in an appropriate manner, most financial institutions are proving to be amenable to reasonable requests for refinancing, extensions and holidays, and we are likely to see more of this type of work as the year proceeds.

Without question, in the years preceding the global pandemic, the shipping market in Bermuda was characterised by the number of new listings of

Bermuda-incorporated shipping and shipping-related companies on the Norway Over-the-Counter (N-OTC) market and on Oslo Axess or the Oslo Stock Exchange.

The pathway from Hamilton, Bermuda to Oslo, Norway's capital and financial hub, is a well-trodden one, as evidenced by no less than a dozen new listings in the past five years.

Investors are comfortable with Bermuda because it offers a tax-neutral, business-friendly environment with a strong regulatory framework that protects investor and creditor rights. Bermuda companies are proven vehicles for accessing high-quality capital efficiently. A newly incorporated Bermuda shipping company looking for capital turns to Norway as an obvious source to raise funds quickly. Undergoing private placement transactions while at the same time agreeing to list the shares on the N-OTC market is a fast-track way to access fresh capital.

Bermuda shipping companies commonly use the N-OTC as a stepping stone to a full listing on Oslo Axess or the Oslo Stock Exchange. As of March 2020, there were 26 Bermuda companies listed on the Oslo Bors and the NOT-C combined, with a total market capitalisation of over US\$7 billion, many of whom are MJM clients.

Over the years, strong working relationships have been forged with Norwegian law firms and financial institutions, which helps to ensure a smooth pathway to accessing capital in Oslo. Also, we have a wealth of experience with New York initial public offerings should a NYSE or Nasdaq listing beckon. There are a number of Bermuda shipping and shipping-related companies that maintain New York listings.

3 | Are there any recent domestic or international political or legislative developments that may have an impact on your country's shipping market?

Following a commitment by the Bermuda government to the European Union to address concerns that the jurisdiction should not facilitate offshore structures or arrangements aimed at attracting profits that do not reflect real economic activity in the jurisdiction, legislation requiring entities to maintain a substantial economic presence in Bermuda came into effect last year. Similar legislation has been enacted in other offshore jurisdictions, and the EU's economic substance requirements are expected to soon become a global Organisation for Economic Co-operation and Development-standard.

All entities carrying on relevant activities must comply with full economic substance requirements. These requirements will be met if the entity is managed and directed in Bermuda, core income-generating activities are undertaken in Bermuda with respect to the relevant activity, the entity maintains adequate physical presence in Bermuda, there are adequate full-time employees in Bermuda with suitable



qualifications and there is adequate operating expenditure incurred in Bermuda in relation to the relevant activity.

Entities must file an economic substance declaration annually, with information provided in relation to the previous financial year, no later than six months after the last day of each relevant financial period. The declaration must demonstrate compliance with the economic substance requirements. There is an offence of knowingly making a false economic substance declaration.

The Bermuda Registrar of Companies is responsible for implementation, monitoring and enforcement. The Bermuda Registrar has issued guidance notes comprising general principles confirming that relevant activities are being carried on as a business where an entity earns any gross income in respect of such activity during the relevant financial period and indicating that, in the analysis of each entity, the Registrar will have regard to the nature, scale and complexity of an entity's business, and will apply criteria such as 'adequacy' in that context.

Shipping is one of the 'relevant activities' within the scope of the economic substance requirements. Sector-specific guidance notes that give contour to the relevant activity of shipping for the purpose of determining adequate economic

substance have been published in draft form by the Bermuda Registrar. At present, this guidance remains subject to approval by the European Union. It is anticipated that when finalised, this guidance will provide further clarity to the application of economic substance requirements to shipping entities.

For example, in determining whether a shipping entity meets such requirements, the Bermuda Registrar recognises that significant activities within shipping are performed in transit outside of Bermuda, and that the value creation attributable to shipping core income-generating activities that occur from a fixed location is more limited than for other relevant activities. This would suggest that meeting these requirements may not be as difficult as may be initially thought.

Also, where a ship owner charters a ship to another entity on a bareboat charter basis, the owner will generally not be carrying on shipping because it does not operate the ship. The entity chartering the ship on a bareboat charter basis will be carrying on shipping because it is transporting goods for a charge in connection with the operation of a ship.

In addition, where a ship is chartered, the question of whether the ship owner or the entity chartering the ship (or both) are carrying on shipping may be determined by the terms of the relevant charter party. It is, therefore, possible that both a ship owner and a charterer are operating a vessel if they undertake aspects of operation of the ship.

Moreover, where an entity that carries on shipping submits evidence to the Bermuda Registrar that it is liable to a tonnage tax regime in a jurisdiction outside of Bermuda, it is expected that the Bermuda Registrar may regard that entity as being exempt from the requirements of the economic substance legislation.

We feel that the registration of vessels on the Bermuda Ship Register will be an important way of demonstrating adequate economic substance for the purposes of the legislation. It has long been the case that vessels owned by companies in the UK, any British territory and most European countries (including Greece) could be registered in Bermuda, and it is particularly noteworthy that the Merchant Shipping (Registration of Ships) Regulations were amended last summer to permit vessels owned by companies incorporated in the Bahamas, Hong Kong, Liberia, Marshall Islands, Panama, Singapore and South Korea to now be registered in Bermuda.

These changes, along with competitive fee pricing for shipping groups that register multiple vessels or use a Bermuda-incorporated vessel-owning entity and have a principal place of business in Bermuda, enhance Bermuda's reputation as a desirable jurisdiction for international shipping groups.

“Where a ship is chartered, the question of whether the ship owner or the entity chartering the ship are carrying on shipping may be determined by the terms of the relevant charter party.”



4 | What are the key regulatory and compliance issues for your country's shipping market? What's coming up in the near future?

We are seeing the Poseidon Principles now being referenced in ship financing documentation. The aim of this global framework, agreed to, and published by, 12 leading banks that jointly represent approximately 20 per cent of the global ship finance portfolio, is to improve the role of maritime finance in addressing global environmental issues. Signatories to the Poseidon Principles are some of the leading maritime financial institutions that have agreed to annually report the overall climate alignment of their respective shipping portfolios and supporting information each year. 'Climate alignment', according to the Poseidon Principles, is the degree to which a vessel's (or portfolio's) carbon intensity is in line with the the International Maritime Organization (IMO)'s decarbonisation trajectory for the respective ship type and size class.

The Poseidon Principles are incorporated into credit agreements through a covenant whereby owners agree to provide lenders with any information they require to comply with the Poseidon Principles. The Poseidon Principles provision

has made its way into loan agreements as a result of maritime lending institutions taking on a larger role in developing solutions for the global environmental issues identified by the IMO.

In practical terms, the provision regarding Poseidon Principles is not particularly burdensome for borrowers, who are generally required through other provisions in their loan agreements to report information regarding vessel operations, IMO compliance and emissions as lenders may reasonably require, but it signals a commitment on all parties to shape a more environmentally responsible shipping industry.

In a similar vein, more than a decade in the making, the IMO 2020 rule mandating lower sulphur emissions from the shipping industry came into effect on 1 January 2020. The new regulations have been the subject of much concern and predictions of vast disruptions and impacts to shippers, customers and producers of diesel fuel since they were first proposed by a United Nations subcommittee, and were subsequently adopted in 2016 by the IMO. Despite those predictions, however, the final implementation of the new rules has resulted in few real disruptions, as extensive planning and preparation has ended up ensuring proper performance in the marketplace.

While most shippers seem to have chosen to use the lower-sulphur fuel option, rather than to install scrubbers on their vessels, the availability of multiple options for the regulated community to achieve compliance has proven to be helpful in avoiding disruptions in the marketplace.

IMO 2020 deals with the reduction of sulphur only, and further rule changes governing carbon emissions are under consideration, with changes coming to mandate carbon reductions, and that is the next wave of what we will see influencing the cleanliness of marine fuel.

On the ship finance side of things, the discontinuance of LIBOR (expected in 2021) has started to gain attention, both from industry participants and the regulators. Shipping being a capital-intensive industry and heavily dependent on LIBOR-based bank debt, LIBOR's impending sunset will have a major impact. The replacement of LIBOR is an important, but fluid issue, fraught with uncertainty, and both borrowers and lenders alike will need to review their loan documentation carefully and keep up to date with the latest market developments in this area.

“More refinancing and restructuring transactions are likely to be on the horizon, as some ship owners struggle to meet the repayment demands of loans.”

5 | What are the shipping industry's current sources of finance? How do you predict they will develop, and what are the advantages and challenges to financing a vessel in your country?

Historically, particularly with regard to the Europe-based shipping companies, the traditional source of finance was their local banks. While some of those banks are still operating in the shipping space, many of those that remain are doing so in much smaller volume and with increased restrictions and harsher covenants. Others have pulled out entirely, deeming the shipping sector too volatile.

What is coming in to replace them is a blend of various sources of finance. Private equity is prepared to invest on the right terms, even entering into joint ventures for certain projects. Chinese leasing companies are entering into sale and leaseback transactions and those that have gone public have increased their access to fundraising on the capital markets. Others have looked to borrow from non-traditional banking institutions keen to enter the market or expand their customer base into new jurisdictions.

The emergence from lockdown in the Northern Hemisphere will be closely watched by lenders, with the expectation that global economies will start to recover. It is thought that any nascent recovery may turn out to be volatile and fragile and that, in this recovery period, many banks will be solely focused on their own loan-related issues. Loan requests are expected to increase as the global economy, international trade and the dry bulk market start to recover. It is hoped that equity market investors start to return, as both the economy and the shipping sector bounce back in the second half of the year, although the capital markets are bound to reflect the global uncertainty of the post covid-19 world for a while longer yet. As a result, we are likely to see even more creative financing solutions, as the need for new finance outstrips the availability from the usual quarters.

6 | Have there been any recent significant domestic or foreign court decisions or arbitration awards that impact on your country's shipping market?

We cannot recall any one specific judgment delivered recently that has made a significant impact on Bermuda's shipping market. Most of the shipping documentation involving Bermuda-incorporated shipping companies may be challenged in the courts, which tend to grant jurisdiction over disputes to the English courts, or sometimes courts in New York or Oslo.

7 | What is the outlook for your country's shipping market? Which sectors are likely to grow, and which not?

We are likely to see fewer companies looking to go public in the foreseeable future, as the depth of the downturn following the global pandemic is ascertained with more certainty as the year goes on. More refinancing and restructuring transactions are likely to be on the horizon, as some ship owners struggle to meet the repayment demands of loans entered into before the lockdown. We may even see further recourse to Chapter 11 proceedings, in the hope of using it to agree a negotiated restructuring once all other options have been explored. Some consolidation in the market cannot be ruled out, as those companies that are undervalued in a weak market may find predators keen to swoop.

More diverse and creative forms of ship finance will be used to replace the traditional ship finance banks, while ethical and 'green' financing is here to stay. The IMO will, no doubt, continue on its path towards demanding cleaner marine fuel and the digital transformation of the shipping industry, including the use of blockchain platforms for sale and purchase of good and logistics and automated crewless ships controlled from an onshore command centre, gathers pace.

Here in Bermuda, we are now seeing the first deadline for the economic substance submissions and it will be interesting to see which of the shipping companies seek to bolster their on-island presence to ensure compliance going forward.

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The Inside Track

What are the particular skills that clients are looking for in an effective shipping lawyer?

Given our role as offshore counsel, we must be responsive to the demands of the onshore law firm through which the ultimate client instructs us. As such, a stand-out Bermuda lawyer must have a solid grounding in shipping-related capital markets and bank finance and must be extremely responsive, cognitively dextrous, forward-thinking, capable of advising on local law requirements at short notice. A shipping lawyer must also be flexible, given the time differences that are inherent in our firm's international shipping finance practice and the critical importance of market timing to our clients.

What are the key considerations for clients and their lawyers when arranging finance for a shipping transaction?

Ship financing for Bermuda lawyers usually comprises assisting onshore counsel with implementing the chosen method of finance for a shipping transaction. Most, if not all, of the key considerations would originate in the jurisdiction of the lenders, which in our experience has most often been that of the major Nordic banks.

Mortgages, transfers and discharges of registered mortgages can be made in prescribed form for registration. Mortgages rank in priority according to the date and time at which they are produced and accepted for registration and not according to the date of the mortgage deeds themselves.

What are the most interesting and challenging cases you have dealt with in the past year?

Numerous legal issues were dealt with advising an Oslo Stock (OSE) exchange-listed Bermuda shipping-related company on the spin-off of its fleet of semi-submersible rigs into a wholly owned Bermuda subsidiary. We also advised on an exchange offer in connection with the spin-off and the listing of the former subsidiary on the OSE. Another matter saw a seller issued with ordinary shares of a NY-listed Bermuda shipping company client of the firm as partial consideration for its sale of a company that held 10 Suezmax vessels, plus further shares issued pursuant to two validly exercised options to purchase a company that had the option to acquire a further four Suezmax vessels. We worked long hours in conjunction with Norwegian and US counsel to ensure the conclusion of this transaction in just one week.

Lexology GTDT Market Intelligence provides a unique perspective on evolving legal and regulatory landscapes.

Led by MFB Solicitors, this *Shipping* volume features discussion and analysis of emerging trends and hot topics within key jurisdictions worldwide.

Market Intelligence offers readers a highly accessible take on the crucial issues of the day and an opportunity to discover more about the people behind the most significant cases and deals.

Covid-19 impact
Financing
Sector focus
2021 outlook