

KEEPING AN EYE ON YOUR MARINE ASSET

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As a lender how would you feel about collateral if the asset operated in a hostile environment that involved day to day risk and month to month deterioration, whose location in the world might not be known from month to month and which was operated around the clock by a poorly paid, poorly trained team whose only common language was a few English phrases? Probably the same as you would feel about obtaining a “genuine” copy of the map to the Lost Dutchman goldmine being sold on a Tijuana street corner. These asset operating conditions might describe a tramp freighter operating under a third world flag of convenience. Although this is an extreme example, marine assets operate under difficult and often hostile conditions. After receiving an appraisal on a marine asset, how do you know what your collateral will look like in two years, five years or whatever the term of the deal?

The simple answer is that you need to know the policies and track record of the operating company or to structure the deal so that there are periodic spot checks of the vessel or vessels to monitor their condition. This is often done by the original appraiser who is already familiar with the equipment. However, there are many types of vessels where maintenance oversight is mandatory for reasons of public interest or for mandatory and/or voluntary insurance reasons. Unfortunately, as you might expect with an international business, the oversight rules vary from country to country in structure, in the type vessels included and excluded, and in the level of enforcement. Although what follows are generalizations, they will at least make some names and policies familiar to you.

Most ocean going ships involved in international trade are periodically inspected for compliance with many regulations promulgated by the International Maritime Organization (IMO). The IMO is a United Nations type organization in that the membership of a maritime nation is voluntary and the regulations are formed by committees and ratification votes. The current IMP catalogue of its regulatory codes and aids to carrying out code compliance is over fifty-five pages long. Actual vessel inspections are carried out by classification societies and port state authorities.

CLASSIFICATION SOCIETIES

Classification societies are private groups that “class” vessels by having them designed, built, and maintained to certain proven engineering and performance levels. If they are built and maintained to specifications, as documented by periodic scheduled inspections, they maintain compliance certificates for the inspected portions/systems. The presence of these certificates figure strongly in reducing the level of insurance premiums. These classification groups enforce many of the IMO regulations along with their own developed parameters. The largest and best known of these groups are Lloyds Register (LR), the American Bureau of Shipping (ABS), Det Norske Veritas (DNV), Bureau Veritas (BV), Germanischer Lloyd (GL), and there are many others. Their names may note their country of origin and main office location but they contract with ships of all nationalities and ships may change from one registry to another as long as they are in compliance with the covering regulations. Unfortunately, some changes involve aging vessels moving from a society with stringent regulations and enforcement to one where the

vessel may receive more lenient treatment. So, even though a vessel has classification certificates, all do not carry the same inspection weight. The good news is that due to the economic pressures of liability suits and oil pollution claims, all societies are becoming more stringent and uniform in enforcing their regulations. Some societies are being “black listed” by the societies umbrella organization and, because of economic conditions, there are mergers afoot.

PORT STATE AUTHORITIES

Port State Authorities (PSA) are like the Marine Inspection wing of the United States Coast Guard. They are all governmental bodies with authority only in their own countries ports. However, since they are protecting the port area and coastline from damage, they have authority over any ships that enter their ports. Unlike Classification Societies, Port State Authorities mainly confine their oversight to safety and oil pollution risks. Even though they don't do in depth inspections of a vessels structural and mechanical condition they do evaluate on board documentation and operational procedures and the availability and condition of safety equipment. The IMO has developed a uniform set of guidelines to be used to bring some consistency to PSA inspections worldwide.

When violations are noted they result in fines with the fines often being mitigated if the discrepancies are rectified immediately. As vessels are required to post bond to cover the full amount of the originally levied fines and, if the discrepancies may cause immediate risk to life and property, be denied permission to leave port until repairs are made or replacement equipment installed. This can be an expensive process and therefore encourage an owner to maintain his vessel to at least a minimum level. A side result of a PSA fine is that it may trigger an unscheduled visit by a Class surveyor and an in depth inspection that may provide more grief for an owner.

For United States flagged vessels the PSA, the United States Coast Guard, is mandated to do in depth inspections of certain types of vessels, mainly those that carry passengers for hire or dangerous cargoes. These vessels are called Inspected Vessels. In the US the determination of what is or is not an inspected vessel is complicated as shown in the accompanying table 24.05-1 (a), taken from the Code of Federal Regulations. The scope of the USCG oversight is often as deep and involved as that of a classification society and in the US you may have both the USCG and a class surveyor looking at the same things. In some cases the USCG subcontracts ABS to perform some of their mandated work. The most well known of these are the ABS inspections for vessel compliance with Federal Load Line (Plimsoll Mark) regulations.

The biggest problem with port state inspectors, including the U. S. Coast Guard, is that they are funded by the government and funding rarely meets need. A recommended target is inspection of approximately 25% of the vessels that arrive in a major port. In northern Europe where government funding is a problem, it was reported that only 6% of the vessels arriving at the major port of Antwerp, Belgium, during the first half of 1996, were inspected.

If you want to take the most conservative route on a vessel loan first get to know the owner. Know if he would be operating the vessel or would be chartering the vessel out to another operator or handing it off to a management company. If there was another party involved you need to know a little about the charter or management agreement to see how the costs of maintenance and crewing are handled so that you might have a feel for how the asset will be cared for when out of sight. This homework won't guarantee anything but it may keep you out of a disaster.

It is preferable to deal on an American flag Inspected Vessel that is fully classed (hull and machinery) with one of the major classification societies. At the other end of the spectrum would be a generally elderly vessel flying a flag of convenience from one of the countries that is on the Coast Guards' or other PSAs' "watch list". This list ranks the countries whose vessels are at or near the top of a list indicating the percentage of vessels that fail port arrival inspections. However, there are many ships from St. Vincent and the Grenadines or Russia that are in acceptable shape while a U. S., Canadian or Norwegian ship may occasionally be found in violation of regulations. All you can do is play the odds so that the largest number and/or the strictest group of third party inspectors are looking out, however indirectly, for your interest.

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