

# Mainbrace Live: All Aboard! Webinar Series: [Part II]

Maritime Environmental Update and the Role of Insurance in Ship Finance





# Maritime Environmental Update and the Role of Insurance in Ship Finance

**Moderated By:**

Jeanne Grasso, Partner and Co-Chair,  
Maritime & International Trade Practice Group

**Presenters:**

Dana S. Merkel, Associate, Maritime Practice  
Stefanos Roulakis, Associate, Maritime Practice  
Natalie M. Radabaugh, Associate, Maritime Practice

# Today's Moderator



**Jeanne Grasso**

Partner & Co-Chair  
Washington, D.C.

Maritime & International Trade

- Jeanne Grasso focuses her practice on maritime, international, and environmental law for clients worldwide. Jeanne counsels owners and operators of vessels, charterers, cargo owners, and facilities, including manufacturing facilities.
- Her practice involves regulatory compliance counseling related to the U.S. Coast Guard; Environmental Protection Agency; U.S. Customs and Border Protection; and Maritime Administration, among other federal and state agencies, including providing advice regarding ballast water, air emissions, EPA's Vessel General Permit, and maritime security.
- Jeanne is highly ranked *by Chambers USA* and *Legal 500* for her work in shipping regulatory matters.

# Today's Speakers



**Dana S. Merkel**

Associate

Washington, D.C.

Maritime & International Trade

- Dana focuses her practice on domestic and international marine transportation and environmental issues for clients worldwide.
- Clients include ship owners, operators, and managers; offshore construction companies; shippers, charterers; and terminals.
- Practice includes compliance counseling under international conventions and U.S. and foreign regulations; coastwise trade; offshore construction; crew citizenship; administrative, civil, and criminal enforcement actions; internal investigations; pollution response; compliance and risk mitigation; solutions to maritime and environmental compliance challenges; vessel construction and flagging; international trade and sanctions issues.

# Today's Speakers



**Stefanos N. Roulakis**

Associate

Washington, D.C.

Maritime & International Trade

- Stefanos helps vessel owners and operators navigate U.S. law and regulations to ensure commercial success and operational efficiency.
- Counsels clients on international and domestic environmental standards; cabotage requirements; and international trade, including sanctions compliance.
- Develops proactive approaches to maritime compliance through audits and trainings
- Assists clients in internal investigations and investigations conducted by the U.S. Coast Guard and the U.S. Department of Justice.

# Today's Presenters



## **Natalie M. Radabaugh**

Associate

Washington, DC

Maritime and International Trade

- Natalie concentrates her practice on maritime transactions, corporate governance, and ship financing matters.
- Natalie has experience in maritime transactions under U.S. and foreign laws, such as:
  - Vessel secured financings
  - Vessel lease financings
  - Ship purchases and sales
  - Vessel charters
  - Maritime bankruptcies and restructurings
  - Corporate governance and structure issues for domestic and foreign companies

# Jones Act + VIDA/VGP Status and Enforcement

Dana Merkel



# The Jones Act

- The Jones Act requires that waterborne transportation of merchandise between two “points” in the U.S. must take place aboard a vessel that is:
  - U.S.-built
  - 75% U.S.-owned
  - U.S.-flag (U.S. crew)
- Similar laws apply to transportation of passengers, as well as towing and dredging
- Collectively known as the coastwise laws





# How do the coastwise laws apply to offshore work?

- All points in the territorial sea (3 nm)
  - Outer Continental Shelf Lands Act (“OCSLA”) extended application of the coastwise laws to installations on the outer continental shelf related to mineral production
- Customs and Border Protection (“CBP”) interprets and enforces the coastwise laws
- For many years, there was a lack of clarity regarding the status of some types of offshore work
  - Interpretations developed through CBP rulings
  - Extremely controversial

# Lifting Operations and Equipment of the Vessel

- CBP issued a Customs Bulletin proposal on October 23, 2019 and a final decision on December 11, 2019 reinterpreting lifting operations and equipment of the vessel
  - Equipment of the vessel
    - Eliminates the “mission of the vessel” and related justifications for determining items to be equipment of the vessel
    - Goes back to initial definition: “necessary and appropriate for the navigation, operation, or maintenance of the vessel and for the comfort and safety of persons onboard”
  - Lifting operations
    - “lifting by cranes, winches, lifting beams, or other similar activities or operations, from the time that the lifting activity begins when unloading from a vessel or removing offshore facilities or subsea infrastructure until the time that the lifting activities can be safely terminated in relation to the unloading, installation, or removal of offshore facilities or subsea infrastructure”
    - Includes the initial vertical movement of an item, as well as any vertical or lateral movement necessary to safely place or remove an item from the vicinity of an existing structure
- Effective February 17, 2020
- At the time, it was still unclear how the coastwise laws applied to offshore wind

# What about offshore wind?

- The 2021 National Defense Authorization Act amended OCSLA to extend the coastwise laws to OCS points related to wind energy
- Same interpretations used for oil and gas projects now also apply to wind projects
- CBP has already issued rulings applying the Jones Act to offshore wind developments



# Potential Penalties

- **Merchandise Violations**

- Penalties may be assessed against any person transporting the merchandise or causing it to be transported, including the importer, consignee, master, vessel agent, or vessel owner/operator

- **Penalties**

- Include seizure of the merchandise transported illegally or a penalty up to the domestic value of the merchandise or actual cost of the transportation, whichever is greater

- **CBP's Mitigation Guidelines: Fines, Penalties, Forfeitures and Liquidated Damages**

- Unless vessel in distress or some humanitarian reason for coastwise violation, it will be considered commercial expediency
- First violations commonly mitigated to 10%
- Repeat offense hurts possibility of mitigation

# Enforcement trends



- For many years, there were few Jones Act enforcement actions
- Upward trend in recent years
  - More penalties being issued
  - Also being issued to multiple parties related to the transportation
- CBP compliance and enforcement efforts
  - Jones Act Division of Enforcement (JADE)
  - eAllegations

# EPA's Vessel General Permit and VIDA (Vessel Incidental Discharge Act)

- **EPA's Vessel General Permit**

- In place since 2008
- Revised in 2013 and VGP 2013, which was generally an improvement on the prior version, is still in effect
- Covers 27 incidental discharges from vessels – BMPs, training, inspections, sampling, annual report

- **VGP 2013 will be replaced by Vessel Incidental Discharge Act**

- Signed into law on December 4, 2018 → amended the Clean Water Act
- VIDA generally preempts state/local laws, some state provisions included, but states can now inspect and enforce
- Provides that EPA must set uniform standards for incidental discharges
- USCG will be the enforcing agency
- ***Applies out to 12 nm, whereas VGP only applied out to 3nm***
  - May pose some operational challenges for managing certain discharges

# VIDA Implementation



- **EPA** is required to develop performance standards for each type of discharge incidental to the operation of a vessel
  - No less stringent than the VGP 2013, absent scientific evidence supporting a less stringent standard
  - *If numeric limits infeasible, EPA may use best management practices*
  - Must review/revise every 5 years



- **USCG** to promulgate compliance, inspection, and enforcement regulations for the design, construction, installation, and operation of the equipment and management practices required onboard vessels
  - No less stringent
  - Develop, with states, inspections and monitoring procedures
  - *This will be very significant part of the rulemaking as it will govern all operations.*

# VIDA Status

- **EPA issued NPRM with proposed performance standards on October 26, 2020**
  - Comment period closed November 25, 2020
  - Several hundred substantive comments were submitted and 28,701 comments overall
- **Final rule was statutorily required to be published by December 4, 2020 – missed deadline....**
  - Anticipated that there will be changes
  - EPA held a listening session last month
  - Continuing to take input despite the comment period having closed nearly a year ago and will accept comments through November 30
  - Speculation that EPA will take next steps in summer 2022, but unclear whether they will finalize a rule or re-propose different standards
- **Once EPA regulations are final, USCG's rulemaking process will begin → 2 years**
- **2013 VGP requirements remain in place, and may not be modified, until USCG regulations are final!**



# VGP Enforcement – Examples (since 2009-2019)

- **Over past 10+ years, only a handful of enforcement actions**
  - *Failure to conduct inspections required by the VGP (2014)*
    - \$6,600
  - *Accidental discharge of pool water (reported to EPA) (2012)*
    - \$20,000 penalty
  - *Excessive underwater ship husbandry discharges reported to EPA, not USCG (2013)*
    - Development of SOPs and training materials and \$37,500 penalty assessed
  - *Discharges exceeding water quality limits for mercury (2013)*
    - \$25,000
  - *Failure to submit NOIs or PARIs (2016)*
    - \$38,397
  - *Discharging without a permit*
    - \$1,500
  - *Warnings for smaller companies*

# VGP Enforcement (2020-2021)

- **EPA 308 Information Requests per the VGP**
  - *“EPA has identified several areas of concern. EPA requires additional information to assess your compliance with the requirements of the CWA.”*
- **Enforcement Actions, particularly in Regions IX and X**
  - Three “significant” enforcement actions
  - Regions coordinating with EPA HQ
  - **Per EPA: “*This is just the beginning...*”**
- **Environmental enforcement dropped dramatically under the Trump Administration**
  - According to a report from the Environmental Crimes Project at the University of Michigan, there was a 70% drop in Clean Water Act prosecutions and a 50% drop in Clean Air Act prosecutions
  - Now, seemingly on the uptick

# VGP Enforcement (2020-2021) (cont.)

- **Key Issues Identified:**

- Notices of Intent (not filed or inaccurate)
- Notices of Termination (not filed, so company still subject to VGP, including Annual Reports)
- Failure to do Routine Visual Inspections (voyage/daily)
- Failure to do Comprehensive Annual Inspections
- Ballast Water – kicks in once BWMSs used
  - Effluent Biological Organism Monitoring
  - Residual Biocide and Derivative Monitoring
  - Equipment Calibration
  - Comparing NBIC reports with Annual Reports
- Impact on non-enforcement policy

# Decarbonization

## Stefanos Roulakis



# Maritime Decarbonization – An Overview

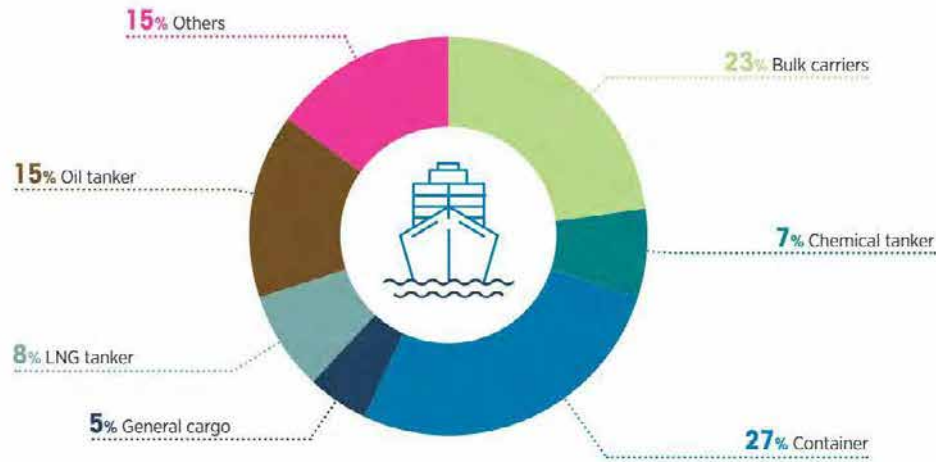
- Maritime decarbonization reduces green house gas (GHG) and Carbon Dioxide (CO<sub>2</sub>) equivalents from the emissions produced by ships and their supply chains. It is a growing global concern and a key goal for the maritime ecosystem.
- The global shipping sector emits 1 billion metric tons of carbon dioxide each year, according to the Ocean Conservancy, which, for reference is the same amount of Germany's annual emissions.
- Recent Developments: COP26, Levy on Fuel



Source: GREEN COMMERCIAL SHIPPING SCITECH EUROP

# Energy Consumption in the Maritime Industry

Figure 3 Voyage-based allocation of energy consumption for international shipping

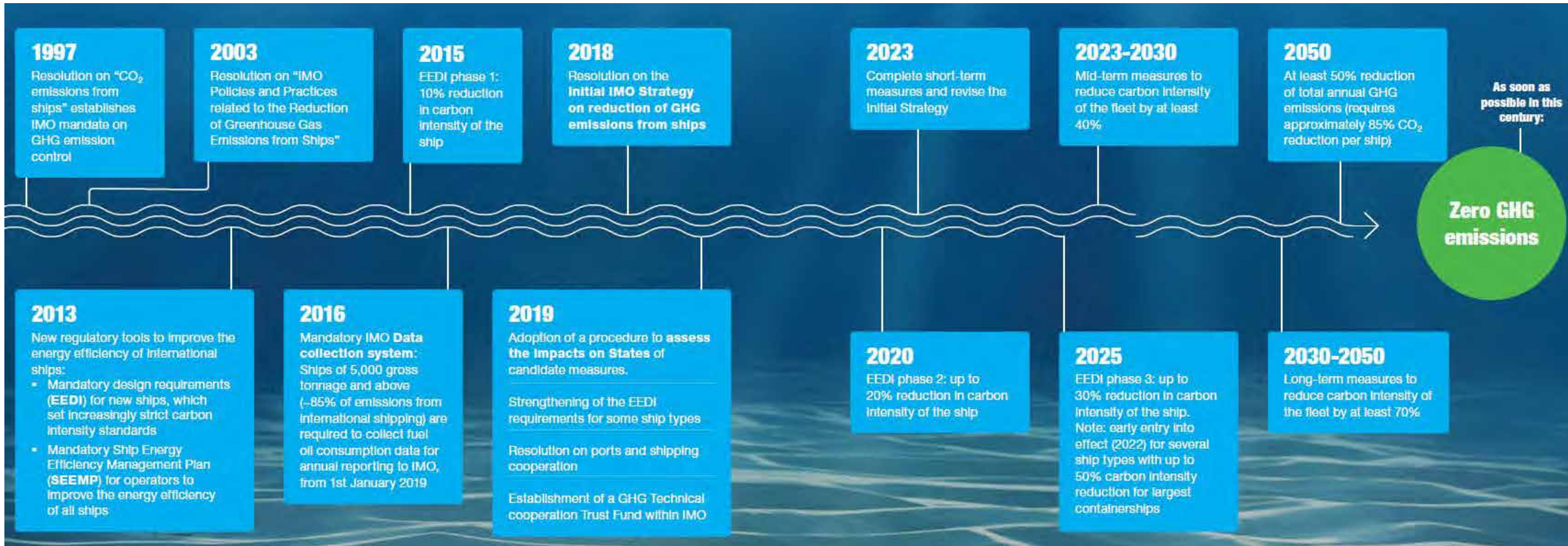


Note: "Others" includes other liquid tankers, ferry-pax only, cruise, ferry-Ro-Pax, refrigerated bulk, ro-ro, vehicle, yacht, service-tug, miscellaneous-fishing, offshore, service-other, miscellaneous-others.

Source: IMO (2020a)

- Shipping accounts for about 2.9% of global greenhouse gas emissions, according to the International Maritime Organization.
- IMO forecasts that maritime trade could increase between 40% and 115% by 2050 in comparison to 2020 levels.
- About 99% of energy demand from the international shipping sector is met by fossil fuels.
- IMO warned that in the absence of suitable mitigation policies, GHG emissions associated with the shipping sector could grow between 50% and 250% by 2050.
- Studies show that simply reducing emissions in current vessels will not be enough to reach the goals; zero-emission ships must start entering the global fleet by 2030 and increasing their numbers significantly in the following years.

# Timeline of IMO Action to Reduce GHG's from Ships



Source: IMO

# Overview of IMO's strategy

- IMO's MEPC met to discuss decarbonization during the MEPC 76 meeting, held from June 10-17, 2021.
  - The Committee adopted resolution MEPC.328(76) containing amendments to MARPOL Annex VI concerning mandatory goal-based technical and operational measures to reduce carbon intensity of international shipping. These amendments will enter into force on 1 November 2022. Relevant EEXI and CII Technical Guidelines were adopted.
  - The IMO's Marine Environment Protection Committee (MEPC) has settled on an achievable 11 percent carbon intensity reduction target for 2026. The target is calculated on a per-tonne-mile basis.
  - The Committee also adopted resolution MEPC.329(76) containing amendments to MARPOL Annex I to incorporate a prohibition on the *use and carriage* for use as fuel of heavy fuel oil by ships in Arctic waters (banning HFO on and after July 1, 2024)
- IMO's MEPC's next meeting, the 77th Session will be held from November 22 – 26, 2021.



# Facts and Figures

- The IMO conducted its 4<sup>th</sup> GHG study in 2020. Earlier IMO GHG Studies have been published in 2000, 2009 and 2014. Findings from the 2020 study include:
  - The share of shipping emissions in global anthropogenic emissions has increased from 2.76% in 2012 to 2.89% in 2018.
  - Carbon intensity has improved between 2012 and 2018 for international shipping as a whole. The overall carbon intensity, as an average across international shipping, was 21 and 29% better than in 2008, measured in AER and EEOI respectively in the voyage-based allocation

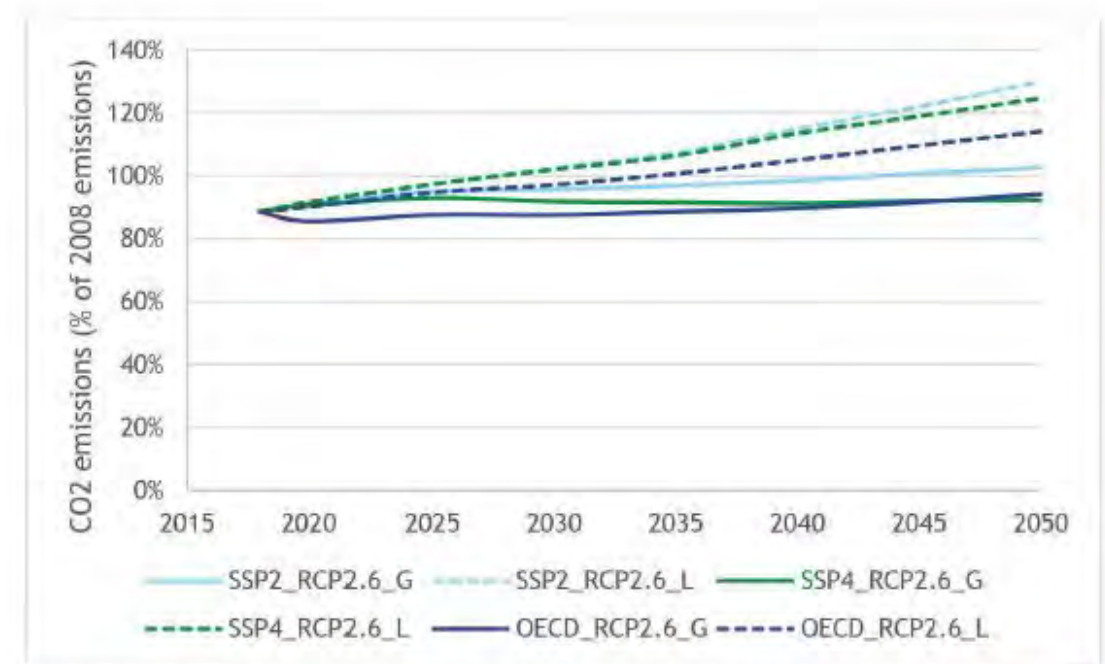


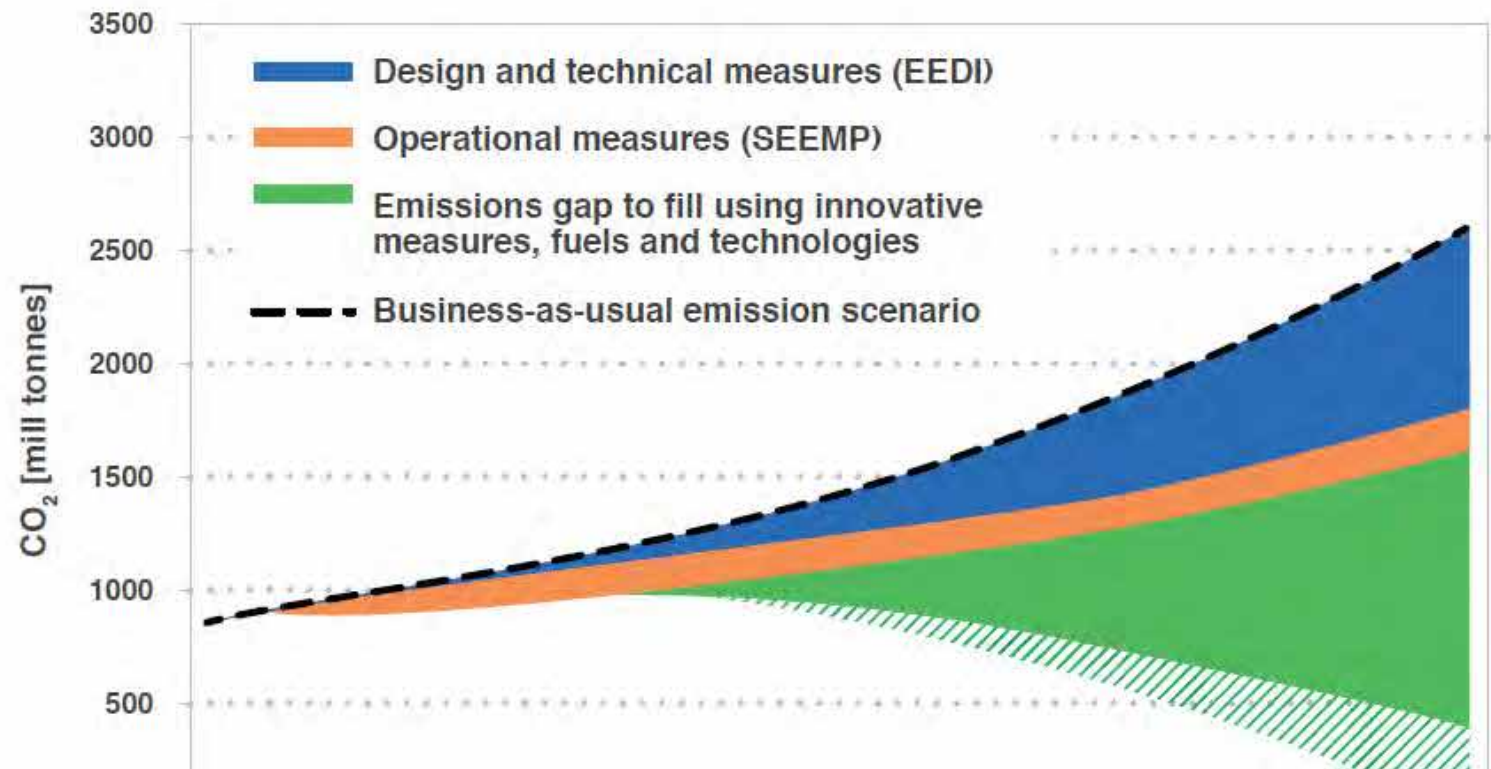
Figure 1 – Projections of maritime ship emissions as a percentage of 2008 emissions

Source: IMO

# How to Achieve the IMO's GHG 2050 Goals

The chart is an illustration of the overall GHG reduction pathway to achieve IMO's ambitious goals, i.e. the absolute level of GHG emission reduction identified in the IMO GHG Strategy (at least 50% reduction by 2050 expressed in the illustrative chart in solid colours and green stripes).

The IMO GHG Strategy provides a wide list of **candidate short-term, mid-term and long-term measures**, including for example further improvement of the EEDI and the SEEMP, National Action Plans, enhanced technical cooperation, port activities, research and development, support to the effective uptake of alternative low-carbon and zero-



Source: IMO

# Regulation of Shipboard Emissions

## *International*

- MARPOL Annex VI (Air)—SOx and NOx emissions

## *Paris Accords*

- COP26
- *Potential Levy on Fuels*

## *Current U.S. Law*

- The Act to Prevent Pollution from Ships (APSS) (33 U.S.C. §§1905-1915)
- USCG and EPA develop standards and enforce vessel air emissions

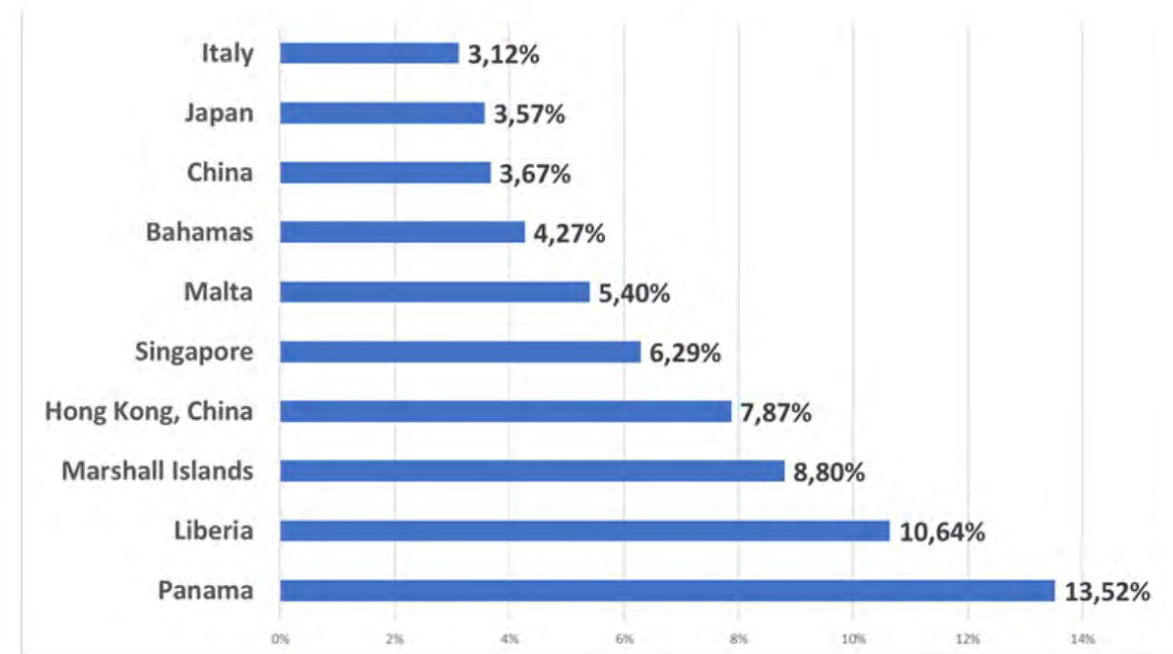
## *Pending Legislation and Regulation*

- In both the 116<sup>th</sup> and 117<sup>th</sup> Congresses, there have been bills introduced to regulate air emissions from shipping, as well as hearings
- The U.S. “is committ[ed] to work with countries in the International Maritime Organization to adopt a goal of achieving zero emissions from international shipping by 2050, and to adopt ambitious measures that will place the sector on a pathway to achieve this goal.”

# The Role of Flag States in Maritime Decarbonization

- Flag states will have to ensure that ships are compliant with applicable IMO rules regarding the implementation of the IMO GHG emissions strategy
- Flag states could see their involvement also as a business opportunity, where more transparent and reliable flag states provide better services than others.
- Many flag states are themselves experiencing the results of sea level rise and other aspects of climate change. Thus, it is also in their interest to reduce GHG emissions from ships.
- In fact, on September 27, 2019, the Governments of Fiji, the Marshall Islands, Solomon Islands, Tuvalu and Vanuatu launched a partnership to make shipping in the Pacific Ocean zero carbon by 2050.
- A notable flag state, the Marshall Islands, submitted a proposal to levy a \$100 per ton bunker carbon tax. However, this was voted down at the MEPC 76 meeting.
- Role of Chartering agreements to serve these markets is also important

Estimated share of global maritime CO2 emissions, 2019  
Top 10 flags of registration



Source: UNCTAD

# Decarbonization Efforts

- **Technological measures:** low-sulfur fuel oil; switch to alternative fuel options (such as hydrogen, methanol, biofuel, LNG/LPG, batteries, and ammonia); fuel cells, speed reduction, hull coating / cleaning, air lubrication, and weather routing.
- **Operational measures:** (fleet-related): speed management, route planning, and voyage optimization to maximize safety and fuel efficiency.
- **Market-based measures:** Economic mechanisms such as taxes, incentives, and green shipping credits.
- **Management measures and “Decision Support Models”:** network design, fleet deployment, berth allocation, scheduling optimization, and vessel routing.



# Decarbonization Efforts (Cont'd)



- Sea transport is the most environmentally friendly way of carrying goods; however, some cargo ship operations can be grossly inefficient, for example the practice of “Steam Fast, Then Wait”: ships sail to their port of destination at their service speed, without regard for the conditions at that port. Largely as a result of this, dry bulk carriers and tankers spend about 8-10% of their entire life at anchorage.
- Academic research suggests that eradicating the steam fast and wait practice and introducing Just-in-Time practices would result in emissions’ savings in the order of 20-25%

# Decarbonizing Marine Propulsion - Alternative Fuels

## FUTURE MARINE FUELS

### PATHWAYS TO DECARBONIZATION

IMO has developed the ambitious target of a minimum **50% reduction** in greenhouse gas (GHG) emissions **by 2050**.

Shipowners have **alternative fuel options** to help them meet IMO's ambitions, each with its own advantages and challenges.

- Advantages
- Challenges



Source: ABS

# Fuel R&D Realities

- The report entitled A Zero Emission Blueprint for Shipping, prepared with strategic consultancy Ricardo, outlines the urgent steps that they believe will be required to completely transform shipping's current dominant propulsion technology and fuels.
- To ensure shipping can achieve what the report calls "its 4th propulsion revolution," they highlight the need for a major scaling up of finance for technology and development in shipping.
- They have identified a list of more than 260 example R&D projects needed to overcome key technical and systemic challenges and accelerate the transition to zero-carbon emissions in shipping. They estimate the cost for those projects to be \$4.4 billion.
- Among the projects are 20 example projects in hydrogen, ammonia, and battery power that they contend could serve as a potential blueprint for R&D projects to be commissioned in the future. Many of the projects identified will take between one and six years to reach commercialization.
- The ICS is using the report to again call attention to the proposal for a \$5 billion R&D fund, called the International Maritime Research Fund, that they have been advocating for to assist with the efforts for decarbonization.





# Funding the Global Transition



- It is important to obtain varied sources of funding, going beyond those offered by banks, such as private investment, and blended financing.
- Concerns exist with securing funds when scaling up projects after trial periods.
- Maritime innovation is currently considered a niche sector for financial stakeholders, which may be the reason for a limited number of participants in this market.
- The IMO is active on this front, together with European Bank for Reconstruction and Development and the World Bank, they have created the FINSMART Roundtable, to bring together project beneficiary countries, donors and International Financial Institutions, as well as other financial sector representatives to discuss financing risks, opportunities and identify potential financial product.

# Decarbonization Funding Proposals

- The CEO of Maersk Tankers A/S, stated that wants a carbon tax for his industry by 2025, and he's confident his customers are willing to pay for it.
- A.P. Moller-Maersk A/S previously pitched a fee of \$150 a ton for CO2, which would increase the cost of a common marine fuel in Rotterdam by about 75%, using current figures.
- \$100/ton gained traction at COP26
- Commodities giant Trafigura Group Pte suggested \$250-\$300 a ton.
- A global industry carbon tax would come from the IMO, Discussions are still in the early stages. The IMO's next major meeting on marine pollution is in late November.

# Recent Developments in Maritime Decarbonization

- The Port of Seattle's commission has voted to speed up its carbon-cutting efforts by ten years and now aims to achieve net-zero emissions from its own operations by 2040. The port is also participating in two regional studies to evaluate the potential role of renewable hydrogen - among other potential fuels - as an emerging zero-emission energy source for maritime industrial uses.
- Shipping decarbonization was a central topic of discussion at the Global Maritime Forum's Annual Summit in London, following the presentation to the COP26 Presidency of the Getting to Zero Coalition's [Call to Action on Shipping Decarbonization](#). The signatories include the Panama Canal and more than 150 other organizations across the maritime value chain
- As it stands, the IMO is targeting a 40% reduction in CO<sub>2</sub> emissions by 2030 and a 50% cut in greenhouse gas emissions by 2050. But the European Union, US, UK, Norway and Costa Rica have pushed for more ambitious cuts with hopes of reaching zero-emissions shipping by 2050.
- The US, UK, Norway and Costa Rica submitted a proposal in September arguing for the more aggressive cuts and requested the MEPC review the strategy in the coming months.

# Recent Developments in Maritime Decarbonization (Cont'd.)



- A group of nine major companies including Amazon, Ikea and Unilever pledged on October 16, 2021, to only use ocean shippers that run on zero-carbon fuel by 2040. The initiative is known as [Cargo Owners for Zero Emissions Vessels](#).
  - The companies said that they will work to track their maritime transportation emissions, seek opportunities to expand the group of cargo owners engaged in maritime decarbonization and unify their collective freight demand to help accelerate the transition.
- Royal Caribbean group announced that it has achieved its carbon reduction target of 35% compared to a 2005 baseline and has committed to further reduce emissions by 25% by 2025 from 2019 levels.
- The IMO and the Maritime and Port Authority of Singapore have launched the NextGEN web portal, an online collaborative global ecosystem of maritime transport decarbonization initiatives.
  - Currently, the portal encompasses over 140 projects spanning over 500 partners and 13 fuel types.

# Potential Challenges and Questions to Consider

## Potential challenges include

- the costs of outfitting mid-aged vessels to run on alternative fuels
- the availability and cost of zero-carbon fuels

## Questions to be considered include

- When will any new legal requirements take effect?
- How will maritime decarbonization affect the role of autonomous shipping?
- How will AI play a role in maritime decarbonization?
- Can developing nations help address this challenge while also creating major business and investment opportunities?
- Will there be incentives for early actors?
- How will uniform enforcement be administered?
- How will port infrastructure and impacts be addressed?
- How will adequate financing be obtained for R&D and infrastructure?

# Role of Insurance in Ship Finance

Natalie Radabaugh



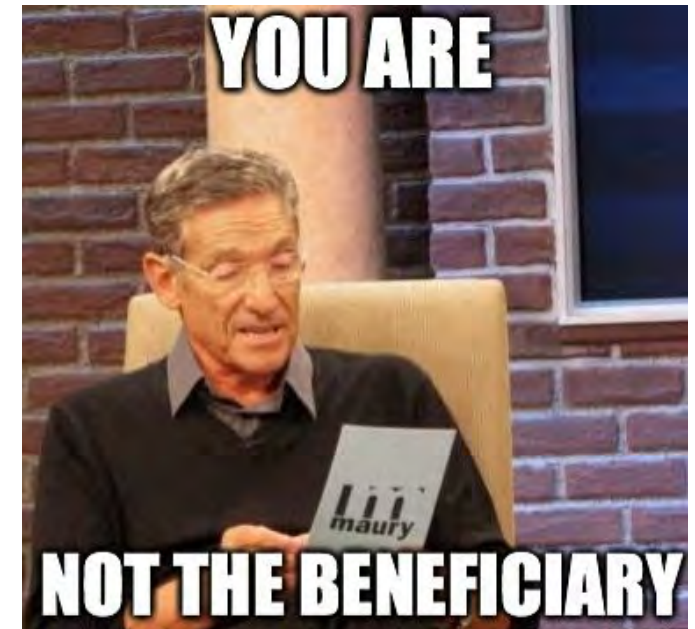
# Why talk about Insurance?

- Protect investment
- Reduce risks
- Preparedness
  - Understanding the rationale behind types of insurances and specific requirements and ensuring the insurances are placed properly at closing can save time and money in the future if a casualty event or a default under the loan agreement by the borrower occurs.



# Insurance Requirements Overview

- Deal Specific
  - Customary set of requirements that are negotiated and modified by the parties based on factors such as loan amount, vessel type and intended use, existing coverages, single vessel vs. fleet cover, price of additional coverage
- Location of Requirements
  - Comprehensive schedule of insurances vs. insurance provisions scattered throughout multiple loan documents
- Who gets the insurance proceeds?
  - Generally, require that the mortgagee is entitled to all insurance proceeds.
- Prudent Shipowner Standard
  - Require the shipowner to carry insurances in the type and amount that a prudent shipowner of similar vessels engaged in similar trade would have.
- Insurance Requirements at Closing and Annual Renewals
  - Prepare and preposition in advance of closing vs. post-closing requirements
  - Annual Renewals – often require same documentation as at closing
- Be on the look out for new or changing requirements related to ESG
  - Marine insurers are debating their own Poseidon Principles scheme for monitoring emissions performance of vessels.





# Main Categories of Marine Insurances

- Two main categories of marine insurance in a ship financing:
  - Hull and Machinery (H&M)
  - Protection and Indemnity (P&I)
- Other common types of insurances in ship financing:
  - Mortgagee's Interest Insurance (MII) and Mortgagee's Interest Additional Perils Pollution (MAPP)
  - Increased Value (IV)



# Types of Insurance – Hull and Machinery

- Hull and Machinery
  - Protects against physical damage to the hull and all other tangible property that is part of the vessel (e.g., engines, equipment, machinery, generators, etc.).
  - May also contain protection against war risks, for the perils of confiscation, expropriation, nationalization, seizure, blocking, and terrorism
  - Coverage amount – typically not less than 110-120% of the principal amount of the loan outstanding at closing and at each renewal.



# Types of Insurance – Protection and Indemnity (P&I)

- Protection and Indemnity = liability insurance
  - General Liability Policy vs. Entry into a P&I Club
    - P&I Club – mutual insurance association that pools risk amongst its members
  - Common coverages include protection against:
    - Loss of life, injury and sickness of crew, passengers, third parties
    - Collision liability
    - Wreck removal costs
    - Damage to cargo on board the vessel
    - Damage to certain fixed floating objects such as piers, docks, and jetties, etc.
    - Pollution, spillage, leakage
  - Extra coverages for passenger vessels → passengers, liquor, premises liability
  - Coverage amount – require coverage at the maximum amounts available
    - Estimated to be \$7,500,000,000 for standard marine practice and \$1,000,000,000 for pollution.

**IGP&I** International  
Group of  
P&I Clubs



**BLANKROME**  
maritime

# Types of Insurances - Mortgagee's Interest Insurance (MII) and Mortgagee's Additional Perils (Pollution) Insurance (MAPP)

- “Back-Up” Policies – Provide cover in the event the borrower’s insurances does not respond.
  - Lenders often require these to avoid any potential risk of loss and shipowners generally believe these are an unnecessary expense because they operate in compliance with the insurance policies.
- MII
  - Covers the mortgagee for the outstanding loan amount plus interest in the event that a claim that would generally be covered under the underlying policy is not paid out due to a breach of the insurances by the shipowner.
- MAPP
  - Cover triggered when a vessel is held liable for a pollution spill that exceeds the limit provided by the P&I policy leading to the seizure of the vessel or the proceeds of the total loss of the vessel.
  - Most common for tankers trading to the United States.
- Who should place the MII/MAPP policies?
  - Best practice → From lender’s perspective, placed directly by the lender/mortgagee not the shipowner.

# Types of Insurances – Increased Value (IV)

- Provides cover in excess above the market value up to the full loan/mortgage amount.
- Intended to cover the additional costs of replacing a vessel following a total loss.



# Special Scenarios

- Pre vs Post Delivery Insurances

- There are different insurances and insurance requirements for when a vessel is being constructed and after delivery.
  - Builder's Risk – covers the vessel and related property through construction and sea trials.
- Cover switches once the vessel is delivered.
- For a newbuild where the lender is providing both pre and post delivery financing, it is common to have all insurances negotiated together before closing.



- Laid Up Vessels – Navigation vs. Port Risk Insurance

- Navigation insurance – standard insurance for vessel that is operating
- Port Risk Insurance – reduced coverage for a vessel that is laid up for an extended period of time (generally more than 30 days).
- Beware of Classification Society requirements and restrictions in the loan documents.



# Insurance Requirements – Key Lender Provisions

- Lender will want to be a loss payee and named as an additional assured or insured or, as applicable.
- For policies of insurance (not P&I club entries), contain provisions waiving the underwriters' rights of subrogation thereunder against any assured named in such policy and any assignee of that assured.
- Provide that the lender and its successors and assigns shall not be responsible for any premiums, club calls, assessments or any other obligations or for the representations and warranties made therein by the shipowner or any other person.
- Lenders often want to restrict deductible amounts to ensure the borrower can cover the amounts.

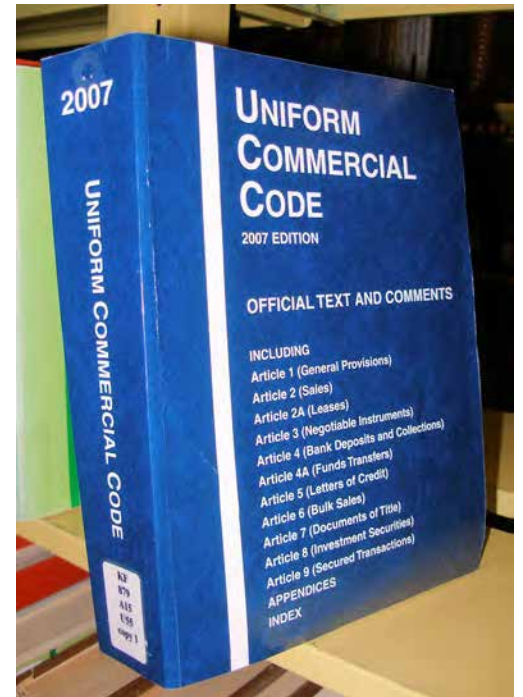
# Insurance Requirements – Key Lender Provisions (Cont'd)

- Provide that the insurer will provide the lender prior written notice (usually 14 or 30 days) of expiration, cancellation, termination, non-renewal, default in the payment of any premium, reduction in amount or any material alteration or modification of any of such insurances.
- In the event of a total loss of the vessel or if an event of default has occurred and is continuing, the amounts recoverable by the shipowner under the insurances in respect of the total loss or any other claim shall be paid to the lender per the loss payable clause for distribution pursuant to the loan agreement.
- In case any underwriter proposes to pay less on any claim than the amount thereof, the shipowner shall immediately inform the lender, or if there is a total loss of the vessel, and if an event of default under the loan agreement has occurred and is continuing, the lender shall have the exclusive right to negotiate and agree to any agreement, arrangement or compromise with the underwriters of such claim.



# Insurance Policies and the Uniform Commercial Code (UCC)

- Not all types of insurances are treated equally under Article 9 (Secured Transactions) of the UCC
- Included in “Proceeds”
  - The definition of “proceeds” in 9-102(64) includes insurance payable by reason of the loss or damage to the collateral.
  - Under 9-315(c), if a lender has a perfected security interest in the underlying collateral, then it has a perfected security interest in the proceeds thereof.
  - Thus, if a lender has a perfected security interest in tangible personal property, then any payments under the property insurance policy resulting from loss or damage are considered proceeds of the property and would be subject to the provisions of the UCC that deal with proceeds.

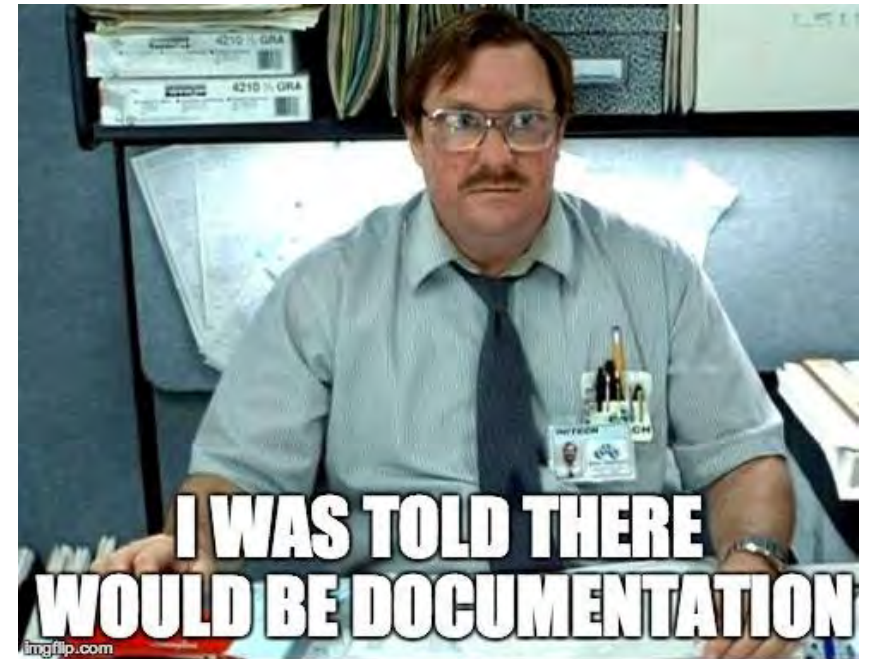


# Insurance Policies and the Uniform Commercial Code (UCC) (Cont'd)

- However, there is a long-standing general exclusion of most types of insurance policies and the rights under such policies from the scope of Article 9:
  - UCC § 9-109(d)(8) – This article does not apply to: “a transfer of an interest in or an assignment of a claim under a policy of insurance, other than an assignment by or to a health-care provider of a health-care-insurance receivable and any subsequent assignment of the right to payment, but Sections 9-315 and 9-322 apply with respect to proceeds and priorities in proceeds.”
  - *In re Montreal, Maine & Atlantic Railway, Ltd.*, 799 F.3d 1 (1<sup>st</sup> Cir. 2015)
    - Lender had a perfected security interest in the accounts, general intangibles, and payment intangibles, but it did not have a separate pledge agreement or assignment of the insurance policy.
    - First Circuit ruled that payments under a business interruption policy fell within the exclusion of 9-109(d)(8) – “[T]he assignment of a right to payment under an insurance policy, which is inseparable from the policy itself, falls squarely within the heartland of the exclusion.”
    - “[B]y its terms, the insurance exclusion applies broadly to interest on as well as to claims under an insurance policy.”
    - Need to look to state law other than the UCC for the assignment and a security interest in the insurance policies.
- Best practices – a secured lender should require that it is listed as an additional assured/insured and be named as loss payee on the policies and obtain a common law assignment of the insurances that satisfies the applicable state law rules.

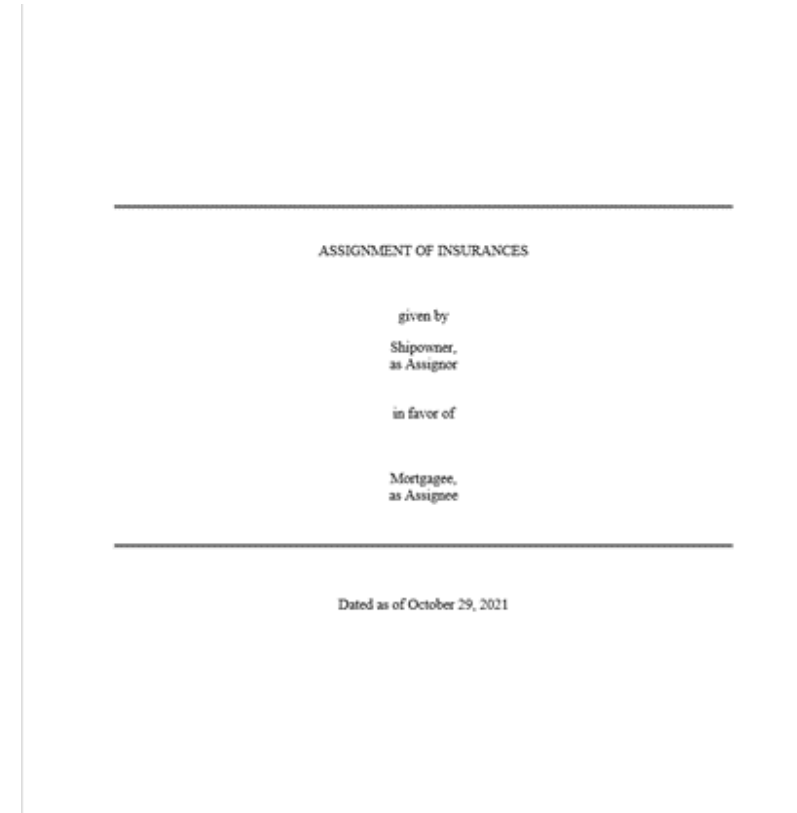
# Insurance-Related Documents

- Customary Insurance Documents
  - Loan Documents
    - Assignment of Insurances
    - Notice of Assignment
    - Loss Payable Clauses
  - Broker Documents
    - Broker's Letter of Undertaking
    - Evidence of Insurance
      - Copies of policies, Certificate of Insurance, Certificate of Entry, etc.



# Insurance-Related Documents – Assignment of Insurances

- Common law assignment
  - Formalizes the mortgagee’s rights to the insurance policies and proceeds.
  - Shipowner will grant the lender a first priority security interest in the insurance polices, moneys due to the shipowner paid out under the policy, and proceeds of the foregoing
- Grant of a security interest in the following (“Insurances”):
  - all policies and contracts of insurances (including all insurances with respect to hull and machinery, war risk, protection and indemnity, breach of warranty, pollution, requisition of title or otherwise), and the Assignor’s rights under all entries in any protection and indemnity or war risk association or club, relating to the Vessel, its hull, machinery, equipment, appurtenances and outfits, freights, earnings, disbursements, profits or otherwise, whether heretofore, now or hereafter effected, and all renewals of or replacements for the same;
  - all moneys and claims for moneys due and to become due to the Assignor under such insurances with respect to the actual, constructive, agreed, arranged or compromised total loss or any other loss or damage to the Vessel, including requisition for title, seizure, condemnation, confiscation, sequestration or compulsory acquisition or otherwise of the Vessel, and all claims for damages or compensation with respect thereto;
  - all rebates and returns of premium under such insurances;
  - all other rights and benefits of the Assignor under or in respect of such insurances, including all moneys and claims for moneys in connection therewith; and
  - any and all proceeds of all of the foregoing.



# Insurance-Related Documents – Assignment of Insurances (Cont'd)

- Other key provisions under an Assignment of Insurances
  - Requirement that the Notice of Assignment be sent to all underwriters, insurance brokers, and P&I clubs and that the loss payable clauses be endorsed on all policies and or certificates of entry.
  - Step-in rights
    - Following an event of default, typically have the right (but not the obligation) to assume the shipowner's position under the insurances and in such capacity perform the shipowner's obligations, if any, under the insurances and to exercise the shipowner's rights under the insurances

# Insurance-Related Documents – Notice of Assignment

- Purpose: Provide Notice to the underwriters, insurance brokers, and P&I club that the Shipowner has assigned all of its right, title, and interest in, to and under all insurances with respect to the vessel to the lender/mortgagee.
- Directs the underwriters, insurance brokers, or P&I club to make payments in accordance with the loss payable clauses.

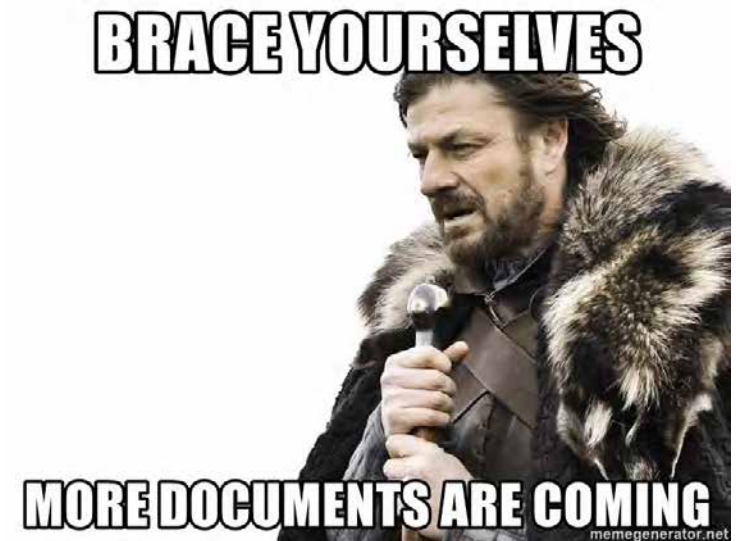


# Insurance-Related Documents – Loss Payable Clauses

- Typically, one for Hull and Machinery and one for P&I
- Generally, will direct any payments due to the shipowner be made to the lender/mortgagee.
- Ideally from a lender’s perspective, the loss payable clause will require the underwriters to provide notice to the lender/mortgagee with respect to any of the following:
  - Impending cancellation of the policy
  - Failure to renew the policy
  - Any material change in coverage prior to such material change becoming effective
  - Any act, omission, event that the insurer has knowledge of that may invalidate or render the insurances unenforceable
  - Any default in payment of premiums
- Ensures there is no recourse against the lender/mortgagee for payment of premiums, calls, commissions, assessments, or advances and provides that the lender/mortgagee may, but is not required to, pay any premiums not paid by the shipowner.
- Specific to Hull & Machinery
  - Typically, there is an exception in the case of any loss involving damage or liability to the vessel that permits the underwriters to pay the directly for the repair, salvage, liability or other charges involved, or if the shipowner has already fully repaired and the damage and paid for the cost thereof out-of-pocket, or discharged the liability or paid all of the salvage or other costs, then the underwriters may reimburse the shipowner for such costs.
    - Usually, there is a dollar cap on this amount and payments to the shipowner are not permitted if there has been an event of default.
- Specific to P&I
  - P&I Clubs usually have their own standard forms that are basically non-negotiable.
  - Lender is not able to pick off any payments owed directly to third parties.

# Insurance-Related Documents – Broker Documents

- Because the broker arranges the coverages, it is customary for lenders to require the broker to provide certain documentation and assurances.
- Broker's Letter of Undertaking (LOU)
  - Confirms the particulars and placement of the marine insurances covering the vessel and its compliance with the insurance requirements under the loan documents.
  - Confirms the acceptance or acknowledgment by the underwriters of the notice of assignment of insurances and the endorsement of loss payable clauses on the policies.
  - Agrees not to make any material changes to the insurance without first notifying the lender/mortgagee.





# Insurance-Related Documents – Broker Documents (Cont'd)

- Broker's Letter of Undertaking (Cont'd)
  - Notice to the lender/mortgagee
    - broker will advise if any of the following occur: if the broker is no longer the broker for the policies, there are changes to the policies that would materially adversely change the terms of the policies, and if they have not received renewal instructions from the owner/bareboat charterer with a certain time frame before expiration of the policies
    - Broker will forward any notices of cancellation of the policies received from the insurers
    - Upon written request from the lender/mortgagee, advise of the current premium payment situation for the policies
  - Cause the policies to be endorsed to require notice to lender/mortgagee before any cancellation, termination, or material modification of the policies (subject to non-payment)
  - Broker's lien on fleet policies for premiums is confined to the outstanding premiums due on the subject vessel(s) only.
  - Set off
    - Broker will not set off against any sum recoverable in respect of a claim against a vessel, any sum claimed by the broker of any other vessel.
    - Broker will cause the policies to be endorsed to provide that the insurers shall neither (1) set off against any claims in respect of a vessel any premiums due in respect of other vessels under the fleet cover or any premiums due for other insurances, nor (2) cancel the insurance for reason of non-payment of premiums for other vessels under the fleet cover or of premiums for such other insurances, and that insurers will, if required, issue a separate policy in respect of a vessel.

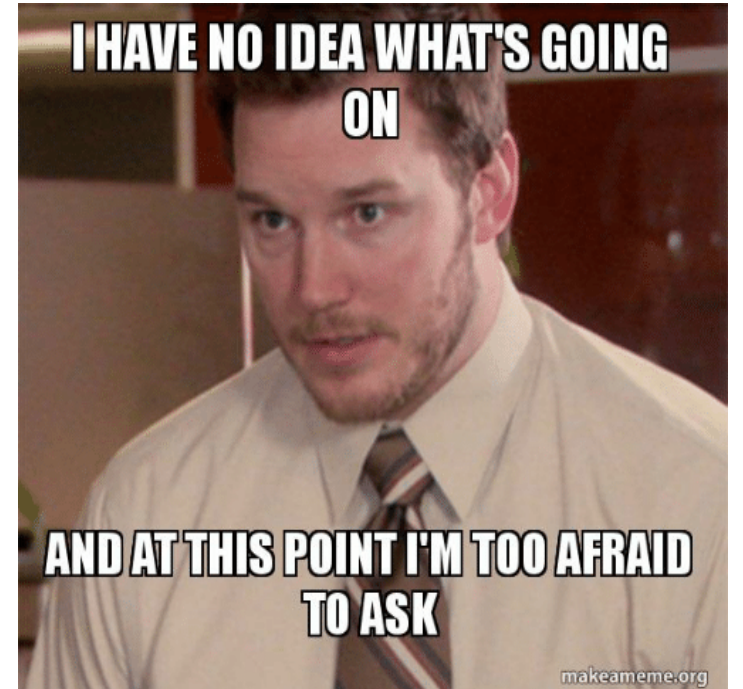
# Insurance-Related Documents – Broker Documents

- Evidence of Insurance
  - Cover notes, policy binders, etc.
  - Certificate of Insurance on Acord Form
    - Industry standard form - Certificate of Marine/Energy Insurance
  - Certificates of Entry (COEs) for a P&I club
    - Standard form from the P&I Club
    - Confirms entry of the vessel into the club and provides information about the cover



# Questions?

- Please use the Q&A button on the left side of your screen to submit questions to our presenters.
- If we do not have a chance to respond during the live session, we will follow up with you after the session.



# For more information, please contact:



**Dana S. Merkel**

Associate  
Maritime & International Trade  
Washington, DC  
202.772.5973  
[dana.merkel@blankrome.com](mailto:dana.merkel@blankrome.com)

**Stefanos N. Roulakis**

Associate  
Maritime & International Trade  
Washington, DC  
202.772.5958  
[stefanos.roulakis@blankrome.com](mailto:stefanos.roulakis@blankrome.com)

**Natalie M. Radabaugh**

Associate  
Maritime & International Trade  
Washington, DC  
202.420.2704  
[natalie.radabaugh@blankrome.com](mailto:natalie.radabaugh@blankrome.com)

**Jeanne Grasso,**

Partner & Co-Chair, Maritime &  
International Trade  
Washington, DC  
202.772.5927  
[jeanne.grasso@blankrome.com](mailto:jeanne.grasso@blankrome.com)



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