

# Green Finance in Shipping

## The IMO 2020 Tsunami



**Michael A. Antapasis**  
Legal Counsel  
TMS OFFSHORE SERVICES LTD.



**WORLD  
SHIPPING**  
Law Forum

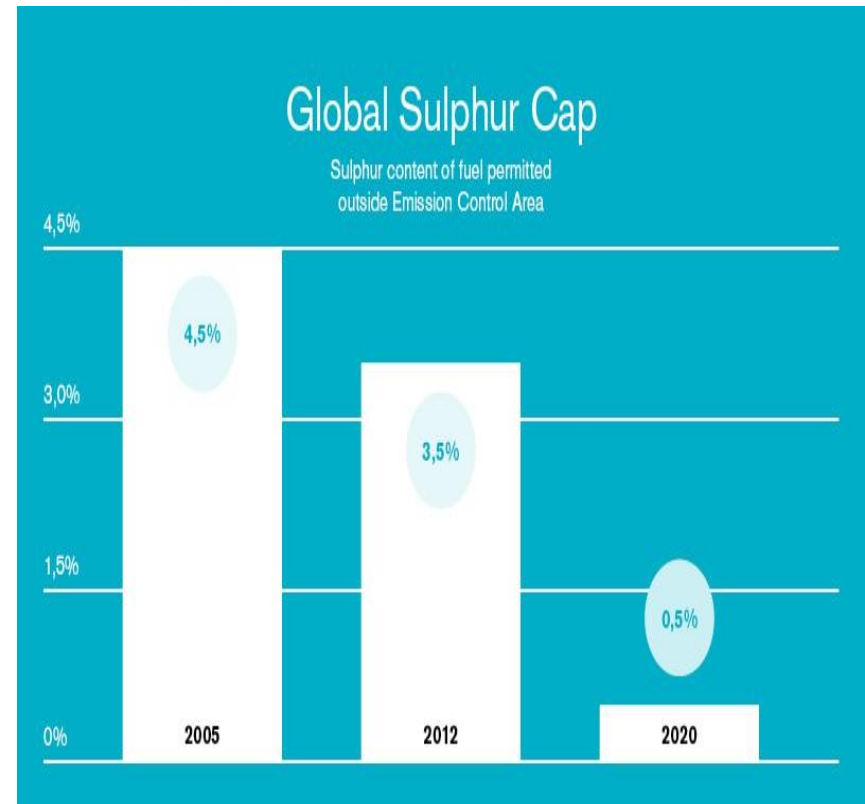
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# Environmental impact in shipping

- Emission control regulation is not new.
- State Emission Control Areas (ECA)
- Devolvement and compliance is slow due to the nature of the business
- It's the first time the industry needs to rapidly adapt and take action
- IMO 2020: ships operating outside ECA will use fuel with 0.5% sulphur or use scrubbers
- Effective date 1/1/2020
- This action will be expensive and need to find alternatives to avoid high cost



## Shipowners' Options

- Bunkers using 0,5% low sulphur fuel oil (LSFO)
- Retrofit the ships with exhaust gas cleaning systems (scrubbers) and continue to use 3.5% high sulfur fuel oil (HSFO);
- Retrofit the ships with power units which will use LNG or LPG as fuel.



# LSFO usage

- Worldwide availability question - Refineries and Fuel Providers are making investments – will they be ready on time?
- If instantly applicable, 50% of production in refineries should be thrown away in 2020!
- What happens with low trading areas or 2<sup>nd</sup> tier ports?
- HSFO/LSFO Price difference - Today estimated around 150\$ - In 1/1/2020 HSFO will be cheaper. What about 2023?
- LSFO is expected to become significantly cheaper than diesel. When though?
- So Owners can play the price market and lock today's prices with providers
- Concerns around stability and compatibility are also expected to diminish over time as refiners are increasingly developing fuels.





# LNG / LPG as fuel



- Eco-friendly solution
- Cheap and viable compliant fuel option
- Its contribution in the global bunker fuel mix is expected to be only 5% by 2030
- Extremely expensive project, especially to retrofit.
- So far great lack in infrastructure
- Considered to be an experiment project for the future (Sovcomflot 6 vessels by Q2 2019) – Still, 6 out of 144 vessels of the fleet

# Scrubber Units

- Hot Topic – General idea: it takes the sulphur from the air and injects it into the ocean
- Open Loop / Close Loop / Hybrids
- Open Scrubbers are preferred due to:
  - lower cost (\$2 – 3m)
  - technical stability
  - Uncertainty should they be banned in the future – Should be hybrid ready
- Will make the vessel more attractive to major charterers/give higher rate
- Cheaper fuel
- Lot of technical / operational experience with HSFO
- Relatively short pay-back period
- As a commercial option, should be installed and ready early 2020 – not so viable after 2023 – 2024
- Owners should have a long term supply contract for HSFO



# Scrubbers Financing Options

- Owner with good credits/financial sheets are able to raise financing – what about the others? Alternative solutions but more expensive
- Easiest way → expand existing facility
- Use company's funds and suspend any loan instalments for the pay-back period
- Sale a number of assets (vessels) and finance instalment
- Issue more complicated if a 3<sup>rd</sup> party is financing the project → need for extra securities and get existing mortgagee's consent
- Even if the 3<sup>rd</sup> party is unsecured, you will need to make sure you are in alliance with existing loans' covenants
- Manufacturer's financing → leasing



# Scrubbers Financing Options Unencumbered Ship

- Easier to finance – no restrictions to covenants or necessity to obtain consent
- Able to provide 1<sup>st</sup> priority mortgage
- In shipbuilding contracts, financing bank will increase the facility amount with an addendum to the loan agreement





# Scrubbers Financing Options

## Encumbered Ship

- Increase existing facility amount / possibility of 3<sup>rd</sup> party to provide capital and sub-participate to existing loan → 1<sup>st</sup> priority mortgage on a *pari passu* basis and contractual subordination of the 3<sup>rd</sup> party
- But, any equipment installed on the ship becomes part of the ship and the 1<sup>st</sup> mortgagee's mortgage; so if 3<sup>rd</sup> party financier, will lose any proprietary claim and will rank behind the 1<sup>st</sup> mortgagee unless there is a subordination
- Depending on the jurisdiction, the scrubber financier may or may not have a maritime lien
- Solution: Scrubber financier to retain title and lease the equipment → in arrest it will be able to take injunctive action to postpone a sale of the ship and either arrange for the scrubber to be returned, or come to some arrangement to cover its loss (may not work in US Chapter 11 proceedings)



# Charterer's financing

Directly

- Big hire down-payment
- Increase charter rate
- Additional set-off right

Indirectly

- Discount to the charter rate

Depending on the time charterparty:

- Owner can demand charterer to use and pay LSFO
- Charterers can demand to retrofit with scrubbers, pay for the cost and set off with agreed reduction of hire
- For new time charterparties drafting should be very clear when allocating the cost of compliance



# Conclusion



- Market has been very adaptable and open minded in financing scrubbers
- Variety of options, but the market will show the way as to which decision is best
- In terms of timing, this adds more pressure on the owners which have been facing difficult times for the last several years
- How to comply with IMO 2020 is still an ambiguous issue
- Nevertheless, IMO 2020 is just the pioneer of many environmental regulations to follow in the future
- Green approach in shipping will be unavoidable in the future and both Charterers and Lenders will examine it as a *sine qua non* to proceed.
- Market will have to adjust one way or the other and new financial instruments need to emerge



Questions



**THANK YOU**

**Michael A. Antapasis**

Attorney at Law, LLM

Legal Counsel

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