

SHIP FINANCE IN CYPRUS: OPPORTUNITIES AND CHALLENGES

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In today's ever-changing environment, the shipping industry is being called upon to face enormous challenges, deriving from the need to transform the industry into a "green area" and satisfy environmental requirements and evolving regulation. Most ship owners choose to either transform their current fleet or to build new vessels in order to meet the updated environmental regulations which include, amongst others, provisions for reducing greenhouse gas reductions, air pollution, bio-fouling, plastic pollution and underwater noise.

Inevitably, the transformation of the sector requires the relevant funding and ship financing has become crucial for the shipbuilding sector and shipping companies around the world. Ship financing involves both the corporate financial management of shipping companies for the refinancing of existing debts and newbuilding finance for the construction of new vessels.

Cyprus, as one of the leading maritime centres (the Cyprus Registry is classified as the 11th largest merchant fleet globally and the 3rd largest fleet in the European Union), is one of the focal points of ship financing, both through the maritime sector and by providing securitization solutions for financing.

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Pledging of shares of a Cyprus Company owning the ship

The pledging of shares of a Company is a widely used tool as it offers commercial security in Cyprus. It is also used as a security in the shipping finance area, in cases where the ship is owned by a legal entity which is incorporated in Cyprus. The pledging of shares is achieved through the execution of a share pledge agreement, which specifies the terms of the pledge and provides that, upon execution, specific documentation must be simultaneously provided to the pledgee i.e. the specific security mechanisms that

will facilitate the effective out-of-court enforcement of the pledge.

The documentation enables the pledgee to enforce the pledge in the event of default without the need for engaging in time-consuming court procedures. Therefore, the documentation provided to the pledgee by the pledgor allows the pledgee to transfer the shares to his name, if the obligations specified in the share pledge agreement fail to be discharged. Pledged shares should be fully paid up and no other charges should be registered against them. A pledge is a form of real security providing to the pledgee proprietary rights over the shares belonging to the pledgor. The possession of the pledged property may be actual or it may, more commonly, be constructive. Actual possession of the property brings concerns regarding risk and the duty of care. Therefore, constructive possession is a more commonly used practice.

Ship Mortgages

The most common forms of security in ship financing are ship mortgages. The relevant Cyprus legislative framework (the Merchant Shipping Law) allows a vessel or a share over a vessel to be registered as security for the creation and/or securitization of a loan. More explicitly,

a security over a ship, will be used by a ship owner as a tool for obtaining the relevant financing for the purchase and/or transformation and/or construction of a vessel while, at the same time, a lender will acquire an interest in the mortgaged vessel. The two parties in a ship mortgage agreement will be the mortgagor, who is the ship owner and the mortgagee, who is the lender.

A mortgage must always be accompanied by a collateral deed of covenants where the commercial/contractual terms of the agreement between the mortgagor and mortgagee are included, which, to a large extent, reflect the agreed provisions between the lender and the borrower, as they have been incorporated in the underlying document (the facility agreement). Although the relevant Law does not prescribe for a specified form for the deed of covenant, it is mandatory, pursuant to the Merchant Shipping law, for specific terms and matters to be reflected. These include, but are not limited to, the following:

- repayment of principal
- payment of interest
- insurances and renewals thereof
- application of insurance proceeds
- limitations on employment of the vessel
- events of default upon which statutory or other agreed powers of the mortgagee may be exercised and
- powers exercisable by the mortgagee

It is noted that, pursuant to the provisions of 4.3(e), First Schedule of the Stamp Duty Act of 1965, the mortgaged documents are exempted from any stamp duty obligation. This parameter is, of course, an additional incentive for the parties interested in acquiring and registering a vessel

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under the Cyprus flag.

The mortgage and the deed of covenants are registrable with the relevant registry of the Deputy Ministry of Shipping. The details of the mortgage, of the beneficiary, date-time of creation and the vessel or the number of shares which are mortgaged are registered with the said registry. The time and date of the mortgage are important and play an integral role, since the priority of the mortgages is regulated by the relevant time and date of their registration. It is further noted that it is a very common practice for the mortgage to be executed and filed with the Deputy Ministry of Shipping's registrar simultaneously with the execution of the main underlying document (facility agreement) in order to eliminate any security gap which may be created between the execution of the facility agreement and the registration of the mortgage in the relevant register. In addition to the aforementioned registration procedure and pursuant to the provisions of section 90 of the Companies Law, in the event

where the shipowner is a legal entity registered in Cyprus, the mortgage is also registrable with the Registrar of Companies in Cyprus within 21 days from the day of creation of the relevant charge. The mortgage can be discharged from the Registrar of Companies through the submission of the relevant application (accompanied by a release letter executed by the lender/mortgagee) and from the relevant register of the Shipping Deputy Ministry following the execution of a memorandum of discharge.

From the aforementioned brief description of the relevant procedures, it is evident that Cyprus has formulated a well-structured framework for ship financing in order to provide the necessary safety nets in this demanding and constantly transforming market of the shipping industry. Cyprus, as a leading maritime country, can and will play a decisive role in this transformation by offering attractive and convenient solutions to both financiers and shipowners looking to develop or update their fleet. **G**



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