Legal issues associated with the SAYS model

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Law firms, including Holman Fenwick Willan LLP, are gaining experience in drafting wording to help owners and charterers work towards eco-efficient vessels, both in relation to new builds and retro-fit technology. This briefing covers the main issues and legal solutions associated with the SAYS model promoted by the Sustainable Shipping Initiative ("**SSI**"), broken down into each agreement.

Charterparty between the vessel owner and time charterer

There are many different standard form charterparties used in the market and the intention behind the pilot project model wording is that it will be capable of widespread incorporation (with appropriate amendments in each case to take into account the individual parties' needs and the wording in the different forms).

The model wording in the charterparty under the SAYS model will accommodate intended retrofit projects, setting out the allocation of costs and obligations in respect of each party and ensuring these are clear and enforceable by the parties. This will be achieved by amending key charterparty clauses, most notably the performance warranty and hire provisions.

Performance warranty

The vessel's description and speed and performance warranty will set out the warranted fuel efficiency to be achieved after the retrofit is carried out.

Charterers will also be able to enforce the speed and performance warranty in the usual way, which may include a claim for the cost of any fuel consumed over and above the warranted amount.

Hire provisions

The efficiency premium payable by charterers to owners will be set out in a separate clause from the regular hire payable under the charterparty, but will be agreed by usual negotiation between owner and time charterer.

The reason for clearly separating the efficiency premium from the regular hire is to facilitate the financing of the retrofit costs by creating a separate stream of hire which is capable of being assigned as security for the SAYS loan whilst leaving the mortgage provider to take an assignment of all other income under the charterparty.

The hire rate and premium combined should total the same as the hire rate for the vessel were it to be upgraded without a SAYS loan; the charterer is financially in the same position regardless of the SAYS arrangements. Charterers also have the advantage of access to the publically available SAYS financial modelling tool to increase their understanding of the fuel savings and how they have been accrued by each party involved.

Typically, the objective will be for the premium to be calculated to be less than the overall savings in fuel costs that charterers expect to make from chartering a more fuel efficient vessel. The charter wording will create an enforceable obligation to pay the premium.

Performance guarantee between each technology provider and the owner

Technology providers, subject to considerations in each case, may be prepared to give owners performance guarantees similar to those currently offered on fuel saving measures. These guarantees will be structured so that in the event the technology fails to provide the guaranteed fuel efficiency increases, the owner can make a claim for a partial refund of the purchase price.

Loan agreement between SAYS finance provider and owner

The SAYS model intends that the retrofit will be financed by way of a loan from a finance provider (e.g. a bank) to the owner, usually with a proportion of the costs paid in cash by the owner. The loan will be subject to the finance provider's standard terms and will be secured by way of an assignment of the efficiency premium which can be applied against the SAYS loan in the event of a default by the owner. The loan should be structured so that the efficiency premium payments to the owner exceed the SAYS loan instalment sums. In this set up, owners will benefit because they keep the difference between the premium hire rate and the loan instalment costs, and the capital value of the vessel should also be greater.

The SAYS loan will need to conform with the requirements of the vessel's existing mortgage providers. If the SAYS finance provider and mortgage provider are different, the documentation will need to allow for the efficiency premium to be paid to the SAYS finance provider under its assignment, rather than to the mortgage provider under its general assignment of earnings. In such cases, an inter-creditor agreement between the owner and different finance providers will be required to regulate the payment of hire under the respective assignments. Such agreements are commonplace in shipping financing transactions where the ship owner borrows from two different lenders or lender groups.

It is anticipated this will be acceptable to mortgage providers for the following reasons: a) the retrofit should increase the vessel's asset value and reduce the probability of default because eco-efficient vessels are in greater demand; and b) the hire rate should not be lower than it would be without the SAYS-related efficiency premium included.

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