

GREEN THINKING: The Challenges of Green Financing

BY DEFINITION

UN Environment, has been working with countries, financial regulators and the finance sector, in order to align financial systems to the 2030 sustainable development goals (SDGs) agenda, breeding thus the concept of “Green Financing.”

Green Finance includes, but is not limited to:

- ⇒ Environmental aspects (pollution, greenhouse gas emissions, biodiversity, water or air quality issues); and
- ⇒ Climate change-related aspects (energy efficiency, renewable energies)

THE TREND

With the final countdown to IMO 2020 implementation date, green financing is becoming increasingly popular within the shipping industry. Exhaust Gas Cleaning Systems (EGCS's), commonly known as scrubbers, come closest to a regulatory definition of a permissible compliance option under regulation 4.1 of MARPOL, Annex VI. It is actually estimated, that 20% of global fleet, will be retrofitted with scrubbers in the next seven years.

Publicly listed companies especially, are embracing this financing trend even more warmly, as it is mandatory for their corporate social responsibility strategies, constituting evident proof that they are contributing in this way to environmental protection and sustainability goals.

SCRUBBER FINANCING Vs. EQUIPMENT FINANCING

Scrubber financing and generally most marine equipment financing, is very different from other types of equipment financing.

Scrubbers are fitted on the asset, there is cost in fitting them and there is loss in earning's, with the vessel being off-hire during installations. We are therefore talking about equipment, which is fitted on the asset, being thus an integral part of its' functionality, operation, seaworthiness and safety.

Therefore, from the financiers' side, regaining possession of the equipment, is not a simple. It entails cost of removal, uncertainty as to whether the second-hand scrubber will sell and cost of off-hire to remove the scrubber, not to mention that removal will mean that the vessel is in breach of IMO 2020 and thus subject to liabilities.

Thus, the equipment in this case, is a compliance tool for environmental protection and compliance. Its' removal can even make the vessel unseaworthy, interfering with its' insurance cover as well as its' financing. Numerous questions arise, and it is yet to be determined, who will be responsible for each cost and how both owners and financiers can be secured.

THE LEGAL CONCERNS

Legal concerns always depend on the party involved. However, areas of concern will be:

- How do we determine if it is a safe investment?
- Does the ship owning corporate structure allow loan extensions or diversified financing?
- Once installed, scrubbers are part of the vessel, will they thus become part of the first mortgage?
- Will the first mortgagee bank, consent to scrubber financing?
- If financing has been provided by vendors or other financiers, the lien will rank second, is the financier secured? For example, under English law, it is unlikely that claims in relation to installed scrubbers will generate a maritime lien in favour of the scrubber financier
- Would a finance lease structure be more suitable?
- Would a sub-participation of existing loans be more favourable?
- What will happen in insolvency procedures?
- How does an owner choose which form or green financing to opt for?
- How can the owner safeguard operations contractually, when engaging in vendor or other methods of scrubber financing?
- Is the chosen option sustainable, will we see new regulation etc.?

Whether by increase of existing mortgage, second ranking mortgages, second tier placing in cash waterfalls, or by some form of subordination, at Michael Kyprianou & Co. LLC, we provide practical solutions for every challenge!

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