MORTGAGE RIGHTS INSURANCE

Mortgage rights insurance (MRI) provides financiers with political risk insurance, and is designed to protect them in the event they are unable to enforce a foreclosure. Such a scenario can result from the local legal jurisdiction preventing financiers from enforcing their legal title and right to repossess or repatriate the collateral asset.

MRI is particularly beneficial for static/stationary assets such as floating storage and regasification units (FSRUs), floating production, storage and offloading vessels (FPSOs), floating storage and offloading vessels (FSOs) and drilling units, which by the nature of the asset (or the contracts they enter into) are based in one legal jurisdiction for a protracted period of time. However, any asset that is to be based predominantly in one jurisdiction for the duration of a charter can be insured (for example, a tanker shipping oil from Venezuela on a "shuttle run"). The need for MRI is governed by many factors, not least of which is the risk appetite of the financiers, which is especially relevant when a collateral asset is to be based in a nation where political, economic, or jurisdictional uncertainties are perceived to exist, or where there is an existing sovereign debt exposure. In such situations, the terms of the loan and mortgage or any lease/bareboat charter agreement are often ignored by the local courts. An MRI policy can be arranged for much longer periods than is customary, and often matches the contract period for the collateral asset, with three to five years being fairly typical.

WHAT DOES AN MRI POLICY COVER?

An MRI policy responds following any one, or more, of a number of perils, including:

- Nationalisation, confiscation, seizure, detention, etc. by the foreign government or a body with governmental authority.
- Refusal or failure of the foreign government to allow the financier to exercise its rights to repossess the asset.
- Refusal or failure of the foreign government to allow the financiers to remove the asset from the foreign country.
- Refusal or failure of the foreign government or flag state to de-register the vessel.
- Preventing the financiers from receiving the proceeds of sale following a seizure of the asset (including scenarios where the financiers have the "benefit" of the proceeds but are prevented from converting/exporting such proceeds).
- Inability of the financiers to recover the asset due to UN/US/EU/UK/etc. sanctions.

In addition:

- Unlike mortgagees interest insurance (MII) and mortgagees additional perils (pollution) insurance (MAPPI), any proceeds paid under an MRI policy can usually be used to discharge the debt, especially if the borrower was not materially to blame for the loss of the asset.

- An MRI policy cannot be voided by action or inaction on the part of the borrower/mortgagor.
- The inability to repossess/enforce mortgage rights is specifically covered.

HOW MUCH DOES AN MRI POLICY PAY?

MRI pays the lesser of:

- The amount lost by the financiers.
- The MRI policy sum insured.

WHY INSURE MORE THAN 100% OF THE OUTSTANDING LOAN?

The seizure of a collateral asset by a foreign government is often accompanied by a default in debt servicing by the borrower, who may well be owed charter payments, etc.themselves. In addition, the loan will incur certain additional expenses, for example, default interest and additional costs incurred in managing a loan in default. These additional amounts can be included as part of the sum insured, typically up to 120% of the outstanding loan is insured under an MRI policy (note that the additional amount in excess of the loan amount must be substantiated).

WHAT IS NOT COVERED UNDER AN MRI POLICY?

- It is not credit risk insurance and will not cover default by the borrower/mortgagor without an intervening insured peril having occurred.
- It does not respond if a vessel/asset is arrested by a third party with a valid claim (for example, cargo interests, another vessel following a collision etc.).
- It does not cover physical damage to the asset (other than wilful damage by the foreign government).

WHY CAN'T FINANCIERS RELY UPON THE BORROWER'S/MORTGAGOR'S WAR RISKS INSURANCE?

The main reasons a financier should not rely upon a standard war risks policy arranged by the borrower are:

- War risks policies can be cancelled by underwriters giving seven days' notice should the political situation deteriorate.
- While a borrower's policy may respond to an overt, or hostile, act of confiscation by a foreign government which undertakes a widespread seizure of assets, an isolated seizure is likely to be resisted by war underwriters on the grounds the proximate cause is a contractual dispute and/or infringement of a local law/regulation.
- Confiscation or requisition by the country of registration is a standard exclusion under war policies.
- Exclusions contained in a war policy would not cover any attempted repossession of an asset following default under the loan.

HOW DIFFICULT IS IT TO ARRANGE AN MRI POLICY?

Arranging an MRI policy is a little more involved than arranging an MII policy. Underwriters will require a written legal opinion from lawyers competent to detail the regulations in force at inception of the policy that address the mortgagee's rights within the foreign country. This will include confirming that the financier's interests as mortgagee have been correctly registered as well as commenting upon the enforceability of the relevant provisions within the loan and mortgage agreements.

CAN AN MRI CLAIM BE SUBMITTED EVEN IF THE BANK HAS ADDITIONAL SECURITY?

Yes. An MRI policy is not subservient to any other collateral or guarantees the financiers may have.

WHY NOT ALLOW THE OWNER TO ARRANGE A POLITICAL RISK POLICY ON BEHALF OF BOTH BORROWER AND FINANCIERS?

An owner-arranged political risk policy will not fully protect the financiers for a number of reasons. Further details can be provided upon request.

WHY DO MRI PREMIUM RATES VARY SO MUCH?

Unlike many other types of insurances, MRI policies are arranged on an individual basis as there are very few common factors between risks. The premium charged will depend upon a number of factors, including:

- The current assessment of the political and economic stability of the country in question.
- The applicable laws that will govern any dispute or enforcement action, and the perceived impartiality of the governing judicial system.
- The type of asset.
- The trading area (a vessel that will be limited to inland or coastal waters will be harder to repossess than a vessel that will periodically sail to other jurisdictions).
- The credit rating and international standing of the operator.
- The appetite underwriters have for the country in question (which will be influenced by the risk exposure they have already underwritten).

CAN AN MRI POLICY BE ARRANGED FOR THE BENEFIT OF A LESSEE?

Yes. An MRI policy can be amended to protect the equity at risk, whether this is the equity of a lessee or that of an innocent owner.

MARSH

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