GETTING THE DEAL THROUGH

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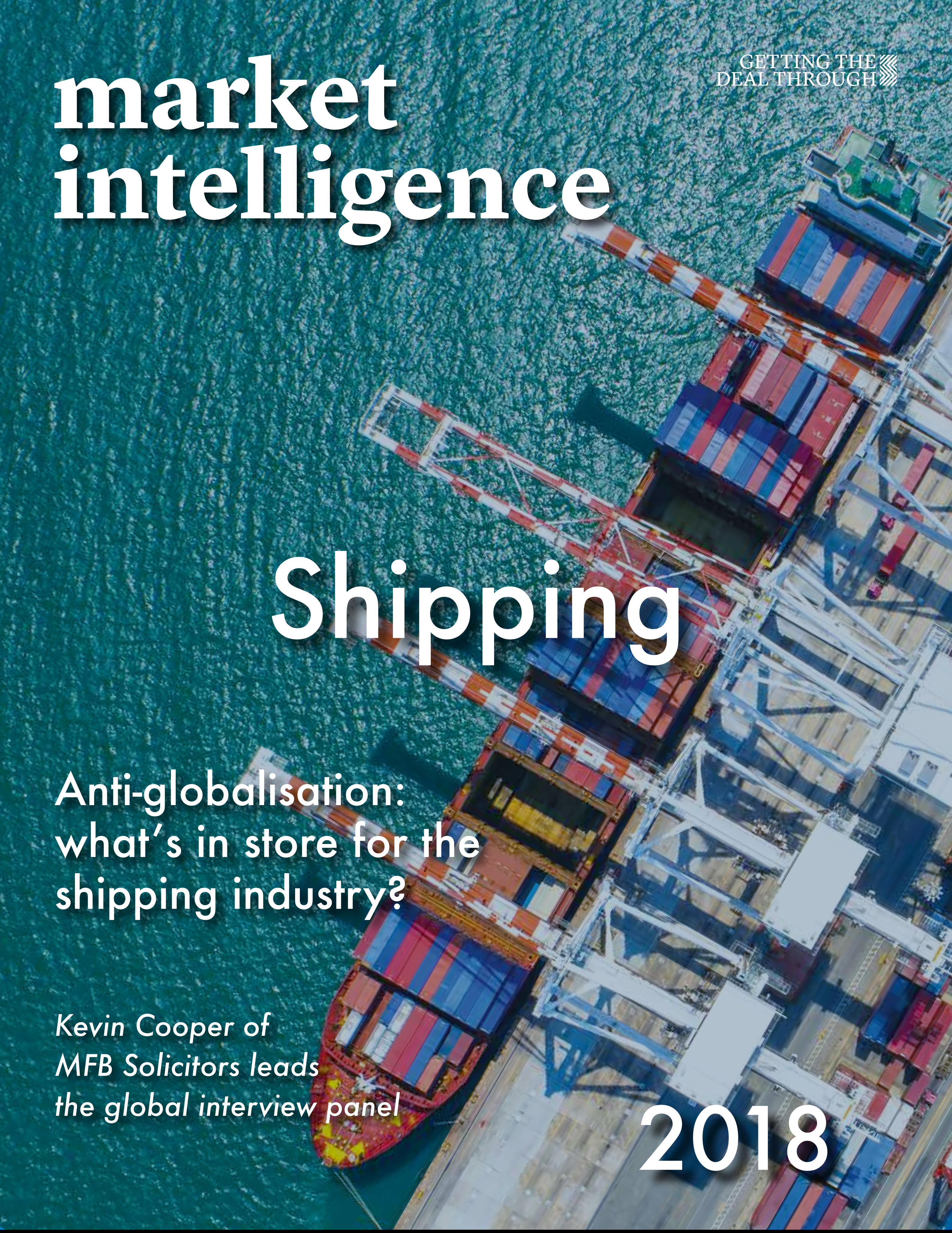

Shipping

Anti-globalisation: what's in store for the shipping industry?

Kevin Cooper of MFB Solicitors leads the global interview panel

2018

The Americas • Asia-Pacific • Europe • Middle East
Industry snapshot • Compliance • Finance • 2018/19 outlook

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market intelligence

Welcome to GTDT: *Market Intelligence*.

This is the 2018 edition of Shipping.

Getting the Deal Through invites leading practitioners to reflect on evolving legal and regulatory landscapes. Through engaging and analytical interviews, featuring a uniform set of questions to aid in jurisdictional comparison, *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 interesting cases and deals.

Market Intelligence is available in print and online at www.gettingthedealthrough.com/intelligence.

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SHIPPING IN INDIA

Mr Shardul Thacker heads the shipping, oil and gas and banking practice group at Mulla & Mulla & Craigie Blunt & Caroe.

Lloyd's List ranked him third in their top 10 lawyers stating: "Highly regarded for his work in the liquefied natural gas sector, particularly for interesting and highly geared finance deals in relation to infrastructure projects, energy, ports and ships."

Thacker handles all types of structured ship and asset finance. He acts for overseas lenders in most India-related ship financings including liquefied natural gas vessels flying foreign flags and chartered by Indian companies. Thacker advises on regulatory issues including Indian flagging, cabotage, tonnage tax, applicable taxes, licensing, assessment of legal risk, including pollution liability.

He advises on ship-building contracts, charter parties, long-term cargo handling agreements, offshore construction contracts.

Thacker is ranked in Band 1 by *Chambers and Partners* for Shipping and Maritime and for Banking and Insurance for several years.

His publications include the India sections in *Maritime Law Handbook, Kluwer* and *The Transport Finance Law Review*.

Who's Who Legal says Shardul Thacker is an "excellent shipping lawyer" with a particularly strong reputation for international ship finance transactions.

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GTDT: What is the current state of the shipping industry in your country?

Shardul Thacker: The shipping industry is one of the most globalised industries and operates in a highly competitive business environment. This industry is far more liberalised than most other industries and is, thus, intricately linked to the world economy and trade. As on 31 December 2017, India had a fleet strength of 1,374 ships with dead weight tonnage (DWT) of 18.80 million (12.36 million gross tonnage (GT)) including Indian-controlled tonnage, with the Shipping Corporation of India having the largest share of around 34 per cent. Of this, around 443 ships of 17.19 million DWT (10.88 million GT) cater to India's overseas trade and the rest to coastal trade. To encourage the growth of Indian tonnage and the higher participation of Indian ships in Indian trade, the government has implemented several measures that, inter alia, include the following.

- Permitted Indian shipping companies to own foreign-flagged ships registered overseas, on condition that the tonnage flagged outside India does not exceed the owned tonnage in India and that 50 per cent of the crew of such foreign-flagged ships is Indian. This Indian-controlled tonnage will be eligible to operate in cabotage regulated Indian waters (ie, cargo movement between two Indian domestic ports).Therefore, with the relaxation on foreign-flagged vessels, Indian shipping companies can own 50 per cent of the new tonnage under a foreign flag as foreign-controlled tonnage.

  In May 2018, the Union Shipping Ministry issued orders that permitted foreign-flagged container ships to carry export-import laden containers for transhipment and empty containers for repositioning on local routes, ie, from one Indian port to another Indian port without obtaining a licence from the Directorate General of Shipping (DGS). This was essential for India's efforts to set up transhipment hubs and reduce dependence on neighbouring foreign hubs to send and receive containers. Global container lines such as Maersk Line, MSC and CMA-CGM will benefit from the decision. The container transhipment terminals run by DP World at Cochin Port Trust; Mundra Port run by Adani Ports and Special Economic Zone Ltd (APSEZ); Krishnapatnam Port run by the CVR Group; and the container transhipment facility being built by APSEZ at Vizhinjam in Kerala, among others, will gain from the new policy. It will help reduce the cost of repositioning of empty containers within India. It will bring competition within the EXIM feedering trade around the Indian coast and encourage use of Indian ports and terminals for aggregation and transhipment as well.
- A foreign-flagged ship is not required to obtain a licence from the DGS for engaging in coasting trade of India, for carriage by sea of agricultural, fisheries, animal husbandry and horticultural commodities as prescribed by the DGS, as adopted by the Director General of Foreign Trade.
- The Goods and Service Tax on bunker fuels used in Indian flagged vessels has been reduced from 18 per cent to 5 per cent.
- Parity has been brought in the tax regime of Indian seafarers employed on Indian-flagged ships vis-à-vis those on foreign-flagged ships.
- In public private partnership projects in the port sector, 100 per cent foreign direct investment is being allowed.
- To develop cruise shipping and tourism in the country, the government has constructed new cruise terminals at Mormugao port and Chennai Port. Also, the capability for foreign-flagged passenger vessels to call at Indian ports without obtaining licence from DGS has been extended from February 2019 to February 2024.
- There are ongoing discussions in relation to scrapping of the right of first refusal that is given to domestic fleet-owners that ensures a supply of local export-import oil and bulk cargo to them at the lowest bid price. This move is sure to benefit foreign shipping lines and foreign-flagged vessels. The intention of the government is to build volumes and see a large-scale shift of cargo movement to waterways from railways and roadways that foreign lines can provide, and eventually reduce the logistics cost.
- India was re-elected as a member of the International Maritime Organization (IMO) Council under Category B, by getting the second highest number of votes during the IMO Council election held at IMO on 1 December 2017.

GTDT: What are the prevailing shipping market trends affecting your country?

ST: India's coastal shipping sector is set to improve in 2018 owing to features such as being environmentally friendly, cabotage relaxation, fuel efficient, and for being a cheap mode of transport for moving cargo from road-and-rail routes along India's 7,500-kilometre coastline.

The Sagarmala Programme is the flagship programme of the Ministry of Shipping to promote port-led development in the country through harnessing India's long coastline, 14,500 kilometres of potentially navigable waterways and strategic location on key international maritime trade routes. It envisages over 508 projects at an estimated investment of more than 8 trillion rupees for implementation over the next 20 years. The Ministry of Shipping, released 2.5 million rupees as grants-in-aid to Jawaharlal Nehru Port


Shardul Thacker

Trust and 500 million rupees to the government of Karnataka for Karwar port, for infrastructure development under the Coastal Berth Scheme of the Sagarmala Programme. These resulting projects would see the development of manufacturing hubs, supported by port modernisation projects.

Recently Indian and global players are joining hands in establishing joint venture companies undertaking floating storage and regasification unit (FSRU) and liquefied natural gas (LNG) projects supported by GAIL, Reliance and others who have constructed gas pipelines across India. This activity has largely supported the offshore industry, increasing the activity for tug owners and anchor handling companies.

Project UNNATI has been started by the government of India to identify the opportunity areas for improvement in the operations of major ports. The aims and objectives of Project UNNATI are as follows:

- benchmark operational and financial performance of the 12 major ports with selected Indian private ports and best-in-class international ports for identifying improvement areas;
- undertake a capability maturity assessment for key processes and functional capabilities (eg, IT, HR, environment, health) and identify gaps and areas for further strengthening;
- detailed deep-dive diagnosis and root cause analysis for the identified opportunity areas in each of the 12 major ports to understand underlying reasons for performance bottlenecks; and
- develop practical and actionable solutions on the basis of root cause findings, and develop a comprehensive improvement roadmap for each of the 12 major ports.

Under Project UNNATI, the global benchmarks were adopted to improve the efficiency and productivity key performance indicators for 12 major ports. A clear roadmap for improvement for each port has been laid out covering changes in the areas of core business processes, equipment, organisation structure, people skills, information technology and infrastructure. Around 116 initiatives were identified across 12 major ports to unlock more than 100 metric tonnes per annum (MTPA) capacity just through efficiency improvement. Out of this, 86 initiatives have been implemented to unlock around 80 MTPA capacity.

The Jal Marg Vikas Project on National Waterways-I in the River Ganga, a large integrated inland water transport project, has been launched between Varanasi and Haldia, covering a distance of 1,380 kilometres at an estimated cost of 53 billion rupees. On completion, the project would enable commercial navigation of 1,500–2,000

> *"There are a number of regulatory and compliance requirements in the Indian shipping market."*

tonne vessels. The major activities under the project are construction of multi-modal terminals, jetties, river information system, channel marking, navigational lock, river training and conservancy works.

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

ST: The Admiralty (Jurisdiction and Settlement of Maritime Claims) Act 2017 (the Admiralty Act) came into force on 1 April 2018. It consolidates the existing laws relating to admiralty jurisdiction of courts, admiralty proceedings on maritime claims, arrest of vessels, stipulates the order of priorities for maritime claims and liens inter se, as well as against other claims and related issues. It also repeals five obsolete British statutes on admiralty jurisdiction in civil matters, namely:
- the Admiralty Court Act 1840;
- the Admiralty Court Act 1861;
- the Colonial Courts of Admiralty Act 1890;
- the Colonial Courts of Admiralty (India) Act 1891; and
- the provisions of the Letters Patent 1865 applicable to the admiralty jurisdiction of the Bombay, Calcutta and Madras High Courts.

The Admiralty Act makes the statute retrospective in application and therefore all admiralty proceedings in the concerned High Courts pending before commencement of the statute, as well as all actions initiated, by laws, rules framed and notices issued under the repealed enactments, will be now be adjudicated by the provisions of the Admiralty Act 2017, as long as they are not inconsistent with the provisions of the same.

The Admiralty Act confers admiralty jurisdiction on High Courts to order the arrest of any vessel that is within its jurisdiction for the purpose of providing security against a maritime claim.

The National Waterways Act 2016 also came into force on 12 April 2016. It designates 101 waterways as national for a fuel-efficient, cost effective and environment friendly mode of transport.

Additionally, the government has proposed the following bills.
- The Merchant Shipping Bill 2016, which enables Indian-controlled tonnage to be registered on foreign registers. Registration of rigs and other coastal vessels, substantially owned vessels (more than 50 per cent) and vessels on bareboat-cum-demise charters by Indians, are to be registered under the new Merchant Shipping Act, which enables mortgagees on rigs to be registered with the Mercantile Marine Department. This act would issue licences to Indian-flagged vessels for coastal operations and for clearance by the Custom Authority.
- Major Port Authorities Bill 2016, which allows for autonomy and flexibility in all major ports. The board of trustees will be replaced by board members representing various stakeholders to ensure a transparent and decentralised decision-making process, to aid expansion of port infrastructure. The emphasis on the professional approach is governance. The Tariff Authority for Major Ports would be dissolved and tariff fixation would be carried out by the board in compliance with the Competition Act 2002. There is a provision for public private partnership enabling the concessionaires to fix tariffs based on market conditions.

GTDT: What are the key regulatory and compliance issues for your country's shipping market?

ST: There are a number of regulatory and compliance requirements in the Indian shipping market, such as corporate and tax compliances by the shipping company, in addition to the registration of the vessels with the registry maintaining several class and security registrations and licences, intimations, approvals as well as reporting required to be undertaken with the Reserve Bank of India and also the authorised dealer bank of the company for overseas finance borrowed for the vessels, etc. However, as part

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of promoting 'Ease of Doing Business in India', a number of proactive steps are being undertaken by the government that include elimination of the requirement to submit manual forms and documentation, direct port delivery, installation of container scanners at ports, and an automation system based on radio frequency identification systems (RFIDs). A RFID system has already been put in place at nine major ports.

Most of the compliances can now be undertaken on an online platform instead of physical submissions. The chartering licence from DGS can also be applied for and obtained online. Further, 100 per cent cashless transactions have been achieved at all major ports, land records have been digitised and all ports pensioners linked with Aadhaar Biometric system. Direct port delivery and direct port entry has been initiated at major ports for EXIM containers.

The Accredited Client Programme was introduced for mega importers that meet the criteria of a clean compliance record, a specified volume of annual imports and payment of duty. If their bills of entry are filed in advance, cargo can be cleared from their containers without assessment or inspection. Duty payment is charged on an annual basis for cargo imported in containers. All government cargo is mandated to have a 'FASTag' for automatic deduction of toll charges and smooth movement of cargo at toll plazas, thereby saving time and logistics costs.

The much needed regulatory change is to reduce the tax burden on Indian shipowners to make the Indian flag more competitive. While tonnage tax is 1–2 per cent of Indian shipping companies' incomes, taxes on the sale of vessels, corporate tax on interest earned on tonnage tax reserve funds and dividend distribution tax, etc, need to be abolished for Indian tonnage to increase in proportion to India's EXIM trade. Also, there is a need for simplification of the customs procedure relating to the shipping industry.

GTDT: 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?

ST: Shipping is a global industry, which has cyclical ups and downs. Indian entrepreneurs, in the context of other industries, have not considered it a 'safe haven' for their investments. It is also dollar-based, and global banks tend to focus on large fleet-owners, which is rare in India. Indian banks are unable to commit to long-term foreign currency financing for a cyclical industry, even if there is a natural hedge by earnings from freight. In addition to this, the financing costs of the Indian banks are not competitive in terms of global financing, as interest rates are high. In view of the stress on banks due to the risk involved in

THE INSIDE TRACK

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

Particular skills that clients look for in an effective shipping lawyer are accessibility, quality of work with clear responses on the issues for which the maritime lawyer is engaged and, most importantly, a quick turnaround of what is required. Since this industry has sensitive moving targets, proactive action is a must.

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

Having predominantly worked for lenders, the key consideration, when arranging for finance for a shipping transaction, is the risk attached to the borrower shipping company effectively servicing the loan facility. Gainful employment of the vessel at rates that sufficiently cover operating expenses as also servicing the loan would be a key consideration. To safeguard the lender's interest, the facility must be adequately secured by assignment of insurance and earnings. In case of multiple ship finances, 'cross-collateralisation' of security and acceleration in the event of default are crucial for the lender. Finance documentation must contain provisions obligating the owner or borrower to furnish additional security, in the event the value of the security falls below the margin.

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

I was involved in a litigation for one of our Singaporean clients, a wholly owned subsidiary of an Indian conglomerate in their claims against a Zurich-based bank, Credit Suisse AG, for arresting the vessel *MV Maverick Gunner* in Singapore for enforcement of their mortgage, when the said vessel was carrying cargo belonging to the subsidiary. I advised clients in their pursuit against the bank for a tort committed by them on the basis of the decision of *The Myrto* [1977 2 Lloyds Rep 243]. There were interesting aspects in the matter as the bank's right to arrest the vessel as mortgagee only arose under the two exceptions listed out in *The Myrto,* namely, when the security of the bank is impaired or when the owner is unwilling or unable to perform, the contract is clearly not for the bank to rely on. It also involved multi-jurisdictional aspects as the mortgagee was a Greek and an expert opinion was sought on the same.

I also acted for Mitsui & Co's Indian subsidiary, which is, inter alia, engaged in the business of setting up India's FSRU on the west coast of India for import of LNG. We reviewed, negotiated and finalised various documentation in relation to Mitsui's role as an operations and maintenance contractor for the FSRU project.

Shardul J Thacker
Mulla & Mulla & Craigie Blunt & Caroe
Mumbai

shipping, only shipping companies with a good credit rating are able to raise bank finance for the replacement of old tonnage and meeting the IMO requirements on emission of zero-sulphur fuels.

This had an impact on small- and mid-size players in the Indian market. Indian shipping companies such as Great Eastern Shipping Co Ltd and the Shipping Corporation of India have been able to withstand the changes. In view of this, shipping companies in India are looking for alternate sources of finance, namely, private equity funds, venture capital, etc.

Owing to the vast difference in the costs of domestic borrowing and external commercial borrowing, Indian companies have long obtained finance for the acquisition of ships from foreign banks. For most lenders, the Indian flag is not an 'approved' flag for financing because of a host of procedural issues. Also, registration of mortgage with the Mercantile Marine Department takes 15–20 days.

Indian shipping companies establish their subsidiaries overseas and take advantage of substantial fiscal incentives. Such subsidiaries seek support from their Indian parent for financing the Indian-controlled tonnage and also raise the revenue stream in the form of a charter or a drilling contract, thereby accessing India's booming cargo base but retaining its earnings overseas. The Indian flag, although considered expensive, is still bankable with several international lenders.

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

ST: On 3 January 2018, the Madras High Court, while hearing a batch of applications filed by various maritime claimants, passed a landmark judgment on a significant question of law. The query that arose for consideration was whether the leave of the Company Court under section 446(2) of the Company's Act 1956 was mandatory prior to hearing the various applications of the claimants while exercising its special admiralty jurisdiction. The court upheld the principle of *Generalia Specialibus Non Derogant* and held that, for deciding any maritime claim in India, it is imperative that the courts adopt the provisions of the Merchant Shipping Act 1958, and the Companies Act, being a general and prior legislation, will have to make way to the special enactment. This judgment, however, has been appealed before the division bench of the Madras High Court (*Shanmugam Rajasekar v Owners and Parties Interested in the vessel MT Pratibha Cauvery*).

Further, arrest of bunkers is not permissible in India. As per Indian law, bunkers are not considered to be maritime property. Therefore the courts exercising admiralty jurisdiction do not permit the arrest of bunkers (*Peninsula Petroleum Ltd v Bunkers on Board the Vessel, MV Geowave Commander* 2015(3) Bom CR 693). This decision was confirmed by the division bench of the Bombay High Court, and was recently reaffirmed in the case of *Mansel v MV Giovanna Iuliano* (5 May 2017).

Similarly, arrest of cargo is not permissible under Indian law by virtue of a recent order passed on 1 September 2017 by the Bombay High Court in the matter of *Pacific Gulf Shipping (Singapore) Pte Ltd v SRK Chemicals Ltd & Anr*.

GTDT: What is the outlook for your country's shipping market?

ST: There are clear signs that the Indian maritime sector is set for steady growth in view of burgeoning EXIM trade. The progress could be faster if the issue of unburdening taxes in the shipping sector is dealt with. Early completion of various projects in the logistics chain is crucial to meet the heavy traffic projections for the future. An efficient intermodal system is vital for the success of a port as it supports seamless movement of cargo across all modes (ship, rail and truck). The 'Make in India' initiative offers tremendous opportunities in the maritime sector, particularly in the shipbuilding and ship repair industry. The government's shipbuilding financial assistance policy provides a boost by encouraging Indian shipyards to bag foreign orders in a more aggressive manner and meet the requirements of Indian ship owners. The government has formulated a policy of financial assistance for shipbuilding for a period of 10 years for contracts signed between 1 April 2016 and 31 March 2026. The financial assistance, at the rate of 20 per cent of the contractual price of a vessel, fair price or actual payments received by the shipyard, is payable after delivery of the vessel and as per the guidelines issued by the Ministry of Shipping. The Indian maritime sector needs to look for new technologies and advancements to help save costs and deliver more for less.

Increasing investments and cargo traffic points towards a healthy outlook for the Indian ports sector. Providers of services such as operation and maintenance, pilotage and harbouring and marine assets, such as barges and dredgers, are benefiting from these investments. The capacity addition at ports is expected to grow at a compound annual growth rate of 5–6 per cent till 2022, thereby adding 275–325 metric tonnes of capacity.

Under the Sagarmala Programme, the government has envisioned a total of 189 projects for modernisation of ports involving an investment of 1.42 trillion rupees by 2035.

The Ministry of Shipping has set a target capacity of over 3,130 million metric tonnes by 2020, which would be driven by participation from the private sector. Non-major ports are expected to generate over 50 per cent of this capacity.

India's cargo traffic handled by ports is expected to reach 1,695 million metric tonnes by 2021–22, according to a report of the National Transport Development Policy Committee.

Within the ports sector, projects worth an investment of US$10 billion have been identified and will be awarded over the coming five years.

It is anticipated that in 2018, demand in the three main segments of the global shipping industry (dry bulk, tankers and containers) will outstrip supply for the first time in several years.

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