GOVERNMENT OF INDIA
SHIPPING
LOK SABHA

UNSTARRED QUESTION NO:2763
ANSWERED ON:15.03.2010
GERMAN KG MODEL OF INVESTMENT
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Will the Minister of SHIPPING be pleased to state:

(a) whether to address the growth requirements of the shipping industry in other countries, the German KG model financing for shipping has been found to be a time tested model wherein high net worth individuals -particularly professionals such as doctors, lawyers and engineers - invest in a special fund for buying ships and the contributions to the fund get tax exemption;

(b) if so, the details thereof;

(c) whether the Government proposes to adopt such model of investment in the country;

(d) if so, whether such model would be viable and operational in Indian conditions; and

(e) if so, the details thereof and if not, the reasons therefor?

Answer

MINISTER OF SHIPPING(SHRI G.K. VASAN)

(a) to (e): In a traditional ship financing deal, the ship owner and the beneficial user are one and the same whereas the German KG Model of financing works more like a lease, with the final user (the Charterer) of the vessel is separate from the shipowner but with the charterer getting the full benefit of the vessel as if it was a owner of the vessel. In KG financing the bulk of the equity is provided by third parties. The equity house creates a fund to purchase the ship. The fund raises the money from the private investors and the loan from a bank. The purchase price of the vessel is financed partly by equity (usually 35-50%) and partly by bank loan (50-65%) secured by a first mortgage over the vessel. The limited liability partnership means private investors taking part in the KG fund are liable only for the amount they have invested.

Initially the KG fund was very attractive in Germany because of the accelerated depreciation that was allowed and high level of tax loss allocation which was extremely beneficial to the investors as they were able to set off the loss against their taxable income. However, subsequently such accelerated depreciation has been discontinued with the introduction of tonnage tax. Under the tonnage tax, the offsetting of loss is no longer the attraction of investment in KG fund. This mode of financing however is more expensive compared to direct lending by bankers to the ship owners as various soft costs like sales and marketing commissions which are paid to sales channels (wholesale and retail) are added. Such costs almost account for 15% to 18% of the amount placed by the private investors.

With the going away of provision of accelerated depreciation, this model of financing is now less attractive. Further, shipping is a volatile industry. Freight rates move up and down drastically. There is huge risk of counter party default when asset prices and freight move downward drastically.

In India,the investors in equity have various options available.Therefore considering the volatility of Shipping Industry there is not likely to be much response to such mode of funding.Presently,there is no proposal for adopting such model of investment.