



VedderPrice

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Inside

GIFT City: A Gift for Aircraft Lessors?

Get Ready! EU Emissions Trading System Expands to Cover Maritime Sector; Effective January 1, 2024

Recent Amendments to Marshall Islands and Liberian Maritime Laws Help Bring Clarity to Common Vessel Mortgage Questions

GIFT City: A Gift for Aircraft Lessors?

Gujarat International Finance Tec-City (**GIFT City**) was established in 2007 as India's first operational smart city and an emerging global financial and IT services hub located in Gandhinagar, Gujarat. GIFT City is a personal project of Prime Minister Narendra Modi and is intended to be a centre for foreign investors to transact in Indian securities with minimal tax and bureaucracy. GIFT City allows non-Indian nationals to become corporate inhabitants and firms such as the Abu Dhabi Investment Authority (the UAE's largest sovereign wealth fund), JP Morgan Chase, MUFG and Bank of America have all set up entities in GIFT City.

As a result of reforms introduced in India in 2020, aircraft leasing is now recognized as a financial product. Entities in GIFT City are now able to finance and lease aircraft with the added flexibility to transact in foreign currency. This reform has led to the development of the aviation sector in GIFT City, and helicopter lessors such as Vman Aviation and business jet lessors such as ModAir Aviation, and commercial airlines such as IndiGo and Air India, have established presences in GIFT City. Having two Indian airlines commit to establishing leasing entities in GIFT City has been seen as a key developmental milestone in India for the government, which has been keen to attract aircraft leasing businesses within India given the success of centres such as Dublin and Singapore.

This year, there have been significant transactions structured through GIFT City including TATA-owned Air India securing the first of six Airbus A350-900 aircraft scheduled to join its fleet through its aircraft leasing entity in GIFT City. In June 2023, IndiGo ordered 500 new aircraft, the biggest aircraft order ever made, and is understood to be planning to receive its first aircraft through its aircraft leasing entity in GIFT City.

What are the benefits enjoyed by GIFT City residents?

Entities established within GIFT City enjoy the unique status of 'persons resident outside India' under Indian foreign exchange laws, granting them the freedom to conduct transactions in freely convertible international currencies without the need for Reserve Bank of India (**RBI**) approval. Provided that the GIFT City entity commences operations on or before March 31, 2024, GIFT City offers its corporate inhabitants favourable tax benefits, such as the following:

- a 100% income tax holiday for any 10 consecutive years during the entity's first 15 years of operation;
- a 100% exemption from capital gains tax on the transfer of specified securities, including aircraft assets, made within any 10 consecutive years of the entity's first 15 years of operation;
- a 100% exemption from stamp duty for aircraft leasing entities on all activities related to setting up the GIFT City entity, including the acquisition of aircraft, commencing from August 2020 for a period of 10 years;
- no goods and services tax (**GST**) payable on aircraft leased into a GIFT City entity or services received by a GIFT City entity provided, however, that a rate of 5% GST is applicable on any operating lease rentals received by the GIFT City entity from an Indian airline based outside of GIFT City in a domestic tariff area;
- no basic custom duty on import of commercial aircraft by a GIFT City entity; and
- a one-stop regulator: the unified International Financial Service Centre Authority (the **IFSCA**) provides the only regulatory clearance required for GIFT City entities, which is a marked change from the process elsewhere in India, where entities are required to approach separate regulators for separate approvals relating to banking, insurance, pension and foreign exchange regulations.

GIFT City's tax incentives have sought to simplify certain aircraft lease complexities arising from Indian tax law, such as the requirement to pay unpaid GST upon an aircraft repossession. Historically, upon an aircraft repossession, any GST unpaid by the airline could become a hurdle to repossession requiring the lessor to pay the unpaid amount as a condition to obtaining possession of the aircraft. Indian airlines leasing aircraft from GIFT City entities are required to pay GST on a forward charge basis to the GIFT City lessor; by ensuring that GST is paid in advance with lease rentals, it seems less likely that a lessor would be liable for any outstanding amounts of GST upon an aircraft repossession.

Shareholder **Edward K. Gross** recently co-authored "Leases" Survey in the ABA's Fall 2023 *The Business Lawyer*. The Survey covers several commercial enforcement, bankruptcy protections and other claimed rights, including the associated rights and interests and liability considerations relating to these leases and financings. To read "Leases" in its entirety, download it [here](#).

Shareholder **John F. Imhof Jr.** recently co-authored, with retired Vedder Price Shareholder Francis X. Nolan, III, a chapter on the *Financing of Vessels in LexisNexis/Matthew Bender's Treatise on Equipment Leasing*. The chapter provides an in-depth analysis of the legal aspects of vessel financing, including registration, finance charters, mortgages and other maritime liens, arrests, foreclosures, bankruptcy and restructuring, with particular focus on the maritime laws of the United States and leading open-registry states Liberia and the Marshall Islands. The chapter also contains an analysis of the recently adopted Beijing Convention on the Judicial Sale of Ships. Global Transportation Finance Associate John H. Geager assisted with the preparation of the chapter.

Shareholder **John F. Imhof Jr.** recently published a chapter on ship finance in the *Marshall Islands in Lexology's Getting the Deal Through – Ship Finance 2023*. In the latest volume of the series of annual reports that provide analysis in key areas of international ship finance law and policy, John writes about Marshall Islands ship registration, preferred ship mortgages and other maritime liens, mortgage enforcement, finance charters, and insolvency and restructuring, as well as recent developments related to the finance of Marshall Islands-flagged ships.

Incorporating a corporate entity in GIFT City

International lessors are able to establish corporate residency in GIFT City either as companies, limited liability partnerships or trusts with a minimum owned fund of US\$200,000 (or equivalent), if the entity wishes to engage in the business of operating leasing only, or US\$3,000,000 (or equivalent), if the entity wishes to engage in finance leases or a mix of operating and finance leases. These entities are able to deal in freely convertible currency and can maintain an Indian Rupee account too, which may be useful in settling administrative expenses.

The process to set up an entity within GIFT City is estimated to typically take three months, but this timing may be further reduced if the IFSCA waives certain requirements and implements the “single window clearance” system, which would reduce the amount of authorities from which approval is required, and which is currently under consultation. In light of the increased interest in GIFT City following the arrival of Air India and IndiGo, the IFSCA is also considering whether the March 31, 2024 tax exemption deadline may be further extended. However, it remains prudent for any interested lessor or financier to initiate the GIFT City incorporation process earlier rather than later in order to meet the existing deadline.

In addition, the growth of leasing entities and other special purpose vehicles within GIFT City has also facilitated an expansion in corporate service providers offering registered entities in GIFT City, improved efficiency and cost-saving opportunities.

What is the impact to Lessors leasing to GIFT City entities?

Tax

GIFT City inhabitants are not deemed to have a permanent establishment in India and will be able to distribute profits and other income streams to group businesses outside India, which should be welcome news to any financiers and lessors that have experienced challenges with the Indian tax authorities, or otherwise become the subject of Indian tax investigations.

Jurisdiction/RBI Approval

By leasing through a lease-in/lease-out structure via GIFT City, a financier or lessor can limit its jurisdictional risk if an airline establishes a special purchase company (SPC) as resident in GIFT City. If the aircraft is leased to the SPC and then subleased from the SPC to the airline, payments made under the head lease from the SPC to the financier or lessor should benefit from the tax benefits explained above. Although payments made from a GIFT City entity to a non-Indian company do not need RBI approval, if the financier or lessor requires a guarantee of the SPC’s obligations from the Indian airline, any guarantee payments may require RBI approval.

GIFT City has the potential to act as a catalyst for the growth of the aviation sector in India. With the presence of leading airlines like IndiGo and Air India, combined with the tax benefits it offers, GIFT City is emerging as a hub for aviation-related businesses. As GIFT City continues to grow and evolve, its impact on the aviation sector may contribute to the development of a more dynamic and globally competitive industry in India.

Insolvency and the Cape Town Convention: an Indian Update

As well as the extension of GIFT City to aircraft leasing, the Indian government has taken steps to cement the proper application of the Cape Town Convention (the **Convention**) and Aviation Protocol (the **Protocol**) in India in recent years.

Improvements have been made in Indian domestic law since the insolvencies of Kingfisher Airlines and Jet Airways. While India had acceded to the Convention and the Protocol in 2008, it did not fully implement it into Indian law.

In 2017, amendments were made to the Indian Aircraft Rules, 1937, which codified the relevant provisions of the Convention and Protocol relating to de-registration and export of aircraft into Indian law, and in 2022 the Indian government introduced a Protection and Enforcement of Interests in Aircraft Objects Bill, 2022 (the **Bill**), to fully implement the Convention and Protocol into Indian law for the purposes of providing lessors and financiers added comfort of the protections, rights and timelines awarded by the Convention and Protocol.



Vedder Price Ranked by U.S. News – Best Lawyers 2024

U.S. News – Best Lawyers, a publication of U.S. News & World Report, has ranked Vedder Price and the Global Transportation Finance team with top-tier status in Equipment Finance Law and Tier 2 in Admiralty & Maritime Law. Additionally, on the Metropolitan level, we received Tier 1 status in Equipment Finance Law in New York City and Washington, DC, and ranked Tier 2 in Admiralty & Maritime Law in New York City.



Vedder Price Distinguished in Chambers UK 2024

Chambers UK 2024 recognized the Global Transportation Finance London team as **Top-Tier Firm/Tier 2** in Asset Finance: Aviation Finance.

Gavin Hill and Neil Poland were recognized as **Leading Individuals** and Dylan Potter was recognized as **Next Generation Partner**. In addition, Gavin Hill, Neil Poland, Derek Watson, Dylan Potter, John Pearson and Natalie Chung were **Editorially Recommended**.

The Bill is currently pending approval of the Indian parliament and it is unlikely that the Bill will be approved ahead of the 2024 Indian general elections. However, as an interim measure and to ensure timely repossession of aircraft in instances of airline insolvencies, the Ministry of Corporate Affairs issued a notification on October 3, 2023 disapplying the moratorium provisions of section 14(1) of Indian Insolvency and Bankruptcy Code, 2016, to transactions, arrangements or agreements under the Convention relating to aircraft, aircraft engines, airframes and helicopters.

As a result, on October 5, 2023, the Cape Town Convention Compliance Index maintained by the Aviation Working Group upgraded India's rating from negative to positive. However, it is not clear whether this notification will apply retrospectively to give relief to the lessors of Go Air currently subject to an insolvency process, which is currently under contention in the Delhi High Court, with several hearings relating to the Go Air insolvency scheduled to be heard in December 2023.



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November 30, 2023

John F. Imhof Jr. presented at the 2nd Annual Marine Money Marine Finance Forum in New Orleans. John interviewed Brendan Crystal, Vice President of ATLAS SP, in a session entitled "Tapping the Securitization Market with Maritime Assets." They discussed asset securitization as a source of financing for the Jones Act and U.S.-flag maritime industry.

November 16, 2023

Dylan Potter participated in the 24th Annual Ship Finance Forum held in New York City. Dylan interviewed Helene Becker, Managing Director of TD Cowen, in the "What Ship Finance and Investment Can Learn from the Airline Industry" session. The focus of this session was how the shipping industry can learn from the more mature airline industry.



November 6-8, 2023

Cameron A. Gee presented at the 2023 Airline Economics Growth Frontiers Asia Pacific Conference in Singapore. Cameron moderated the JOL & JOLCO panel on Tuesday, November 7th. Additionally, he participated in the Aviation Finance & Leasing School on Wednesday, November 8th, with his session on PDP Financing 101.

November 6-8, 2023

David M. Hernandez and **Edward K. Gross** participated in panel discussions at the Corporate Jet Investor Conference in Miami. David and his panelists participated in the "Who wants to be an aircraft trustee" session that addressed the topics of the FAA rejecting non-citizen ownership and what the future for trustees entails. Eddie moderated the "Financing aircraft" session focusing on aircraft finance topics, including interest rates and inflation, when an aircraft gets old, and business aviation deals.

Get Ready! EU Emissions Trading System Expands to Cover Maritime Sector; Effective January 1, 2024

Under the European Climate Law,¹ European Union (EU) Member States are working collectively to reach net zero – cutting greenhouse gas emissions as close to zero as possible – by 2050. As a first milestone, the EU is aiming to reduce net emissions by at least 55% by 2030, when compared to a 1990 baseline. The shipping industry is crucial to global trade, but it also contributes significantly to greenhouse gas emissions. To achieve the necessary emission reductions, the scope of the EU Emissions Trading System (ETS) has been expanded to include maritime transport emissions, effective January 1, 2024, with a two-year phase-in period.

Background and Goal Setting

Launched in 2005,² the EU ETS is the world's first international emissions trading system and currently stands as a major pillar of EU energy policy. The EU ETS applies in all 27 EU Member States and the European Free Trade Association countries (Iceland, Liechtenstein and Norway). In general, the EU ETS makes polluters pay for their greenhouse gas emissions, encouraging emitters to reduce their emissions and generating revenue to help finance the EU's transition to net zero.

Cap and Trade

The EU ETS works on the 'cap and trade' principle; the system aims to incentivize emission reduction efforts by penalizing companies that exceed their allocated allowances and rewarding those that emit below their limits. A cap is set on the total amount of greenhouse gases that can be emitted by the installations, aircraft operators and ships covered by the system. The cap is expressed in emission allowances, where one allowance gives the right to emit one tonne of carbon dioxide equivalent. The cap is reduced annually in line with the EU's climate target, ensuring that total emissions decrease over time.

Annually, companies must surrender sufficient allowances to fully account for their emissions in the preceding year, by reducing emissions to below their allocated allowances or purchasing allowances, otherwise heavy fines are imposed. Within the cap, a Shipping Company³ can buy allowances in the primary market through auctions on the European Energy Exchange (EEX). There is also a secondary market in which allowances can be sold bilaterally or through various derivatives provided by financial institutions and on exchanges such as ICE, EEX and Nasdaq and on the over-the-counter market. If an installation or operator reduces its emissions, it can then choose to either keep the spare allowances to use in the future or sell them, noting that any allowances issued after 2013 do not expire.

Scope

Starting from January 1, 2024, the EU ETS will apply to vessels engaged in the commercial transportation of cargo or passengers above 5,000 gross tonnage. In 2027, offshore vessels above 5,000 gross tonnage will also come under its scope and there will be an evaluation on whether to include offshore vessels of 400 to 5000 gross tonnage in 2027.

The EU ETS covers emissions that can be measured, reported and verified with a high level of accuracy: carbon dioxide (CO₂), nitrous oxide (N₂O) and perfluorocarbons. As it relates to the shipping industry, CO₂ will be covered in the initial 2024 reporting period, with both methane and N₂O being covered beginning in the 2026 reporting period.

100% of emissions from ships performing voyages between EU ports as well as 100% of emissions from ships within an EU port (i.e., docked) will fall within the scope of the EU ETS. In addition, 50% of the emissions from ships performing voyages between an EU port and a non-EU port will fall within the scope of the EU ETS. In each case, this is regardless of the proportion of the voyage that occurs outside of the EU or the EEA's territorial waters.

Following the 2025 reporting period, representing emissions from 2024, allowances equivalent to 40% of the emissions falling under the EU ETS must be surrendered. Following the 2026 reporting period (being 2025's emissions) this increases to 70%, with this increasing to 100% the following year.

Under the EU ETS, the owner of a vessel is always responsible for compliance with the EU ETS mandate for that vessel. Each owner will be associated with the administering authority of an EU Member State.

October 17, 2023

Kevin A. MacLeod participated in an interactive discussion on the unsecured bond market at the Ishka Aviation Investival: North America event held in New York City. Kevin participated with other industry colleagues in the "Is this unsecured bond market now fully open for aviation credits" session.



September 6-7, 2023

Edward K. Gross moderated a session at the Revolution.Aero in San Francisco. Eddie's session entitled "How can OEMs finance production" focused on debt versus equity, using government incentives, managing supply chains, and customer finance and support.

DEAL CORNER

Vedder Price Advises De Lage Landen Financial Services, Inc. in \$1B Securitization Transaction of Agricultural Equipment Financings

Vedder Price is pleased to announce that it represented De Lage Landen Financial Services, Inc.'s (DLLFS) affiliates, AGCO Finance LLC (AGCO Finance), as originator and sponsor, and DLL Finance LLC (DLL Finance), as servicer, in connection with the DLLAA 2023-1 securitization that closed recently, issuing notes totaling \$1 billion. The notes are backed by secured loans and leases involving new and used agricultural equipment originated by AGCO Finance, a joint venture between DLL U.S. Holding Company, Inc. and AGCO Corporation. Vedder Price previously advised DLL Finance in connection with a securitization transaction that closed in February 2023, and DLLFS in connection with a securitization transaction that closed in May 2023. The Vedder Price team was led by both Capital Markets Shareholder Kevin A. MacLeod and Global Transportation Finance Shareholder Edward K. Gross.

For ships registered in the EU, the administering authority will be that EU Member State. For ships not registered in the EU, the EU Member State with the greatest estimated number of port calls from voyages performed by that ship in the last four monitoring years will serve as the administering authority. If a ship is not registered in an EU Member State and did not carry out any voyage falling within the preceding four monitoring years, the administering authority will be the EU Member State where that ship first arrives or starts its first voyage.

A shipowner is allowed to delegate this responsibility to a third party and the parties are expected to agree upon reimbursement arrangements for the costs arising from surrendering of allowances. If a shipowner does elect to delegate this responsibility, it must deliver documentary evidence of that delegation to the applicable administering authority.

Requirements and Associated Sanctions for Failure to Comply

The EU has determined that the monitoring and reporting of greenhouse gas emissions must be robust, transparent, consistent and accurate for the EU ETS to operate effectively. The annual procedure of monitoring, reporting and verification (MRV) and all of the associated processes is known as the “ETS compliance cycle.”

During the ETS compliance cycle, each Shipping Company covered by the EU ETS is required to have an approved monitoring plan for monitoring and reporting annual emissions. Further, on an annual basis, operators must submit an emissions report for each ship under their responsibility and an emissions report must be submitted at the company level as well. The data for a given year must be verified by an accredited verifier by March 31 of the following year. Once verified, owners must surrender the equivalent number of allowances by September 30 of that year. Accordingly, the first ETS allowances for shipping will be surrendered by September 30, 2025 for emissions reported for 2024.

All operators in the EU ETS must surrender annually the number of allowances corresponding to their emissions in the preceding year. For each tonne of emissions for which no allowance is surrendered in due time, there is a penalty of EUR 100 (adjusted in accordance with the European consumer price index). This penalty is in addition to the cost of surrendering the allowances due. Names of the penalized operators are also disclosed to the public. The severity of sanctions continues to escalate until, in a worst-case scenario, ships may be denied permission to trade, or may even be expelled, from the EU.⁴

Considerations and Anticipated Challenges

The integration of the shipping industry into the EU ETS represents a significant milestone in the pursuit of a sustainable maritime sector: close collaboration with authorities, port operators and stakeholders necessary to comply with the EU ETS may lead to the development of more efficient vessels, the use of renewable energy sources and the adoption of other emission reduction strategies that benefit the entire industry.

For example, Shipping Companies may want to optimize vessel routes, reduce idle times and adopt slow steaming practices to align with emission reduction targets. These actions will require careful planning and coordination to maintain the efficiency and effectiveness of supply chain logistics. Shipping Companies which have already started adopting practices to aid the reduction of emissions will need to consider how the EU ETS requirement interacts with their existing frameworks. For example, emissions resulting from the combustion of sustainable biomass compliant with the sustainability criteria established by the Renewable Energy Directive⁵ have an emission factor of zero under the ETS. However, if a company already offsets their emission through a different scheme, they will still have to report under the EU ETS Directive.⁶

To stay within their allotted allowances, substantial capital investments will also likely be necessary for the eventual adoption of emission-reducing technologies and sustainable fuel alternatives.

As a marketplace being driven by supply and demand, there will be some unpredictability regarding the underlying price of the allowances, which Shipping Companies will have to absorb during the first stages of adoption by accounting for likely additional expenses, while they build familiarity with the compliance requirements and the market dynamics. Large shipping and logistics companies have already announced plans to pass the costs of the EU ETS as a surcharge applied to all bookings and incentivize customers to book on “eco” deliveries which use less-polluting fuels. Upcoming regulations like FuelEU Maritime⁷ aimed at increasing the demand for and consistent use of renewable and low-carbon fuels and reducing the greenhouse gas emissions from the shipping sector, will focus specifically on the shift to low-carbon or renewable fuels, expected to take effect after 2025.

For the purposes of the legislation, and in line with MRV requirements, the Shipping Company will be the holder of the Document of Compliance (DOC). Shipping Companies will also need to work with their technical teams and management companies when considering the identity of the DOC holder to make sure that this does not present any logistical issues. For example, DOC holders are often management companies which may not be equipped for dealing with the business of buying and surrendering allowances for multiple owners during the same reporting period.



Global Transportation Finance Associate **John Pearson**, along with Lev Gantly (Philip Lee LLP) and Robert Stevens (Climate Impact Partners) co-wrote an article entitled *CORSIA – it’s (almost) crunch time* where they explore the global aviation industry’s efforts to address climate change. CORSIA’s First Phase is approaching, leading to an increased demand for Eligible Emissions Units. Aircraft lessors and financiers have an opportunity to support sustainable projects and contribute to emissions reduction goals.



The Global Transportation Finance team attended two major environmental conferences in the month of November: Aviation Carbon 2023 on November 6 and 7 in London Heathrow and the Aircraft Leasing Ireland’s Global Aviation Sustainability Day on November 20 in Ireland.



Our dedicated team has been on an inspiring mission alongside our esteemed pro bono client, a trailblazing company dedicated to promoting green consumer travel choices. Together, we are harnessing our industry expertise to elevate their understanding of the aviation ecosystem, reaching beyond the surface to navigate the intricacies of sustainable practices up the aviation food chain. By sharing our insights and working in tandem, we aspire to contribute meaningfully to their mission of fostering sustainable choices in the world of travel. Stay tuned for more updates on this exciting project.



We are thrilled to announce the involvement of John Pearson in the upcoming **Airline Economics’ Sustainable Aviation Fuel and Carbon Finance Day** on February 1, 2024. John not only played a crucial role in organizing this groundbreaking event but will also take center stage as a distinguished panel moderator and conference co-host.

Given the multi-layered approach to vessel operation and the numerous parties involved, it is anticipated that the EU ETS cost arrangements will be addressed and documented by EU ETS specific contractual clauses which will need to be included in relevant documents such as sale and purchase agreements, charterparties and contracts of affreightment. Emissions will also play a more significant role when negotiating chartering arrangements as parties will need to agree upon an allocation of responsibility scheme for bearing the costs of compliance with the EU ETS. Baltic and International Maritime Council (BIMCO) has already produced an 'ETS - Emissions Trading Scheme Allowances Clause for Time Charterparties' which we anticipate will form the basis of negotiations between owners and charterers.

Next Steps

While the EU ETS for shipping begins on January 1, 2024, there are still many issues that are under consultation that will need to be monitored, such as:

- necessary rules, templates and methods to ensure the good functioning of the system;
- sector-specific rules and templates (for monitoring plans, emissions reports and reports at company level) in relevant implementing and delegated acts which are yet to be adopted by the end of 2023, to ensure uniform implementation of the EU ETS and MRV rules;
- adoption by the EEA countries, which is yet to be confirmed;
- contractual clauses to address reimbursement for costs arising from surrendering of allowances by charterers; and
- an attribution list concerning administering authorities.

As the new regime is implemented, stay tuned for updates from the Vedder Price team.



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The Global Transportation Finance team hosted a dinner on November 15 at Del Frisco's Double Eagle Steakhouse in connection with the 2023 Marine Money Ship Finance Forum in New York City. It was a wonderful evening of networking with clients and colleagues in the maritime industry. Thank you to all who attended!



Recent Amendments to Marshall Islands and Liberian Maritime Laws Help Bring Clarity to Common Vessel Mortgage Questions

Both the Marshall Islands and Liberia, two of the three largest open ship registries in the world, recently enacted certain important amendments to their respective maritime laws that bring clarity to common questions surrounding vessel mortgages. In part, the amendments to the Liberian Maritime Law, which went into effect in August 2022, clarify to some extent that one need not attach evidence of the obligations secured by Liberian vessel mortgages to these mortgages and clarify the circumstances under which mortgages must be amended following modifications to underlying secured obligations.¹ In 2023 the Maritime Act 1990 of the Republic of the Marshall Islands was amended to clarify what may constitute written proof or evidence of the amounts and dates of any documents or evidence of mortgage debt to be submitted with or included in vessel mortgages, among other amendments affecting vessel registration and operation.² Both nations' recent maritime law amendments also included other important amendments that are relevant for both ship-owners and financiers alike, including amendments (in both Liberia and the Marshall Islands) that made permanent the ability for instruments to be filed electronically,³ continuing a practice that was born out of the need to eliminate in-person filings during the COVID-19 pandemic.

The recent amendments to Liberian maritime law have made clear that, to be enforceable under Liberian law, a vessel mortgage must recite, among other things, "the instrument or instruments which evidence the direct and/or contingent obligations secured by such mortgage ... including the date of each such instrument and the parties thereto," but is not required "to ... annex any copies or summaries of the instrument(s) which evidence the direct and/or contingent obligations secured thereby, or ... any copies or summaries of any agreement or other document that is incorporated by reference into the mortgage...."⁴ Similarly, the Marshall Islands law that had already required the submission of "written proof ... of the amounts and dates of any documents or evidence of debts in support" of a vessel mortgage was amended to provide that such written proof or evidence of debt *may* be satisfied by attaching to the mortgage the documents evidencing such debt (whether in whole, in part or with or without redactions), or by describing the terms of the debt in the mortgage, including the total amount."⁵ While the amendments eliminate the previous uncertainty around attaching underlying instruments to Liberian and Marshall Islands vessel mortgages as a matter of Liberian and Marshall Islands law, secured lenders and their counsel may still wish to attach to a mortgage all of the documents setting forth the obligations secured even if the amendments appear to eliminate the need to do so. It remains somewhat uncertain whether another jurisdiction in which a Liberian or Marshall Islands vessel mortgage is enforced might still require the attachment of these documents as a matter of local law.

These amendments are notable for maritime vessel financings, where parties often face the question of whether (and which) underlying debt instruments should be attached to a vessel mortgage as evidence of the underlying mortgage debt secured. This issue is of particular concern in jurisdictions whose maritime law is based on U.S. law, including Liberia and the Marshall Islands, where entire vessel mortgages are typically filed with all these attachments, as opposed to the statutory mortgage filings in so-called "Red Ensign" jurisdictions – British Commonwealth countries and territories. However, these recent amendments to the Liberian and Marshall Islands maritime laws⁶ signal an effort to clear up the sometimes muddy waters around attaching debt instruments to vessel mortgages.

Entire texts could be (and have been) written on the development of ship finance, and in particular the ship mortgage as a financing instrument. After legislative attempts to create a preferred mortgage by the U.S. Congress in the late nineteenth century eventually led to enactment of the Ship Mortgage Act of 1920,⁷ the concept of a chattel mortgage was elevated to that of a maritime lien, requiring a mortgage to meet a short list of additional requirements as to form, content and filing. To create a maritime lien, a "preferred mortgage" must state, among other things, the amount secured, the date the indebtedness matures, the name and official number of the vessel, and the names and addresses of the mortgagor and mortgagee, and be filed in substantial compliance with U.S. federal law.⁸ Importantly, in Liberia and the Marshall Islands, maritime legislation and regulatory provisions generally adopt the non-statutory general maritime law of the United States.⁹

The requirements of ship mortgages are also tied to the varying jurisdictions and national registries that regulate them. The second half of the twentieth century saw the growth of open registries at the expense of national or "closed registries"¹⁰ including Liberia and the Marshall Islands. Open registries are commonly understood to be ship registries that permit registration of vessels under the flag of a nation where the registered owner is not a citizen or resident. As the United Nations Conference on Trade and Development's ("UNCTAD") statistics reveal, closed registry fleets have declined every year in modern memory while the overall inventory of vessels in international trade has expanded. As of 2008, three open registries—Panama, Liberia, and the Marshall Islands—accounted for approximately 42% of the global fleet,¹¹ which has since increased to over 43% as of 2023.¹²

The Global Transportation Finance team gathered for their annual holiday dinner at the iconic Sparks Steakhouse in the heart of New York City. The evening was a delightful blend of camaraderie, festive cheer and networking, bringing together colleagues and friends in the spirit of celebration.



The growth in the number of vessels registered with the Marshall Islands and Liberian registries, and the size and number of mortgages being filed on these vessels, demonstrate how important those jurisdictions have become in international ship finance, prompting some to call for clarity as to whether underlying instruments evidencing mortgage debt must be annexed to a vessel mortgage in order for it to be enforceable and in what circumstances a mortgage must be amended. While there is no express requirement under U.S. law¹³ (or previously under Marshall Islands law¹⁴ and Liberian law¹⁵) that any instruments be (or need not be) annexed, the requirement of stating the particular terms of the underlying obligations secured has led to differing perspectives on how much specificity is required in describing the underlying obligations. Common practice has been to attach copies of the relevant instruments to evidence the obligations secured and the amount of such obligations. This has led to several concerns, including the disclosure of confidential information in the underlying documents attached to recorded mortgages.

Though the amendments to Liberian and Marshall Islands maritime law address the attachment of credit documents to vessel mortgages, there were other notable amendments to each. The amendments to the Liberian Maritime Law also brought an answer to another common mortgage financing question by clarifying that a mortgage will continue to secure obligations notwithstanding certain modifications to these obligations, including changes to the interest rate and payment terms, decreases in the total amount secured or changes to the maturity date (other than an extension of the maturity date stated in the mortgage).¹⁶ The amendments to the Marshall Islands Maritime Act clarify that a mortgage may secure an agreed-upon maximum amount representing all debts or obligations arising or that may arise between the debtor and the creditor within a specified period, “whether or not such debt or obligations arise pursuant to commitments under the relevant agreement between the debtor and the creditor existing at the time the [m]ortgage is recorded.”¹⁷

These amendments, and any similar subsequent amendments to the maritime law of other jurisdictions with respect to vessel mortgage requirements, then bring into question two issues that will likely continue to evolve. First, there is the question of whether the law of the vessel’s flag state requires (or does not necessarily require, as is now clear in Liberia and the Marshall Islands) annexation of the underlying instruments. Second, there is a question of whether the law of the jurisdiction in which a vessel may be arrested requires such annexation for a mortgage on that vessel to be enforceable in that jurisdiction. At this time, it does not appear there have been any cases of vessel arrest that might result in any interpretation of these amendments to Liberian or Marshall Islands law.



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EVENTS cont.

The Women of the Global Transportation Finance team, in partnership with Natixis Corporate & Investment Banking, Macquarie Group, Goldman Sachs and Sun Country Airlines, hosted an uplifting Women in Aviation Reception. It was a dynamic evening of connection with and celebration of the women shaping the future in aviation.



Endnotes

Get Ready! EU Emissions Trading System Expands to Cover Maritime Sector; Effective January 1, 2024

1. Regulation (EU) 2021/1119 of the European Parliament and of the Council of 30 June 2021 establishing the framework for achieving climate neutrality and amending Regulations (EC) Nos. 401/2009 and (EU) 2018/1999.
2. Directive (EU) 2023/959 of the European Parliament and of the Council of 10 May 2023 amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union and Decision (EU) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading system.
3. "Shipping Company" means the shipowner or any other organization or person, such as the manager or the bareboat charterer, that has assumed the responsibility for the operation of the ship from the shipowner and that, on assuming such responsibility, has agreed to take over all the duties and responsibilities imposed by the International Management Code for the Safe Operation of Ships and for Pollution Prevention, set out in Annex I to Regulation (EC) No. 336/2006 of the European Parliament and of the Council.
4. In practice, this means that every EU Member State is required to refuse entry to the ships under the responsibility of the Shipping Company concerned into any of its ports, until the company fulfils its surrender obligations. Where a ship flies the flag of an EU Member State and enters or is found in one of its ports, the EU Member State concerned will, after giving the opportunity to the company concerned to submit its observations, detain the ship until the company fulfils its obligations.
5. Directive (EU) 2018/2001 of the European Parliament and of the Council of 11 December 2018 on the promotion of the use of energy from renewable sources.
6. Directive (EU) 2023/959 of the European Parliament and of the Council of 10 May 2023 amending Directive 2003/87/EC establishing a system for greenhouse gas emission allowance trading within the Union and Decision (EU) 2015/1814 concerning the establishment and operation of a market stability reserve for the Union greenhouse gas emission trading system.
7. Regulation of the European Parliament and of the Council on the use of renewable and low-carbon fuels in maritime transport and amending Directive 2009/16/EC.

Recent Amendments to Marshall Islands and Liberian Maritime Laws Help Bring Clarity to Common Vessel Mortgage Questions

1. See The Liberian Maritime Law, RLM-107, § 105(1) (2022).
2. See The Maritime Act 1990 of the Republic of the Marshall Islands, MI-107 § 307 (2023).
3. See The Maritime Act 1990 of the Republic of the Marshall Islands, MI-107 § 119 (2023); see, e.g., The Liberian Maritime Law, RLM-107, § 100(4) (2022); see also The Liberian Maritime Regulations, RLM-108, § 3-105(2) (2023);.
4. The Liberian Maritime Law, RLM-107, § 105(1) (2022).
5. The Maritime Act 1990 of the Republic of the Marshall Islands, MI-107 § 307 (2023) (emphasis added).
6. See The Liberian Maritime Law, RLM-107, § 105 (2022); The Maritime Act 1990 of the Republic of the Marshall Islands, MI-107 § 307 (2023).
7. Ship Mortgage Act of 1920, 41 Stat. 1000 (codified as amended at 46 U.S.C. §§ 31301–31343) (2018). The Ship Mortgage Act, as amended, was codified into the Commercial Instruments and Maritime Liens Act, 46 U.S.C. § 31325(a) (2018).
8. *Id.* at § 31321.
9. See The Maritime Act 1990 of the Republic of the Marshall Islands, MI-107 § 113 (2023); The Liberian Maritime Law, 21 RLM-107 § 30 (2022).
10. See U.S. Department of Transportation, Maritime Administration Report, *Comparison of U.S. and Foreign Flag Operating Costs*, September 2011, which notes in its introduction that, as of the end of 2010: "The Marshall Islands, Singapore, and Liberia represent the top three registries, which accounted for 31, 11, and 10 percent, respectively, of U.S.-owned vessels in 2011. These registries are examples of 'open' registries. A registry is considered 'open' when more than 90 percent of its vessels are foreign-owned. Today, roughly 80 percent of the world fleet is operating under a flag of convenience from an open registry."
11. UNCTAD, *Review of Maritime Transport 2015* ch. 2 (2015).
12. Clarkson Research Services Limited (January 2023), *World Fleet Register*, <https://www.clarksons.net/wfr>.
13. 46 U.S.C. § 31325(a) (2018).
14. See, e.g., The Maritime Act 1990 of the Republic of the Marshall Islands, MI-107, § 302(3) (2016).
15. See, e.g., The Liberian Maritime Law, RLM-107, § 105(1) (2018).
16. The Liberian Maritime Law, RLM-107, § 105 (1) (2022) ("A mortgage or financing charter which recites the particulars required to be stated... secures modifications, if any, that may be made from time to time to the direct and/or contingent obligations secured thereby in respect of (i) interest rate and payment terms, (ii) a decrease in the total amount of the direct and/or contingent obligations secured by such mortgage or financing charter, (iii) any maturity date (other than an extension of a maturity date stated in the mortgage or financing charter), and (iv) any covenants (except as otherwise provided in the foregoing items (i) and (iii))").
17. The Maritime Act 1990 of the Republic of the Marshall Islands, MI-107 § 309(2) (2023).

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Global Transportation Finance

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