

## Offshore Energy Law

# LNG Long-term charters: What next?

Under the new rules, charterers will be required to treat all time charters for a period exceeding one year in the same way as a lease of an identified asset. A charterer cannot avoid that obligation by drafting a time charter to look less like a lease; it would be necessary for the alternative form of charter to sever entirely the link between the transportation service to be performed and the charterer's right to use an identified vessel.

Any alternative form of charter must allow the shipowner the unfettered option to nominate the performing vessel for each voyage throughout the charter period.

The reality may be that the owner chooses to nominate the same vessel for a number of consecutive voyages, but the owner would have the right at all times to nominate alternative vessels, provided of course they meet the contractual description and performance requirements. Thus, the operation of the long-term charter would resemble more closely a contract of affreightment.

COAs are rarely used for LNG transportation because under a COA, cargo is conventionally carried on voyage charter terms, whereas LNG is, conventionally, carried on time charter terms.

As Max Lemanski explained in his article 'Issues arising in relation to LNG COAs,' in Well Heeled Ed 1, the advent of BIMCO and GIIGNL-approved voyage charters provide an opportunity for LNG to be carried on COA terms. This presents a suitable alternative for a charterer who does not wish to enter into a time charter which must be treated as a lease.

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However, this option may not necessarily suit those charterers who have always used time charters. Such charterers who have no experience of voyage charters may be reluctant to switch to a COA and would prefer an amended time charter form.

The question which then arises is whether the necessary changes to a standard time charter to avoid it being treated as a lease, would fundamentally alter the usual balance of commercial risk between owner and charterer?

At first sight, it appears that the answer is yes. If the owner has the unfettered right to nominate a vessel for each voyage, there may be periods during which the charterer is obliged to pay continuous daily hire, as with conventional terms, even though there is no performing vessel.

For example, whilst a vessel is carrying cargo, the charterer gives orders for loading a subsequent cargo, calculated by reference to the time needed for the current vessel to discharge cargo and proceed to the next load port. If the discharge port is in the UK, and the next load port in the US, the anticipated return ballast voyage would be of a considerable period.

If the owner has a vessel positioned closer to the load port, it may choose to nominate that vessel, and allow the current vessel to proceed elsewhere. Provided the alternative vessel is available by the time that the first vessel would have been available, there is no event of off hire, and the charterer pays continuous daily hire for the full period of a transatlantic voyage, even though the ballast voyage for the actual performing vessel is far shorter.

In such event, the charterer may be surprised to be paying hire for periods when no service is being provided, but, of course, in this scenario, the charterer is paying the same hire for the same service as it would have paid under conventional time charter terms.

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Although this hybrid form of charter would be suitable to allow LNG to continue to be carried on time charter terms, the obvious difficulty may be that an owner of LNG vessels would not have a sufficient number of vessels available at any time to make an effective substitution.

If, as a consequence, the same vessel performs throughout the charter period, the charter takes the form of a lease. This creates a conundrum. If a time charter is treated as a lease because its performance is by one nominated vessel only, would this difficulty be overcome by adopting a COA model?

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If the owner does not have available vessels to provide substitution under a time charter form, it is likely the same vessel would in fact carry cargoes throughout the COA period, effectively as a form of consecutive voyage charter of a particular asset. Thus the new accounting rules would treat this as a lease.

As the clock ticks towards 2019, it is difficult to say with certainty the route that charterers may follow. One key feature is emerging. If an owner has sufficient vessels available to perform charters on COA or similar voyage-nomination terms, the new rules may not apply.

However, if in reality, the charter will be performed by the same vessel throughout the charter period, the terms on which that vessel is chartered have no material effect on whether the charter is treated as a lease.



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