

The Evolution, Revolution and Preservation of Legal Infrastructures in the World of Shipping

Francis X. Nolan, III

April 4, 2019

I. Flag and Nationality

- Genuine Link
- Double Breasted Registries
- Open Registries
- Bareboat Charter Registries
- Vessels under Construction

II. Impact of Open Registries on Vessel Finance

- Financial products
- Security
- Creation
- Enforcement

III. Applicable Laws and Dispute Resolution

- Law and applicable standards
 - Contract
 - Flag
 - Port State
 - International Conventions
 - Classification Societies
- Forum
- Enforceability
 - Reliability

IV. Insolvency

- Availability of regimes to address
- Bankruptcy tourism

I. FLAG AND NATIONALITY

The Rise of Open Registries

Life in 1966

Who built, who sailed, who financed, and how.

“Predict U.K. to Lose Maritime Supremacy”

Chicago Tribune

(Chicago Tribune Press Service)

LONDON, July 2-The British trading fleet, long the largest in the world, seems destined to lose its supremacy this year. Threatening Britannia’s rule of the seas is the surging growth of shipping registered in Liberia.

Growth projections of the small African nation’s fleet – from virtually no ships after World War II to more than 10 million gross tons in 1958 and 19,332,000 tons in 1965 – point to first place for Liberia by the end of the year among the world’s merchant fleets of ships 599 gross tons and more.

The United States, not including its reserve fleet of 10,100,000 tons in “mothballs,” ranks fifth with 9,931,000 tons. Norway is third with 15,589,000 tons, and Japan next with 11,250,000. The Soviet Union trails America with 7,455,000 tons.

While Liberia will almost surely overtake Britain this year as the world maritime leader by this yardstick, it’s ascendancy will be largely statistical. Ship companies use Liberian registry as a “flag of convenience” – a guise to evade higher taxes and crew costs than if the vessels were registered in the shipowner’s own country.

United States companies use Liberian registry extensively – 40 per cent of the Liberian fleet is estimated to be owned by Americans. (Among savings are the much lower crew costs. American seamen receive wages that are at least twice the scale in all other countries.)

Greek shipowners are thought to have a slightly higher percentage of Liberian registered vessels than United States companies, and the remaining 15 per cent is spread fairly well among the other leading maritime nations.

Then, too, there is the fact that the Liberian fleet has a high percentage of oil tankers – less prestigious than the sleek passenger-cargo and cargo liners that characterize the British fleet.

But even in the category, Liberia is creeping up in Britain’s wake.

In passenger service British lines continue to lead the world in the most heavily traveled routes, particularly the North Atlantic run. There, Cunard’s proud [but aged] Queens Elizabeth and Mary carry more passengers than the ships of any other nation.

Chicago Tribune, Sunday July 3, 1966, Section 4, page 4, columns 1-2

Flag and Nationality

- What are “Flags of Convenience” and “Open Registries”
- The concept of “genuine link” and what duties does it create?

Flag and Nationality

- Convention on the High Seas of 29 April 1958, Article 5:

“1. Each State shall fix the conditions for the grant of its nationality to ships, for the registration of ships in its territory, and for the right to fly its flag. Ships have the nationality of the State whose flag they are entitled to fly. There must exist a genuine link between the State and the ship; in particular, the State must effectively exercise its jurisdiction and control in administrative, technical and social matters over ships flying its flag.”

“2. Each state shall issue to ships to which it has granted the right to fly its flag documents to that effect.”

Flag and Nationality

- United Nations Convention on the Law of the Sea (1982), ART 91.1

Nationality of ships

“Every State shall fix the conditions for the grant of its nationality to ships, for the registration of ships in its territory, and for the right to fly its flag. Ships have the nationality of the State whose flag they are entitled to fly. There must exist a genuine link between the State and the ship. (Emphasis supplied)”

- M/V SAIGA (NO. 2) (1999), International Tribunal for the Law of the Sea
 - Registered and flagged in St. Vincent and the Grenadines
 - Seized by Guinea for violation of Guinean law
 - Was it “stateless” for want of “genuine link?”



Panama	1920
Liberia	1948
Singapore	1969
Marshall Islands	1990

Extracted From:

U.S. Department of Transportation

Maritime Administration

MERCHANT FLEETS OF THE WORLD

PRIVATELY-OWNED, OCEANGOING MERCHANT VESSELS OF 1,000 GROSS TONS AND
OVER AS OF JANUARY 1, 2016

Includes Government-owned ships (U.S. and Foreign-Flag)

Source: IHS Markit Lloyds Maritime Database Files

Registry	Number of Ships	GT	DWT
United States of America	337	9,400,648	10,616,525
Privately-Owned Merchant Fleet	167	6,648,597	7,782,930
Jones Act Eligible	90	3,250,891	4,562,872
Non Jones Act Eligible	77	3,397,706	3,220,058
Great Lakes Trading	41	815,184	1,633,349
Passenger/Ferry	83	436,546	94,661
Ready Reserve Fleet	46	1,500,321	1,105,585

FOREIGN REGISTRIES (Open Registries)			
	Number of Ships	GT	DWT
Antigua & Barbuda	992	8,628,343	11,121,727
Bahamas	1,141	52,483,094	67,553,798
Belize	250	1,575,549	2,371,258
Cayman Islands (British)	118	3,330,592	4,391,122
Cyprus	799	20,504,818	32,520,442
Denmark (DIS)	348	14,825,776	16,905,673
Gibraltar (British)	249	2,779,558	3,259,011
Hong Kong	2,238	101,389,102	165,588,980
Isle of Man (British)	311	13,578,155	21,948,545
Liberia	2,969	126,690,266	198,749,031
Malta	1,927	63,074,278	95,638,923
Marshall Islands	2,661	116,714,309	189,448,831
Norway (NIS)	362	13,037,031	17,206,155
Panama	6,156	212,367,784	324,589,815
Singapore	2,133	79,014,559	119,961,433
St Kitts & Nevis	121	800,410	1,070,825
St Vincent & The Grenadines	207	1,728,069	2,416,841
Vanuatu	74	978,872	1,536,063
Total – All Listed Foreign Open Registries	23,056	833,500,565	1,276,278,473
World Fleet Totals – ALL FLAGS	41,674	1,139,012,950	1,704,512,742
Open Registry – % of Total	55.3%	73.5%	74.9%

	Container		
Registry	Number of Ships	GT	DWT
United States of America	69	2,848,323	3,101,484
Total – All Listed Foreign Open Registries	3754	169,120,727	192,167,559
World Fleet Totals – ALL FLAGS	5,119	215,329,001	244,551,002
Open Registry % of Total:	73.3%	78.5%	78.6%

	Dry Bulk		
Registry	Number of Ships	GT	DWT
United States of America	47	974,120	1,893,394
Total – All Listed Foreign Open Registries	7,839	333,096,911	597,470,449
World Fleet Totals – ALL FLAGS	10,682	416,747,753	756,771,074
Open Registry % of Total:	73.4%	79.9%	80.3%

	General Cargo		
Registry	Number of Ships	GT	DWT
United States of America	21	294,276	288,986
Total – All Listed Foreign Open Registries	3,805	32,806,905	44,739,297
World Fleet Totals – ALL FLAGS	10,635	59,998,943	81,456,136
Open Registry % of Total:	35.8%	54.7%	54.9%

	LNG/LPG		
Registry	Number of Ships	GT	DWT
United States of America	0	0	0
Total – All Listed Foreign Open Registries	973	41,376,459	37,082,417
World Fleet Totals – ALL FLAGS	1,528	59,713,578	53,224,662
Open Registry % of Total:	63.7%	69.3%	69.7%

	Passenger		
Registry	Number of Ships	GT	DWT
United States of America	83	436,546	94,661
Total-All Listed Foreign Open Registries	362	14,706,013	1,757,935
World Fleet Totals – ALL FLAGS	2,141	35,678,417	5,898,071
Open Registry % of Total:	16.9%	41.2%	29.8%

	Ro-Ro		
Registry	Number of Ships	GT	DWT
United States of America	63	2,567,241	1,419,010
Total-All Listed Foreign Open Registries	745	32,628,380	11,456,095
World Fleet Totals – ALL FLAGS	1,467	49,193,256	19,341,316
Open Registry % of Total:	50.8%	66.3%	59.2%

	Tanker		
Registry	Number of Ships	GT	DWT
United States of America	54	2,280,142	3,818,990
Total-All Listed Foreign Open Registries	5,598	210,704,057	380,069,905
World Fleet Totals – ALL FLAGS	10,102	302,352,002	543,270,481
Open Registry % of Total:	55.4%	69.7%	70.0%

The Impact of Open Registries on Vessel Finance

- Safety, labor laws, quality and security. Review of Maritime Transport, Part 2 (UNCTAD 2015)

“Historically, when the first shipowners started to “flag out” by registering their ships in a foreign open registry in the 1970’s or even earlier, one of the motivations may have been less stringent safety and environmental regulations. Today, there is no generalized difference between open and national registries as far as the ratification and implementation of relevant international conventions is concerned. A comparative table provided by the International Chamber of Shipping shows that both national and open registries can be found among the best and among the worst service providers (International Chamber of Shipping, 2014). The registries with youngest fleets among the top 35 flags were Hong Kong (China), the Marshall Islands and Singapore.”*

* Review of Maritime Transport, Part 2, at 41-43 (UNCTAD 2015).

The Impact of Open Registries on Vessel Finance

- The perspectives of Lenders, Investors, Owners and Operators
 - Benefits
 - Drawbacks

The Impact of Open Registries on Vessel Finance

- Impact on marine finance
 - Safety of capital
 - Rule of law
 - Martin Stopford, *Maritime Economics* (3rd Ed. 2009)

“To be successful an open register’s ships must be acceptable in the ports of the world and to bankers lending against a mortgage on the ship. As the scrutiny of ships by shippers and port authorities has increased it has become more important for open register flags to comply with international conventions, and most open registries, whilst offering shipowners freedom in the areas of taxation and company law, enforce legislation regarding the operational and environmental safety of ships registered under their flag.”*

* Martin Stopford, *Maritime Economics* (3rd Ed. 2009), page 671.

The Impact of Open Registries on Vessel Finance

- Flexibility of Open Registries to adapt to opportunities and developments
 - Bareboat Registry provisions
 - Marshall Islands Maritime Act, Sections 260-264 (inbound); Sections 270-274 (outbound); Liberian Maritime Law, Sections 85-89 (inbound); Sections 90-94 (outbound)
 - Financing Charters as preferred mortgages
 - Marshall Islands Maritime Act, Section 302A, as amended by Maritime (Amendment) Act 2016
 - Liberian Maritime Law, as amended, Section 100A
 - registration and mortgaging of “vessels under construction”
 - Marshall Islands Maritime Act, Section 303(1)
 - domestication of pre-existing foreign preferred mortgages in new registry
 - Marshall Islands Maritime Act of 1990, Section 303, as amended; Liberian Maritime Law, as amended, Sections 101(3), (4)

Changing Sources of Shipping Capital

- US and U.K. Banks
 - Declined
- German and Scandinavian Banks
 - Large scale sales of German Bank shipping portfolios
- Export Credit Agencies
 - Motivations and effects
 - Title XI, shipyards, labor operations and defense
 - Asian ECA's - support shipyards
 - Will Chinese banks finance other flags over significant periods?

Changing Sources of Shipping Capital

- Public Markets
 - Disclosure requirements
- Private Equity
 - U.S. markets yield expectations
- Leasing
 - Chinese lessors
 - Recharacterization risks
 - Greater threat of pricing liens drowning equity
- Other Alternative Sources
 - Crowd sourcing

III. Applicable Laws and Dispute Resolution

- Laws of the Flag
- Classification Societies – ABS, DNV GL, BV, Lloyds, China
- Port State laws
- Extra-territorial laws of affected jurisdiction
- International conventions
- Bilateral treaties
- Contract forms (limitations: *see Icon Amazing* case (2013))
- Contractual agreement on applicable laws

The Burden of New Laws – the Expansion of Covenants – Flag Neutral

■ Anti-Terror Burdens

- Fighting crime and terror through bankers
 - security covenants
 - “Know-Your-Customer”, Patriot Act of 2001, Public Law No. 107-56, 115 STAT. 272
 - control of chartering rights and vessel employment
 - Foreign Corrupt Practices Act of 1977, as amended, 15 U.S.C. Section 78dd 1, et seq.
 - impact of Trading With the Enemy Act, U.S.C. Section 95a 95b, 50 U.S.C. App. Section 1 144 and Office of Foreign Assets Control, U.S. Treasury Dept.

Choosing a Forum

- Integrity
- Expertise
- Cost
- Reliability

Arbitration or Courts?

- Enforceability

IV. Insolvency

- What are the options? (World Bank Study)
- Expanding reach and utility of U.S. Bankruptcy law
 - The rise of the foreign shipping “bankruptcy tourist” in U.S. Bankruptcy Courts
 - U.S. proceedings in aid of foreign bankruptcies, Chapter 15 of the Bankruptcy Code

Conclusions



VedderPriceSM

Francis X. Nolan, III

Shareholder

Vedder Price P.C.

1633 Broadway

New York, NY 10019

212-407-6950

fnolan@vedderprice.com