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MARITIME

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- CAREFUL ANALYSIS IS REQUIRED TO DETERMINE WHICH VEHICLE AND JURISDICTION IS PREFERABLE FOR A SPECIFIC PROJECT
- BOTH JURISDICTIONS OFFER RELATIVELY INEXPENSIVE START-UP ANNUAL COSTS



Why do so many shipping businesses use Marshall Islands and Liberian entities in their structures? What benefits do they offer? And what is the difference between the three main entities they both offer: corporations, limited liability companies (“LLCs”) and limited partnerships? This briefing explores some of their key characteristics and advantages.

Main types of entities and key advantages

In both jurisdictions, the local laws relating to corporations, LLCs and limited partnerships are based on the equivalent Delaware and New York laws. Each entity has its own features, making it important to select the one which best suits the requirements of a particular transaction.

A careful analysis of the purpose(s) for which the offshore entity will be used, the nature of any major assets it is to own or operate, the location of any physical activities it undertakes and any specific requirements of the participants in a particular project (for example, regarding tax treatment or corporate governance) is likely to suggest that one vehicle and jurisdiction is preferable to the other potential options.

“IN BOTH JURISDICTIONS, THE LOCAL LAWS RELATING TO CORPORATIONS, LLCs AND LIMITED PARTNERSHIPS ARE BASED ON THE EQUIVALENT DELAWARE AND NEW YORK LAWS.”

KEY ADVANTAGES

- No requirement for a person, office or headquarters to be located in the Marshall Islands or Liberia (unlike other offshore jurisdictions with residency requirements);
- Start-up costs and annual costs are relatively inexpensive;
- Entities formed in the Marshall Islands or Liberia that do not conduct business or operations in those countries (and, in the case of Liberia, where less than a majority of the equity interests by vote or value is held directly or indirectly by holders resident in Liberia) are generally not subject to local income tax;
- Non-resident equity holders of Marshall Islands or Liberian entities are not subject to local taxation or withholding on distributions or dividends;
- Non-resident equity holders are not subject to Marshall Islands or Liberian stamp, capital gains or other taxes on the purchase, ownership or disposition of equity;
- No local requirements for either the entity or non-resident equity holders to file a tax return; and
- Streamlined and user-friendly processes to register vessels and record ship mortgages.

“ENTITIES FORMED IN THE MARSHALL ISLANDS OR LIBERIA THAT DO NOT CONDUCT BUSINESS OR OPERATIONS IN THOSE COUNTRIES ARE GENERALLY NOT SUBJECT TO LOCAL INCOME TAX.”

Notable characteristics: Corporations

Incorporation: Articles of incorporation are a public document; the bylaws are not.

Payment for shares: Liberian (but not Marshall Islands) corporations may issue shares before full payment for them is made.

Articles of incorporation prevail: To the extent that there is a conflict, the articles of incorporation prevail over the bylaws of a corporation or any shareholders' agreement.

Three levels of governance: The board of directors, elected annually by the shareholders, makes significant decisions for the corporation. Officers are appointed by the Board to act on behalf of the corporation on a day-to-day basis.

Directors make decisions: Directors make, but do not implement, decisions and do not have the apparent or ostensible authority to act on behalf of the corporation.

Officers implement decisions: Officers of the corporation should be appointed to act on the corporation's behalf on a day-to-day basis, as officers are recognised under Marshall Islands and Liberian law to have authority to bind a corporation in relation to third parties.

A secretary is required: Both the Marshall Islands and Liberia require corporations to have a secretary (or, in the case of Liberia, an officer that performs the tasks of a secretary). Neither jurisdiction requires any other officer.

“WHEN DRAFTING THE SHAREHOLDERS’/ STOCKHOLDERS’ AGREEMENT AND BYLAWS OR LLC AGREEMENT OR LIMITED PARTNERSHIP AGREEMENT CARE MUST BE TAKEN TO REFLECT MANDATORY PROVISIONS OF MARSHALL ISLANDS OR LIBERIAN LAW AND PROCEDURE.”

Notable characteristics: LLCs

Akin to partnerships: A certificate of formation must be publicly filed, but the LLC Agreement governing LLC operations is agreed between the equity holders and is not public. LLCs have much greater flexibility than corporations to contract out of the standard rules that would otherwise apply to its organisation and operation. Unlike a partnership, an LLC may be owned by one person and all equity holders can benefit from limited liability.

Tax planning: Even though an LLC has been formed in the Marshall Islands or Liberia, documents may need to be filed in other jurisdictions shortly after formation, e.g. relating to tax treatment in relation to equity holders.

Complying with a LLC Agreement: LLCs must be managed in accordance with the LLC Agreement and, to the extent it is not properly followed, the manager may be subject to personal liability and actions it takes may not be valid.

High Utilisation: Although LLCs are relatively novel, they have become the investment vehicle of choice in the United States.

Notable characteristics: Limited Partnerships

Flexible governance: Similar to LLCs, a certificate of limited partnership must be publicly filed, but the Limited Partnership Agreement, which governs how the limited partnership will be operated, is not public. Like an LLC, in many instances the limited partnership may elect to opt out of otherwise applicable rules relating to its organisation and operation.

Understood in foreign jurisdictions: Although a limited partnership is a slightly more complicated structure than an LLC, they are sometimes used in transaction structures because LLCs have more difficulty managing third party internal processes, procedures and banking matters where the relevant foreign jurisdiction does not have the equivalent of an LLC.

Board structure: Although the traditional limited partnership is governed by a general partner, similar to Delaware, the Marshall Islands statute permits the general partner to delegate its rights and powers to manage and control the business and affairs of the limited partnership to other persons.

Some potential pitfalls

Whilst they are generally flexible and straightforward to establish and maintain, the use of Marshall Islands and Liberian entities is not without potential pitfalls. In particular, as well as the importance of choosing the type of entity most appropriate to each project (as discussed above), when drafting the shareholders’/stockholders’ agreement and bylaws or LLC Agreement or limited partnership agreement (as appropriate) care must be taken to reflect mandatory provisions of Marshall Islands or Liberian law and procedure, particularly if a document is to be governed by the laws of another jurisdiction (for example, shareholders’ agreements for Marshall Islands corporations are often made subject to English or New York law and jurisdiction).

FOR MORE INFORMATION

Should you like to discuss any of the matters raised in this Briefing, please speak with a member of our team below or your regular contact at Watson Farley & Williams.



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