

SAFAL

SHIP ACQUISITION, FINANCING AND LEASING



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REPORT OF THE COMMITTEE

ON

**DEVELOPMENT OF AVENUES FOR SHIP
ACQUISITION, FINANCING AND LEASING
FROM IFSC IN INDIA**

28 OCTOBER 2021



FOREWORD

The Committee on Development of Avenues for Ship Acquisition, Financing and Leasing Activities from the International Financial Services Centres (IFSC) in India was constituted by the International Financial Services Centres Authority (IFSCA) vide its Office Memorandum No. 355/IFSCA/Dev/SL/2021-22/241 dated 24 June 2021. Its constituent members were from the government, regulators, private sector experts, academia, financial institutions, legal and tax consultants.

Working towards the fulfilment of its mandate, the Committee carried out a 360-degree review and examination of the existing legal and regulatory regime in IFSC in India for ship acquisition, financing, and leasing. The IFSC regime was compared with those of global top-ranking marine hubs. It further identified challenges and impediments to the realisation of India's shipping sector's growth potential. Focus remained on enablement of cost-effective and competitive delivery of shipping services on ships owned and leased from India-IFSC. A holistic consideration covered all types of ships, that is, those deployed for the transportation of goods and passengers across the seas, along India's vast coastline, from/to offshore fields and islands, as well as along inland waterways. The amenability to lease financing of non-weaponised defence ships (transport, fuelling vessels, tugs, barges, etc.) and those deployed in civil leisure activities like cruises was also briefly assessed.

The Committee also developed a ship-owning and financing model, for which the detailed work was done by Price Waterhouse & Co LLP. The assumptions made in the model were finely filtered and confirmed during interactions with industry and ship financiers. The model compared the cost of capital, cost of operations and tax costs and help gauge the overall implications of the suggested asks in this Report.

Gujarat Maritime Board (GMB) has established itself as maritime leader in port development, privatization and specialized cargo handling in India. It has conceived the Gujarat Maritime Cluster (GMC) as a dedicated ecosphere of Ports, Maritime / Shipping and Logistics services providers along with regulators, in GIFT City. GMB has also established the Gujarat Maritime University (GMU) in its endeavour to provide a fillip to this growth by bridging the knowledge gaps within the industry. IFSCA has signed a Memorandum of Understanding (MOU) with GMU to promote the Gujarat International Maritime Arbitration Centre (GIMAC), which is to be set up at GIFT House¹.

The synergies with the mandate of the Committee were assessed to be real.

Multiple consultations held with industry experts, segmented into three inter-twined tiers in the shipping ecosystem in India and abroad, complemented the abovesaid examination. Public and private sector, and allied classification societies, etc. were consulted. Interactions were thus held with ship-builders, maintenance, repair, and overhaul organisations, and ship recyclers/ breakers in the first part, ship financiers (bankers, non-bank financial institutions, alternate financiers, cash buyers) in the second part, and entities

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from the commercial trade segment comprising of ship owners, charterers, lessors, ship brokers, and industry associations in the third part.

Stakeholder were unanimous that India has to plan for an accelerated presence in global shipping markets with suitable foreign investments. Apart from acting as a hedge against large freight bills of India's mercantile trade, holding significant control in global maritime bankable assets can also offer the industry potentially higher returns on investments. Indian trade industry has to be equipped with the best tools available to manage and mitigate freight risks, while Indian capital has to be provided an opportunity to participate in this large and profitable global segment with added skills and dexterity. These interactions also reaffirmed that India-IFSC has certain inherent cost advantages for enterprise established therein and offers the right platform for developing a ship acquisition, financing and leasing ecosystem.

The interactions revealed a few competing claims of stakeholders in domestic jurisdiction. These will arise perforce whenever an India-offshore regime is created to help Indian entities compete with global marine hubs flush with global best practices. Such asks were put to the tests of balance of considerations and of developing avenues which strength and offer competitive advantage holistically to Indian enterprises participating in end-to-end value chains. Germane to the matter is that existing domestic industry stands to fully benefit from a host of new ship financing and leasing avenues sought to be developed from India-IFSC. Ship leasing and financing from IFSC will buttress the efforts being put in to build up the shipping sector in India.

The objective of the Committee has unambiguously remained enabling the seeding of a robust **Ship Acquisition, Financing And Leasing (SAFAL)** regime at India-IFSC. A crucial element is making it future-proof, so that it can steadily ride the tailwinds of innovations over time towards decarbonisation through "green financing", besides carrying a self-sustaining impetus in its engine-room for the medium to long terms.

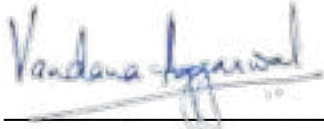
For this to happen, India must develop a world-class globally integrated ecosystem, where expertise and tools to fulfil the objectives are available. Presence of a vibrant ship finance regime with foreign participation will enable India to keep abreast of sector developments and access to global capital and talent. Understanding of complex global sea trade, its interplay with traders and end-users and ability to tap into the expertise of seasoned industry players will allow India's strategic planners to better appreciate the threats and opportunities that international shipping presents.

In conclusion, the Committee has thus developed a set of critical and necessary changes required to be made in the legal and regulatory framework, including in direct and indirect taxes and other duties, and in the export-import provisions relating to ships, ship finance and shipping services in India-IFSC.

The Report also provides policy makers with suitable inputs by way of detailed drafts of the proposed regulatory and legal changes. It draws out the way forward for realising the true transformational potential of India's shipping industry. This may also be an opportune time for the shipping ministry to brand the India flag appropriately. Adopting the theme of 'Greening the Blue Ocean' could fit well with the Maritime India Vision 2030.

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The Report is submitted herewith to the IFSCA.



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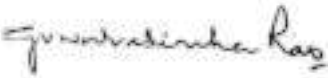
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Note: Members have served on this Committee ad personam. Comments, views, analysis and/or examination herein are neither attributable to, nor are the recommendations binding upon, the organisations to which the Members belong.

Dated: 28-10-2021



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The Committee would like to convey its deep gratitude to all the stakeholders and industry experts, most of whom are recalled in Annex 3 hereto, for appreciating our need for speed and rallying with us in providing written inputs, supplemented with discussions and clarifications at very short notice.

No words can do justice to the multifaceted support provided by Himanshu Jain and K. Kundan Krishna from the IFSC Authority to the Committee right from its constitution to until the submission of this Report.

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ABBREVIATIONS AND ACRONYMS

AIF	Alternative Investment Funds
BR Act	Banking Regulation Act, 1949
BCD	Basic Customs Duty
CAGR	Compound Annual Growth Rate
Central Government	Government of India, acting through the relevant ministry or administrative wing
CGST	Central Goods and Services Tax
Companies Act	Companies Act, 2013
CST	Central Sales Tax
DDT	Dividend Distribution Tax
DMCC	Dubai Multi Commodities Centre
DTA	Domestic Tariff Area
DTAA	Double Taxation Avoidance Agreement
DWT	Dead Weight Tonnage
EDPMS	Export Data Processing and Monitoring System
FDI	Foreign Direct Investment
FEMA	Foreign Exchange Management Act, 1999
FEMA IFSC Regulations	Foreign Exchange Management (International Financial Services Centre) Regulations, 2015
GAAR	General Anti Avoidance Rules
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GIFT	Gujarat International Finance Tec-City
GIMAC	Gujarat International Maritime Arbitration Centre
GMB	Gujarat Maritime Board
GMU	Gujarat Maritime University
GSA	Gujarat Stamp Act, 1958
GRT	Gross Registered Tonnage
GST	Goods and Services Tax
HNIs	High Net Worth Individuals
IDPMS	Import Data Processing and Monitoring System
IFC	International Finance Centre
IFSC	International Financial Services Centre
IGST	Integrated Goods and Services Tax
IIO	International Financial Service Centre Insurance Offices
ILFC	International Lease Finance Corporation
INR	Indian Rupees
Insurance Act	Insurance Act, 1938
Insurance Regulations	IRDAI (Investment) Regulations, 2016
INVITs	Infrastructure Investment Trusts
IFSCA	International Financial Services Centres Authority

ABBREVIATIONS AND ACONYMNS

IRDAI	Insurance Regulatory & Development Authority of India
ISA	Indian Stamp Act, 1899
ITA	Income Tax Act, 1961
LIBOR	London Interbank Offered Rate
LLP	Limited Liability Partnership
MAT	Minimum Alternate Tax
Master Directions (Financial Services by Banks) Directions, 2016)	Master Directions - Reserve Bank of India (Financial Services provided by Banks)
MOF	Ministry of Finance
MRO	Maintenance, Repair and Overhaul
MSA	Merchant Shipping Act, 1958
MoU	Memorandum of Understanding
M/o	Ministry of
NAV	Net Asset Value
NBFC	Non-Banking Financial Company
NCLT	National Company Law Tribunal
NFE	Net Foreign Exchange
NIIF	National Infrastructure Investment Fund
NOC	No-Objection Certificate
NPS	National Pension Scheme
ODI	Overseas Direct Investment
OEM	Original Equipment Manufacturer
PFRDA	Pension Fund Regulatory and Development Authority
PSU	Public Sector Units
RBI	Reserve Bank of India (i.e. the central banking regulator in India)
RCS	Regional Connectivity Scheme
RFP	Request For Proposal
RoFR	Right of First Refusal
SARFAESI	Securitisation and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002
SEBI	Securities and Exchange Board of India (i.e. regulator for the securities market in India)
SEBI (AIF) Regulations	SEBI (Alternative Investment Funds) Regulations, 2012
SEBI (IFSC) Guidelines	SEBI (International Financial Services Centres) Guidelines, 2015
SEZ	Special Economic Zone
SEZ Act	Special Economic Zones Act, 2005
SGST	State Goods and Services Tax
SPC	Special Purpose Company
SPV	Special Purpose Vehicle
TEU	Twenty-Foot Equivalent Unit
T&C	Terms and Conditions
USD	United States Dollar
VAT	Value Added Tax
WHT	Withholding Tax

1. EXECUTIVE SUMMARY

Maritime transport is the backbone of international trade and the global economy. Around 80% of global trade in goods by volume and over 70% by its value is carried on ships across the seas and handled at ports worldwide. Concentration of capital, aided by liberal taxation and regulation, has created global shipping hubs specializing in various activities.

Shipping is essential to India. Nearly half of India's border is covered by sea, with a coastline of about 7,517 km, with 12 major and 205 minor ports. India is also strategically located on the world's shipping routes. Ministry of Shipping has estimated that about 95% of India's goods trade by volume and 70% by value is done through maritime transport. India has a significant exposure to maritime freight rate. Seaborne freight is estimated to be USD 85 billion annually. The share of Indian ships in carrying India's export-import cargo was about 6.53% in FY 2019-20. Each year India is estimated to pay about USD 75 billion seaborne freight to foreign shipping companies. India is thus well placed to step up its investment in the shipping industry.

The financial call for promoting ship acquisitions, financing and leasing from India is readily established. An estimated about USD 3 billion in debt financing for India owners is financed mostly by international financiers currently². About 61% of India's fleet holds a National India flag (15m out of 25m DWT). Based on the current global order book of scheduled commercial vessels, over 3,000 vessels are on order at a value of about USD 200 billion (fair market value)³. Yet, there is serious room for growth – China has 340m DWT tonnage or 16% global market share, while India has 25m DWT tonnage or 1% global market share.

Among the main other considerations to give a concerted push to the establishment of a domestic leasing industry on the pattern of what has been recently done successfully for aircraft – another large mobile bankable asset – is that ship industry holds the key to push the success of “Make in India” initiative, due to the high dependence on connectivity and supply chain, with high output and employment multipliers for the Indian economy. Furthermore, the market share in financing the industry stands presently captured by foreign lessors and financiers, and of late sizeably by Chinese leasing and financing companies. Ship lease finance is a highly profitable avenue, and shipping being a least-polluting form of commercial transport, is critical in the decarbonization efforts. An effective ship financing eco system with adequate risk capital can also be permitted to invest in tonnage in domestic tariff area, ensuring adequate funding for tonnage operating there.

Despite a clear-cut strategic and existential case for establishing and growing the business of shipping from India, many leading shipowners, and operators have chosen leading international maritime centres in India's vicinity, notably, Dubai DMCC, Hong Kong, and Singapore, as their base. These hubs attract companies by offering an integrated and holistic shipping services platform, covering maritime finance, technology, insurance, arbitration and dispute resolution, shipbroking, crew training, and ship management in their respective

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jurisdictions. Maritime cities are benchmarked on factors such as Shipping Centers, Maritime Finance, Maritime Law and Arbitration, Maritime Technology, Ports and Logistics.

Singapore is the top-ranking maritime capital of the world. Despite the “new normal” in traditional commercial shipping and economic stresses due to a still-weak offshore services’ market, Singapore has been able to evolve in order to retain its top-rank. All of its pillars supporting its Marine Centre are strong and resilient, enabling it to outperform other cities which are close competitors. In the Middle East, India and Africa region, Dubai is the leading maritime center and at a global level, now ranked ninth.²

Figure 1: The leading maritime capitals of the world, 2019

RANK	SHIPPING	FINANCE AND LAW	MARITIME TECHNOLOGY	PORTS AND LOGISTICS	ATTRACTIVENESS AND COMPETITIVENESS	OVERALL RANK
1	SINGAPORE	LONDON	OSLO	SINGAPORE	SINGAPORE	SINGAPORE
2	ATHENS	NEW YORK	LONDON	ROTTERDAM	COPENHAGEN	HAMBURG
3	HAMBURG	OSLO	HAMBURG	HONG KONG	LONDON	ROTTERDAM
4	HONG KONG	HONG KONG	BUSAN	SHANGHAI	ROTTERDAM	HONG KONG
5	SHANGHAI	SINGAPORE	TOKYO	HAMBURG	HAMBURG	LONDON

Source: Menon Economics and DNV GL publication

India lags far behind these global leaders in building a base for commercial enterprise. Costs of financing – borrowing and insurance (hull, cargo, and protection and indemnity, P&I) – are unfavourably high compared to international counterparts notably in London and Singapore which offer highly competitive rates. Financing and insuring ships is a specialised area; Indian agencies (banks, insurance companies, pension funds, alternate capital and others) lack exposure to maritime finance and insurance, and hence tend to be non-risk takers or impose lengthy, time-consuming procedures. Besides, India’s tax regimes by and large are not encouraging to shipping industry on par with the tax regimes of Singapore, Malta, Cyprus, and Panama where the majority of the international carriers are registered. The tax burden on seafarers sailing on foreign ships is nil as they are exempted from paying income tax, whereas their counterparts are obliged to pay all taxes. Similarly, the GST provisions on ship building, ship managing, bunkering, repairing (spare parts, for instance) etc. are skewed in favour of foreign entities, rendering Make-in-India unattractive.

Shipping as a global industry has cyclical ups and downs where the asset value gets linked to global charter hire rates. Indian entrepreneurs, in the context of other industries, have not considered investing in shipping sector as a safe haven. Hence India, which has a huge export-import trade, is a country of charterers and not shipowners thereby resulting in a substantial spend of around USD 75 billion annually for chartering foreign flag vessels for India’s international trade. It is heart-wrenching to find that on registering of ships, industry finds it easier and more expedient to resort to Flags of Convenience (Panama, Marshall Islands, Liberia etc.) rather than flagging in India. Through the avenues of development of leasing which is suggested here, it is proposed to impart brand value to India flagged vessels.

It is also felt that Indian-flag be made the flag of choice for vessels involved in international trade for India-IFSC vessels. This can be done by adopting the correct tonnage tax structure

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and giving options to the users without compromising on safety and security standards, while furthering employment of Indian seafarers. A strong, effective, proactive and responsive flag administration and proper ensuring of compliances of the provisions of Port State Controls and IMO's instruments is vital. The performance of regulatory functions/ oversight in an efficient and disciplined manner would ensure that Indian flag upgrades itself from its present position at 43 ("Grey List") to the "White List", and that the India Administration's Recognised Organisations (Indian Registry of Ships) also upgrades from "Medium-level" performance (rating and assessment in 2020) to the "High-Level". Without doubt, these measures will give a significant fillip to the Indian-Flag being the preferred flag for vessels plying in international trade, besides ensuring that exercise of this choice brings financial, fiscal and commercial benefits to the ship owner/ lessor in India-IFSC or to a Wholly-owned-Subsidiary with POEM established in India-IFSC by a foreign ship owner/lessor.

Another hindrance is the lack of monetary incentives provided to the Indian shipping industry. Countries such as South Korea, Norway and China have dedicated maritime fund structures to incentivise ship owners. While some countries facilitate foreign entities to purchase newly-built ships in local shipyards, others provide advice and structures to enable shipowners to finance capital for the purchase of new vessels. In India, shipbuilders are now incentivised since December 2015 by the Financial Assistance Policy for Indian Shipyards under the Sagarmala Project. It provides financial assistance to Indian Shipyards for shipbuilding contracts signed between 01 April 2016 to 31 March 2026. This incentive appears to be in tune with monetary structures adopted by countries across the globe.

Another impediment is the lack of domestic financial institutions specializing in ship finance which has meant a high rate of interest being offered to shipowners. While such interest rates may not be prohibitive to bigger shipowners such as Shipping Corporation of India, they tend to dissuade small shipowners. Additionally, smaller shipowners do not usually have access to foreign lender banks and if they do, they may also be met with extremely high interest rates. All this works towards dissuading Indian parties from entering into or continuing in the Indian shipping industry. It has been recommended herein that a part of the current tonnage in domestic tariff area can also be permitted to be set up in the India-IFSC regime, provided that such tonnage is primarily deployed on international trade routes and meets the set criteria for age and size and/or specialised vessels.

While India has a limited home-owned fleet, there are deep-rooted maritime traditions and thousands of Indian nationals represented at many of the top maritime players – shipping companies and financing institutions supporting the maritime cluster. Those who have set up owned fleets have established the owning companies in other jurisdictions as the tax, regulatory and legal regime covering the maritime market in India is deemed to be too expensive, with extensive bureaucratic red-tapes as compared to other countries. Despite obvious human resources strengths elsewhere, within India there are markedly inadequate commercial skills and understanding of shipping markets which restricts the ability of Indian shipping to go beyond low end back-office functions or highly labour-intensive tasks.

Among India's strengths are its established common law system, world-class ports, proximity to major sources of and markets for goods, and a young, well-educated, creative and motivated workforce. India has the potential to build a base for commercial principals. If more of these principals are attracted to India, related service providers will follow. Many

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tonnage providers around the world continue to search for an Asian base of operations. At the same time, many Chinese vessel leasing companies with all or part of their fleet based or registered outside China in low tax jurisdictions are looking to housing their offshore ownership operations in respectable jurisdictions with a stable tax and legal environment. All these activities present a real opportunity for India.

One step to attract maritime players to set up business in India is to make it easier for commercial principals to move their key employees to IFSC, to facilitate the interaction between various different government departments and regulators.

Traditional sources of capital from the shipping banks are shrinking, making their loans more expensive and harder to obtain, forcing many shipping companies to turn to alternative sources of finance. Export credit agencies (“ECAs”) in shipbuilding nations provide guarantees for facilities arranged by banks or direct lending. Some of these ECAs could be attracted to conduct their shipping business from IFSC or have ECA-related transactions arranged by banks based in IFSC. The Export Credit Guarantee Corporation of India (ECGC) could also design a scheme for securing monthly lease rental dues from lessees for IFSC-lessors, say for 90-days, and thereby add a new financing market altogether for ships built in India to start with.

Fostering the development of ship leasing, financing and owning in IFSC will also serve as foundation for unleashing the employment and output multipliers on the shipping industry and the Indian economy.

Thus, the time is ripe for India to seize the opportunities being created also by the global crisis to promote a shipping ecosystem that can create and sustain companies that are benchmarked against the best globally and be able to compete and profit by participating in the global maritime play. It is time to align India's shipping sector with global centres like Singapore, Hong Kong and Dubai and carve its place in global cross trades, besides leveraging and securing gainful transactions for its marketplace. It is proposed that the concept of IFSC, conceived for financial services, be naturally extended to ship acquisition, financing and leasing (SAFAL) products and services along the lines of the successful recent extension to aircraft acquisition, financing and leasing.

In conclusion, the Committee has carried out a 360-degree review and examination of the extant regulatory framework affecting such activities. It also drew upon industry insights revealed through multiple consultations with a wide spectrum of stakeholders. It has, thus, worked out avenues for seeding ship acquisitions, financing and leasing in the IFSC in India. The critical and necessary legal and regulatory changes and solutions recommended herein have been presented both in short-form analysis of the problem and justification for change as well as in detailed long form analysis which also contains the draft texts of solutions, for the consideration of the competent authority concerned. A bird's eye view of the principal recommendations is provided below:

Authority	Change w.r.t.	Recommendations
IFSCA	Financial Product definition	Notify vessel-leasing activity as ‘financial product’ to enable ship leasing entity to set up unit in IFSC

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Authority	Change w.r.t.	Recommendations
		Alternatively, notify ‘operating lease of any equipment’ as financial product. IFSCA may enable industry-wise operating lease through an appropriate framework
IFSCA	Operating Framework	- Develop framework for vessel-operating lease - Amend ‘Framework for enabling Ancillary Services at IFSC’ to include certain ancillary services relating to vessel financing and leasing
IFSCA	IFSC Exchanges	- Dedicated platform for Shipping on IFSC Exchanges - Bunker derivatives to be offered to manage volatility in Bunker and Freight prices - Provide special regime for INViTs set up in IFSC including trading of such INViTs on IFSC exchanges
DG Shipping	Registration of vessels	- Steps may be taken to make ship registration (including registration of companies/ entities) efficient. - Permit registration of current tonnage in domestic tariff area to be set up in India-IFSC regime, provided that it is primarily deployed on international trade routes and meets the set criteria for age, size, vessel type
DG Shipping	Flagging	Introduce a new category titled ‘Indian IFSC controlled tonnage’, offering certain relaxations
DG Shipping	Licensing	Modify ROFR notification for vessel-chartering by PSUs for bulk imports to include provisions for IFSC vessels
DG Shipping	Import of bulk cargo	- Replace the requirement of sequential waiver by two Ministries by a confirmation of competitiveness of freight terms offered by seller by freight/operational desk of PSU set up in IFSC - Permit PSUs to shift chartering activity to a ‘freight desk’ office at GIFT City
IFSCA	Debt and Statutory Dues Monitoring	Introduce an online monitoring platform by IFSCA for promoting timely fiscal and financial payments and thereby preventing ship repossession / attachments by priority interest holder/ mortgagor under defaults on dues by debtor/lessee
DG Shipping, M/o Shipping	Statutory Mortgages	Provide for enforcement of mortgages by a special commercial court
DG Shipping, M/o Shipping	Dispute resolution	Some legislative changes for speedy resolutions of disputes related to maritime claims and matters
Government of Gujarat	Stamp Duty	Exempt stamp duty for instruments relating to ship acquisition, financing and leasing in IFSC
IRDAI	Insurance Act, 1938	- Exempt insurance companies in IFSC from investment restriction provisions - Remove restriction on investment of funds abroad
IRDAI	IRDAI Investment Regulations, 2016	Enable investment by insurers in equity and listed debt securities and permit investment in unlisted debt securities of private companies undertaking vessel leasing
IRDAI	Insurance IIO Guidelines	Permit insurance companies in IFSC to invest in entities engaged in vessel financing/leasing in an IFSC

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Authority	Change w.r.t.	Recommendations
M/o Commerce	SEZ laws	- Exempt ship leasing and related business in IFSC from Net Foreign Exchange Earning requirement as ship leasing business cannot be NFE earner in 5-years period - Exempt ship leasing and related business from bringing in goods physically into SEZ as GIFT City does not have seaports, and notify ports as SEZ for IFSC vessels - Exempt IFSC units from requirement of having separate office for each unit, for cost-effectiveness for such entities - Develop revised application form for ship leasing IFSC entities; consider issuing separate guidelines to enable such business in IFSC - Develop a mechanism similar to EDPMS/IDPMS system to monitor inflows/outflow of foreign currency by IFSC Unit to control influx of ‘dirty money’ - Revise formats of reporting, Bond, etc. to enable EODB for IFSC business, and its due monitoring
M/o Finance, CBIC	Goods and Service Tax	- Nil rate services of ocean freight provided by IFSC unit to a foreign consignor for transportation of goods in vessel from outside India to India - Exempt services of ocean freight provided by IFSC unit to a foreign consignor (on export freight services) - Nil rate ocean freight and Inland Haulage charges and other ancillary services in relation to transportation of goods in vessel for shipments from one country to another (both outside India) to Indian customers - Provide clarification on registrations at various ports - Nil rate IGST on import of vessels by Indian ship owners - Shift liability of GST under RCM on charter hire services by ship owners in IFSC to ship operators in India - Nil rate GST on bunker fuel imported with the vessel
M/o Finance, CBDT	Income tax	- Exempt from tax any income of a non-resident by way of royalty or hire charges of vessel lease by IFSC unit - Exempt withholding tax requirement on freight paid by Indian charterer to IFSC vessel leasing and owning unit - Exempt tax on capital gains arising on transfer/sale of vessel or transfer/sale of partnership interest/shares of SPV holding the vessel - Exempt tax on dividends paid by IFSC unit in the hands of non-resident shareholder
NIIF, D/o Economic Affairs	Strategic Fund	- Create a Strategic Transport Infrastructure Fund – greenfield funding in IFSC - TOR of this fund could promote decarbonising the shipping sector by funding new technology vessels and other green infrastructure initiatives
RBI	ECB Master Directions	- Ease restrictions and enable ECBs for vessel financing and ship chartering - Permit offshore branches of Indian banks to refinance domestic debt through ECBs

EXECUTIVE SUMMARY

Authority	Change w.r.t.	Recommendations
RBI	FEMA (TIFS) Regulations	Permit investments by mutual funds in unlisted equity/ equity linked instruments and foreign debt instruments issued by IFSC units engaged in vessel leasing
M/o Finance, RBI	BR Act	Allow banks to hold more than 30% shares in a company
M/o Finance, RBI	BR Act	Grant 'infrastructure' status to vessels
RBI, IFSCA	FEMA NBFC Regulations	- Permit NBFCs to set up a branch office in IFSC. - ODI investment by NBFC to be under automatic route.
SEBI, RBI	SEBI (IFSC) Guidelines	Provide clarification on categories of investors that can invest in AIF operating out of IFSC
SEBI, RBI	FEM (TIFS) Regulations	- Clarify the position on investment by AIFs in IFSC whether such investment is domestic or offshore - Provide relaxation on overall cap of USD 1,500mn or specify non-applicability of overall cap for AIFs targeting investment in IFSC unit for vessel financing and leasing - Amend regulations to permit investment by AIFs in debt instruments issued by ship leasing/ financing IFSC unit
SEBI, RBI	FEM (TIFS) Regulations, SEBI (IFSC) Guidelines	- Provide clarification on types of institutional investors covered under SEBI IFSC Guidelines. - Provide additional relaxation under LRS for Indian residents to invest in mutual funds operating in IFSC.
SEBI	SEBI (FPI) Regulations	Remove restrictions on FPIs investing in Category-I and II AIFs
SEBI	SEBI (Mutual Funds) Regulations, 1996	- Amend regulations to create a separate category of mutual funds for investments in ship leasing IFSC units or permit greater concentration of investments in IFSC units engaged in ship financing/ leasing - Provide relaxation under LRS for Indian residents to invest in mutual funds operating in an IFSC
PFRDA	PFRDA Act	- Clarify that pension funds are permitted to invest in domestic AIFs, even if they may use funds for investments in ship financing/ leasing IFSC units, or that investment in IFSC units would not be considered as overseas investment by pension funds - Issue a clarification that entities owning vessels or engaged in ship financing are 'infrastructure entities' - Amend investment guidelines to allow pension funds to invest in equity or debt instruments of IFSC units
M/o Labour & Employment	EPFO Act	Issue a notification to permit investment in AIFs and IFSC units engaged in ship financing/ leasing
ECGC	New Scheme	Design a scheme for securing monthly lease rental dues from lessees for IFSC-lessors, say for 90-days

MARITIME TRANSPORT SERVICES AND INFRASTRUCTURE SUPPLY

In early 2020,
the world fleet totalled
98,140 ships
of 100 gross tons and above
2,061,944 thousand dwt
of capacity

Ship types representing
largest proportion of global
fleet value



FREIGHT RATES



Container ships

Blank sailing and other capacity-management measures applied to adapt supply capacity to reduced demand for seaborne trade and allow freight rates to remain strong

- Third quarter of 2020: capacity-reduction measures pursued in container shipping, although demand picking up, keeping freight rates on the rise.
- Sustaining these measures for a long period during recovery may lead to dysfunctions in the sector, undermining performance of shippers and global supply chains.



Tankers

Lockdown repercussions, geopolitical events, oil price fluctuations and increased use of vessels for floating storage --> higher freight rates (March–April 2020)



Dry bulk carriers

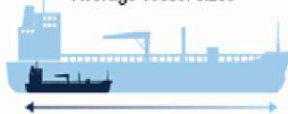
Oversupplied market and shock of negative demand from China, owing to the outbreak of the pandemic, pulled down dry bulk freight rates

FLEET CHARACTERISTICS

Average fleet age



Average vessel sizes



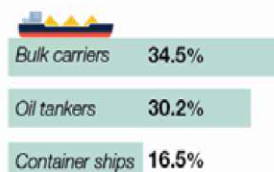
Ships built 20 years ago Ships built in the last 4 years

Oil tankers **9 times bigger**
Container ships **4 times bigger**
General cargo ships **3 times bigger**
Bulk carriers **twice as big**

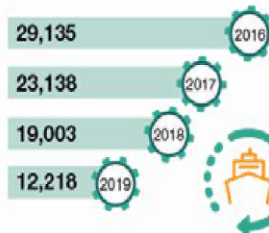
FLEET GROWTH

Newbuildings

65,911,000 gross tons delivered in 2019
of which:



Decreasing global volumes of
ship recycling tonnage
(thousand gross tons)



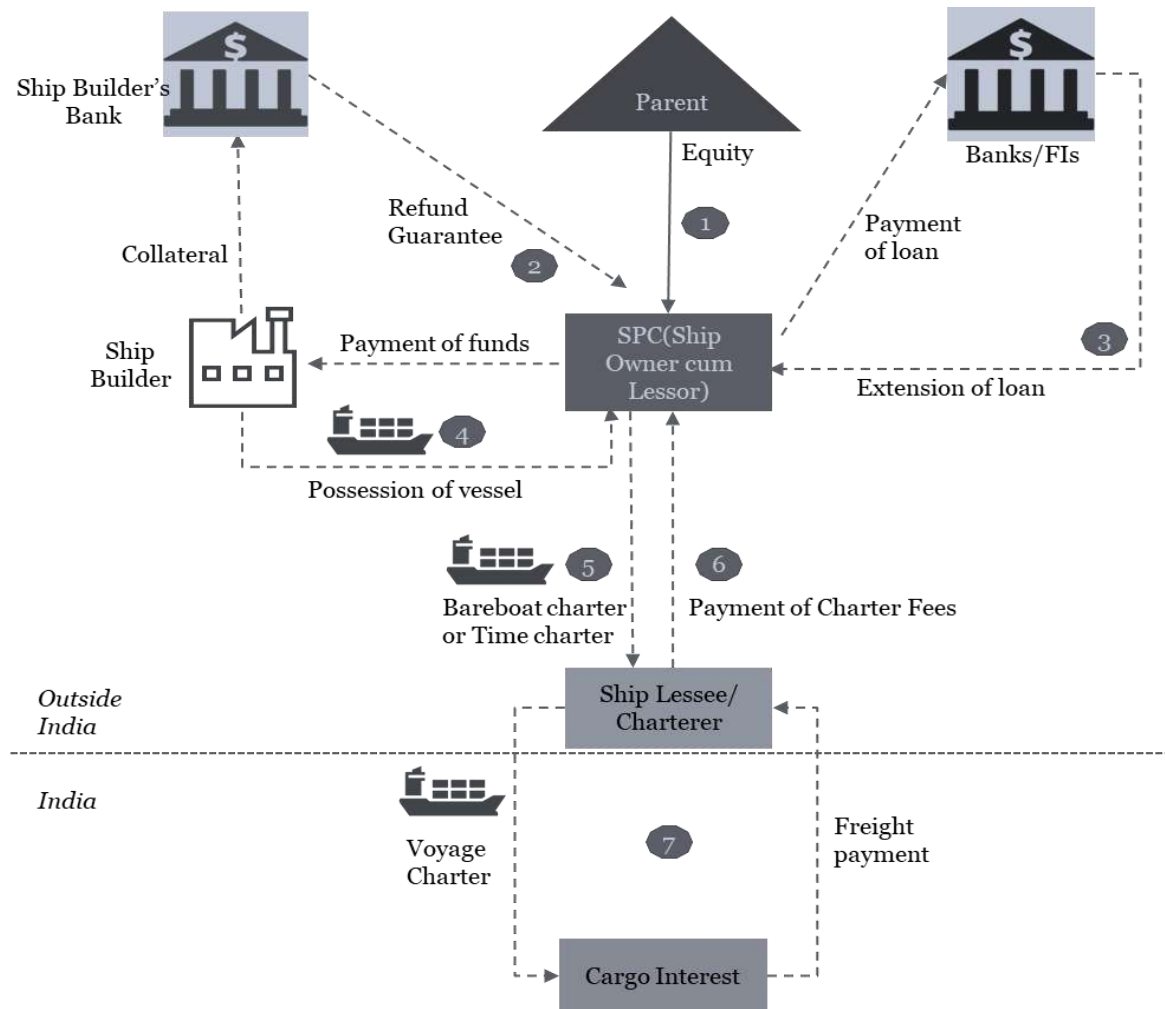
- COVID-19 crisis: container shipping industry sustained earnings as carriers applied discipline and strict capacity management

- 2008–2009 crisis: freight rates reached dramatic lows, as carriers sought to gain greater market shares through scale and capacity expansion, leading to great losses in container shipping trade

Source of Snapshot: UNCTAD Review of Maritime Transport, 2020

2. SHIP OWNING, FINANCING, OPERATING STRUCTURES

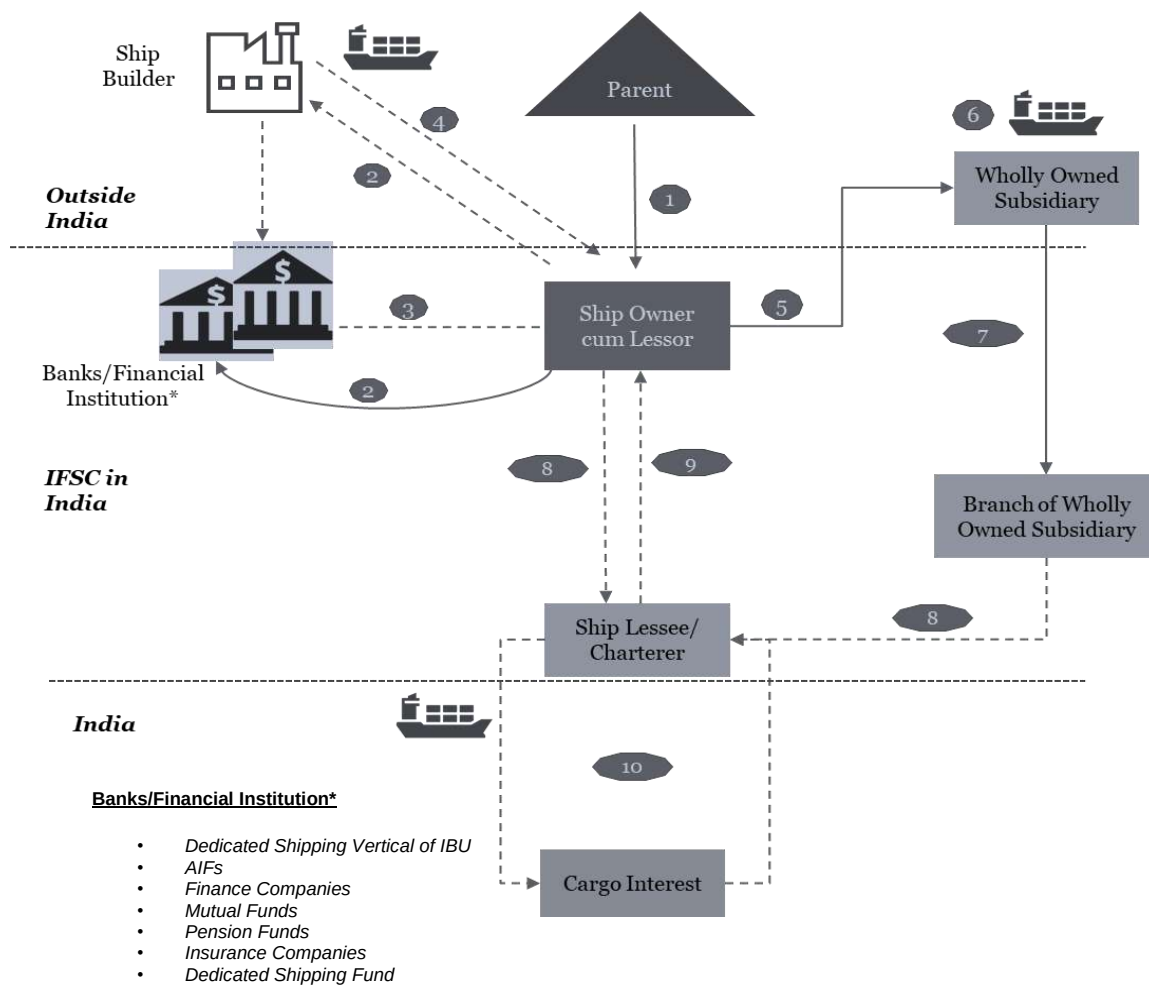
2.1. Typical Ship Owning and Leasing Structure



Key Mechanics:

1. Parent company sets up a SPC – ship owning-cum-leasing entity.
2. Parent company negotiates the terms and conditions with ship builder and SPC obtains guarantee from ship builder's bank.
3. Ship owner borrows funds from bank/financiers for purchase of vessel and completes necessary documentation.
4. SPC takes possession of vessel on payment to ship builder.
5. Ship lessee charts vessel on bareboat/time charter basis from SPC.
6. Ship lessee pays charter fees in return for bareboat/time charter.
7. Ship lessee operates the vessel on voyage charter basis in lieu of freight payments.

2.2. Typical Ship Owning and Leasing Structure – IFSC Model



Key Mechanics:

1. Ship Owning entity will be set up in IFSC by an overseas parent.
2. Parent company negotiates T&C with Ship Builder and Ship Owner obtains guarantee from Ship Builder's bank. Ship Builder's bank can be in IFSC.
3. Ship Owner borrows funds from its bank/financiers for purchase of vessel and completes necessary documentation.
4. SPV takes possession of vessel on payment to Ship Builder.
5. IFSC Ship Owning entity to prefer Indian-Flag, but otherwise be freely permitted to opt for foreign flag of a Flag State subject to certain conditions. 'Infrastructure status' to be granted for vessels owned and financed by or operated by IFSC shipping entities and India-Flagged.
6. In case preference for Indian-Flag is not exercised, Ship Owning entity will set up a wholly owned overseas subsidiary in foreign jurisdiction, e.g. Panama. Overseas subsidiary in Panama to own ship with Panama flag.
7. Foreign company which is a subsidiary of an IFSC unit will be set up a branch in IFSC as a IFSC unit. Place of effective management (POEM) of foreign company will be in IFSC.
8. Ship Lessee charts vessel on bareboat/time charter basis from Ship Owner in IFSC or Wholly Owned Subsidiary in Panama as the case may be.
9. Ship Lessee in IFSC pays charter fees in return for the bareboat/time charter.
10. Ship Lessee operates the ship on voyage charter basis in lieu of freight payments.

2.3. Transaction Structures

A suite of potential ship financing options for different needs

Structure	Senior Debt			Bond Financing	Leasing Structures		
Options	<u>Option 1</u> Pre-delivery Bridging Loan	<u>Option 2</u> Post-delivery Commercial Loan	<u>Option 3</u> Export Credit Agency (ECA) Backed Loan	<u>Option 4</u> Project Bond	<u>Option 5</u> Sale & Lease-back / Finance Lease	<u>Option 6</u> Japanese Operating Lease with Call Option (JOLCO)	<u>Option 7</u> Chinese Leasing Company (CLC)
Financing Amount (% Loan-to-Value)	Upto [70]%		Upto [80]%	[70%] with debt sized benchmarked on contracted cash flows	[85-90%]		
Tenor (years)	Less than [3] years	[7 to 12] years	Upto [14] years	Upto [14] years	Upto [12] years Tend to be longer than unsecured commercial loan		
Considerations	Suitable to part finance pre-delivery milestones	Pricing and tenor would be relatively expensive and shorter, given no ship security Execution will be much faster	ECAs typically need 3-6 months of lead time for approvals Dependent on the shipyard location or country where equipment or services are sourced	More flexible compared to standard senior debt financing as it would typically have less restrictive incurrence covenants compared to maintenance covenants on senior debt Will require external rating	Pricing is much more competitive; tenor and financing quantum can be stretched given there is a ship security Execution can take longer given the involvement of the third party Purchase option is expected to be exercised Strong preference for vessels to be registered under the flag of convenience (for ex. Singapore/ Hongkong) Only a few CLCs have an appetite for tankers (especially VLCCs)		

• **Senior Debt Structures**

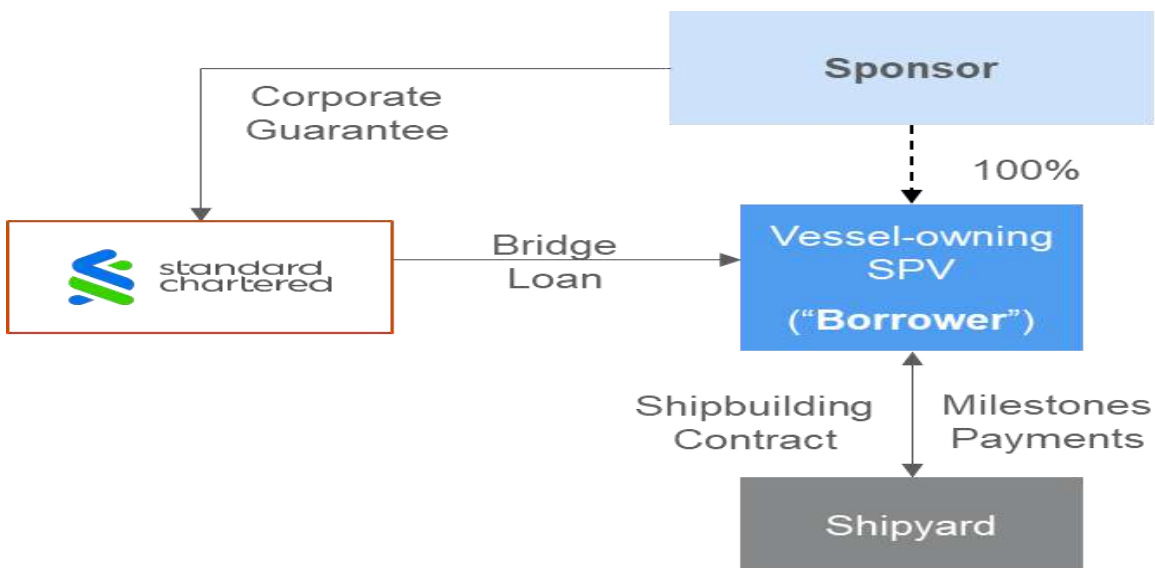
Option 1: Pre-delivery Bridging Loan

Key Considerations

- 1 In case additional time is required to secure the desired financing structure, a short-term bridge could be considered to finance the upcoming milestones payments
- 2 Bridge financing can be executed very swiftly as opposed to a pre-and-post delivery financing

Indicative Terms & Structures

Borrower	Special purpose company (" SPV "), Vessel-owning entity, wholly-owned subsidiary of Sponsor
Lender	Standard Chartered Bank
Facility	USD-denominated Term Loan Facility to finance vessels' acquisitions or milestones payments to Shipyard
LTV	Up to [70]%
Tenor	Less than [3] years
Availability Period	From the date when all conditions precedent have been satisfied up to the date falling [3] months prior to final maturity date
Drawdown	Multiple drawdowns during Availability Period in accordance with pre-delivery instalment payments to Shipyard
Repayment	Bullet repayment upon drawdown of post-delivery financing
Other Terms and Conditions	• Corporate Guarantee from Sponsor • Negative Pledge over Borrower's Assets • Sponsor to retain majority ownership and control over Borrower • Subordination of shareholders' loan • Covenants to be agreed



Option 2: Post-delivery Commercial Loan (Full/Limited Recourse)**Key Considerations**

- 1 Full control over the use and ownership of the Vessels and minimum/no difference in the balance sheet treatment in comparison to finance lease
- 2 Relatively fast execution on the back of no third-party involvement and more straight forward risk assessment/ due diligence/ simpler documentation

Indicative Terms & Structures

Borrower	Special purpose company (" SPV "), Vessel-owning entity, wholly-owned subsidiary of Sponsor
Lenders	Standard Chartered Bank and other financial institutions acceptable to Borrower
Facility	USD-denominated Senior Secured Term Loan Facility to finance vessels' acquisitions or milestones payments to Shipyard
LTV	Up to [70]% of Vessel(s) aggregate CMV
Tenor	[7 to 12] years
Repayment	Amortising Repayments
Security Package	Including but not limited to: (i) Mortgage over Vessels, (ii) Charge over project accounts (earnings account and debt service reserve account), (iii) Pledge over Borrower's shares, (iv) Manager's undertaking, (v) Assignment over Charter Agreements. (vi) Assignment over Vessels' earnings, insurance and requisition compensation
Other Terms and Conditions	• Sponsor to retain majority ownership and control over Borrower • Subordination of shareholders' loan • Covenants to be agreed

