

**AGENDA**  
**YACHT FINANCING SUBCOMMITTEE**  
**April 29, 2015**

**David Bohannon**  
**Chair**

**G. Robert Toney**  
**Vice Chair**

Opening remarks, introduction of guests: David Bohannon

1. Christensen Shipyards, An Update of the US Builder's Insolvency  
--David Bohannon (Handout)
  
2. A Current Report of Mega Yacht Financing New Construction and Purchase Lending  
--Lisa Verbit US Trust/Bank of America
  
3. Briefing on the state of yacht lending from recovery and liquidators perspective  
– G. Robert Toney
  
4. Administrative/other matters of interest
  - a. Tax Law Changes New York
  
5. New business

## An Unhappy Marriage With Christensen Shipyards

by Dean W. Baker

The recent demise of a well known and respected builder of custom yachts in the United States market underscores the significance of state law issues to the "financing buyer's"<sup>1</sup> interest in the vessel under construction and the options the buyer retains in the wake of the builder's insolvency. On February 9, 2015 Christensen Shipyards, Ltd., ("Christensen") stopped construction of all vessels located at its Vancouver, Washington shipyard. See The Columbian, *Christensen Shipyards Close Gates*, February 9, 2015. Prior to November of 2014, potential buyers, as well as existing buyers whose boats were under construction would not have predicted the collapse of Christensen. The yard was teeming with workers constructing more than seven new builds. Despite the appearance of a healthy boatyard, Christensen stopped paying some of its vendors in the last quarter of 2014. Whatever the cause of that failure, buyers found themselves in the uncomfortable position of having to deal with a shipyard that was unable to pay its debts as they became due. The effect on buyers was immediate, resulting in the realization that the boats under construction were now subject to vendor's liens for unpaid bills and that Christensen could no longer perform existing construction contracts for previously agreed-upon fixed prices.

With respect to the vendor liens, Washington state law (similar to federal law) sanctions "secret liens". The liens are "secret" because they do not need to be recorded at either the county or state level. Although, claims for materials, labor, and services rendered prior to completion of new construction of a vessel are characterized as nonmaritime "dry land" liens, the Washington statute explicitly provides that they have "preference over all other demands". See RCWA 60.36.010. Accordingly the statutory language suggests that these liens have priority over all other liens, including any lien that buyers were afforded under their original construction contracts to secure the payment and performance obligations of Christensen. In that regard, Christensen construction contracts were typical of most American-build contracts, providing title to the vessels under construction resided in the builder until delivery and granting the "financing buyer" a security interest in the vessel under construction to secure builder's obligations to the buyer under the contract. Notwithstanding the fact that vendor liens prime the buyer security interest, it is critical that the buyers do have liens (perfected under American law by filing in accordance with the Uniform Commercial Code) in order to preserve their interests in the face of any ensuing bankruptcy or receivership proceedings.<sup>2</sup> Without a lien, the buyer's

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<sup>1</sup> A "financing buyer" provides financing to the shipyard to build the vessel by making payments in installments, typically at agreed-upon milestones of completion. The Christensen contracts provided for monthly installment payments, presumably to better manage cash flow. That arrangement is not standard in the large custom yacht industry and may have been a red flag, reflecting a thinly capitalized builder.

<sup>2</sup> If the construction project is in fact deemed to be construction of a new vessel, buyers perfect their security interests (typically granted under the construction contract) by the filing of a financing statement with the Secretary of State in the state where the builder is incorporated. We have seen form new build contracts that do

contractual interest (as well as all advances made by the buyer to the builder) in delivery of a completed vessel is at risk of being lost. A trustee or receiver has the power to reject the contract, retain the vessel under construction and relegate the buyer to the status of an unsecured creditor in the bankruptcy or receivership proceeding -- a disastrous outcome for the buyer who might receive pennies or no dollars on account of his unsecured claim. The security interest that was afforded buyers under the Christensen contracts, however, does not insulate the buyers from the reach of the vendor liens. The burden of satisfying those liens has now shifted to the only deep pocket available, namely the buyers.

The other immediate consequence of Christensen's bleak financial condition is the certainty that each buyer's bargained for fixed-price contract is no longer possible. Buyers are faced with the choice of moving their vessels to another yard or renegotiating their contracts with Christensen, in some cases for millions of dollars more than what they originally budgeted for a completed vessel. In either case, buyers understand that the original fixed price may be exceeded substantially.

In March of 2015 certain vendors initiated lawsuits to foreclose their liens and on March 20, 2015 a receiver was appointed to take control of and manage Christensen's operations.<sup>3</sup> A receivership proceeding under Washington law is analogous to a bankruptcy proceeding and the receivership statute borrows heavily from the federal bankruptcy code. There is now an automatic stay in effect and buyers that would like to remove their vessels will need to seek court permission to do so, most likely on the ground that there is no residual value in the vessel for the receiver because of the security interest initially granted by Christensen in favor of the buyer.<sup>4</sup> Simply, there is little doubt that the value of each of the vessels under construction is substantially less than the debt owed by the builder to the buyer.<sup>5</sup> In short there is no equity available for the receiver. Additionally, the buyers as secured creditors enjoy a constitutionally protected property interest in the vessels that will diminish over time<sup>6</sup>, unless the buyers agree to renegotiate their contracts with the receiver or any purchaser of Christensen's operations that

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not provide for the grant of a security interest in favor of the buyer. A buyer that is lulled into signing such a contract is playing russian roulette and any lawyer who blesses such an arrangement is risking a malpractice claim.

<sup>3</sup> Any decision to remove a vessel from the yard would have required a transfer from Christensen to the buyer of title to the vessel. Such a title transfer could be effected either voluntarily (i.e. with the agreement of Christensen) or involuntarily by a foreclosure of the buyer security interest.

<sup>4</sup> Any buyer that gained title to the vessel through foreclosure (of its security interest) prior to appointment of a receiver will have an easier time convincing the court that it should be afforded relief from the automatic stay in order to remove the vessel, since the receiver has at most a possessory interest in that vessel.

<sup>5</sup> The debt owed by the builder to a buyer under a defaulted construction contract includes, inter alia, return of all advances made by the buyer to the builder on account of the contract.

<sup>6</sup> The value of Buyer's secured interest will potentially erode from the accrual of interest (if that is allowed under Washington law) on any paramount liens that vendors have under the secret lien statute and from any diminution in the value of the vessels as they sit in the builder's yard and are not worked on.

succeeds the receiver through a court approved sale consummated by the receiver. For now the receiver is educating himself on Christensen's operations and ideally would like to turn a dead shipyard into a going concern that he can either operate or sell to a ready and willing purchaser. Either objective will require at least some level of participation by buyers willing to renegotiate their contracts. Certain buyers have already indicated a willingness to work with the receiver, believing that the option to remove their vessels to another shipyard will be more costly in the long run. At the time of this article it is too early to tell whether the receivership proceeding will benefit the buyers or delay any particular buyer's decision to divorce himself from the proceedings.

## NEW YORK BILL REVISES SALES AND USE TAX LAWS FOR VESSELS

By Steven A. Clark

An exciting change for yacht owners and marine industry constituents in the State of New York was recently signed into law – the new legislation essentially caps the combined state and county sales/use tax liability for the purchase or use of a vessel in the State of New York. New subdivision (JJ) of Section 1115 of the New York Tax Law, to be effective June 1, 2015, will exempt from taxation receipts in excess of \$230,000 from every sale or use of a vessel. By way of example, a \$1,000,000 yacht that is taxable under the current law (assuming taxable in Suffolk County, a popular yachting destination) would be taxed at 8.625% for a tax liability of \$86,250. Under the “new” law, only the first \$230,000 of the \$1,000,000 would be subject to tax, resulting in a tax liability of \$19,837.50; clearly a significant savings.

We wish to caution vessel owners, however, that sales/use tax liability in the State of New York still remains a complicated matter, especially if a vessel owner has previously operated their vessel in New York waters (i.e. prior to June 1, 2015). Prior presence could subject the vessel owner to potential sales/use tax liability under the old law, which as exemplified, can be a much more significant number.

We wish to further caution vessel owners that any advice to quickly register a vessel with the State of New York and pay sales/use tax under the new law could be misguided and might result in unexpected (and needless) additional tax liability. Each situation must be carefully analyzed.

Our firm would be happy to discuss/review with you the new law, the facts concerning your current ownership and operation of your yacht, the potential implications of the new law based on your situation, and ultimately provide guidance as to how best to address any potential tax liability (and hopefully, tax savings).

42 Section 1. Section 1115 of the tax law is amended by adding a new  
43 subdivision (jj) to read as follows:

44 (JJ) NOTWITHSTANDING ANY OTHER PROVISION OF THIS ARTICLE: (1) RECEIPTS  
45 IN EXCESS OF TWO HUNDRED THIRTY THOUSAND DOLLARS FROM EVERY SALE OF, AND  
46 CONSIDERATION GIVEN OR CONTRACTED TO BE GIVEN FOR, OR FOR THE USE OF, A  
47 VESSEL SHALL BE EXEMPT FROM THE TAXES IMPOSED BY THIS ARTICLE. FOR  
48 PURPOSES OF THIS SUBDIVISION, "VESSEL" SHALL HAVE THE SAME MEANING AS  
49 SUCH TERM IS DEFINED IN SECTION TWENTY-TWO HUNDRED FIFTY OF THE VEHICLE  
50 AND TRAFFIC LAW AND ANY OUTBOARD MOTOR OR TRAILER, AS DEFINED IN SECTION  
51 ONE HUNDRED FIFTY-SIX OF SUCH LAW, WHEN SOLD IN CONJUNCTION WITH SUCH  
52 VESSEL.

53 (2) FOR PURPOSES OF SUBDIVISION (B) OF SECTION ELEVEN HUNDRED ELEVEN  
54 OF THIS ARTICLE, THE PURCHASE PRICE, CURRENT MARKET VALUE, OR FAIR  
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1 RENTAL VALUE, AS THE CASE MAY BE, OF A VESSEL PURCHASED BY A RESIDENT OF  
2 NEW YORK STATE OUTSIDE OF THIS STATE FOR USE OUTSIDE OF THIS STATE THAT  
3 SUBSEQUENTLY BECOMES SUBJECT TO THE COMPENSATING USE TAX IMPOSED UNDER  
4 THIS ARTICLE SHALL BE DEEMED NOT TO EXCEED TWO HUNDRED THIRTY THOUSAND  
5 DOLLARS.

6 (3) FOR PURPOSES OF SUBDIVISION (I) OF SECTION ELEVEN HUNDRED ELEVEN  
7 OF THIS ARTICLE, RECEIPTS FROM, OR CONSIDERATION GIVEN OR CONTRACTED TO  
8 BE GIVEN FOR, THE LEASE OF A VESSEL THAT IS SUBJECT TO SUCH SUBDIVISION  
9 (I) IN EXCESS OF TWO HUNDRED THIRTY THOUSAND DOLLARS SHALL BE EXEMPT  
10 FROM THE CALCULATION OF TAX DUE UNDER SUCH SUBDIVISION (I).

11 (4) FOR PURPOSES OF PARAGRAPH ONE OF SUBDIVISION (Q) OF SECTION ELEVEN  
12 HUNDRED ELEVEN OF THIS ARTICLE, THE LIMITATIONS ON EXCLUSIONS FROM THE  
13 DEFINITION OF RETAIL SALE IN PARAGRAPH ONE OF SUCH SUBDIVISION SHALL  
14 APPLY ONLY TO THE FIRST TWO HUNDRED THIRTY THOUSAND DOLLARS OF RECEIPTS  
15 FROM EVERY SALE OF, OR CONSIDERATION GIVEN OR CONTRACTED TO BE GIVEN  
16 FOR, OR FOR THE USE OF, A VESSEL.

17 (5) FOR PURPOSES OF PARAGRAPH TWO OF SUBDIVISION (Q) OF SECTION ELEVEN  
18 HUNDRED ELEVEN OF THIS ARTICLE, THE PURCHASE PRICE OR MARKET VALUE, AS  
19 THE CASE MAY BE, OF A VESSEL SUBJECT TO TAX UNDER PARAGRAPH TWO OF SUCH  
20 SUBDIVISION (Q) SHALL BE DEEMED NOT TO EXCEED TWO HUNDRED THIRTY THOU-  
21 SAND DOLLARS.

22 (6) FOR PURPOSES OF SUBDIVISION TWO OF SECTION ELEVEN HUNDRED EIGHTEEN  
23 OF THIS ARTICLE, THE LIMITATION ON THE EXCLUSION FROM COMPENSATING USE  
24 TAX IN SUCH SUBDIVISION TWO WITH RESPECT TO QUALIFIED PROPERTY, AS  
25 DEFINED IN SUCH SUBDIVISION, SHALL APPLY ONLY TO THE FIRST TWO HUNDRED  
26 THIRTY THOUSAND DOLLARS OF CONSIDERATION GIVEN OR CONTRACTED TO BE GIVEN  
27 FOR, OR FOR THE USE OF, A VESSEL.

28 (7) FOR PURPOSES OF PARAGRAPH (A) OF SUBDIVISION SEVEN OF SECTION  
29 ELEVEN HUNDRED EIGHTEEN OF THIS ARTICLE, THE REFUND OR CREDIT ALLOWABLE  
30 UNDER PARAGRAPH (A) OF SUCH SUBDIVISION SEVEN SHALL BE COMPUTED ONLY  
31 WITH REGARD TO TAX LEGALLY DUE AND PAID TO ANOTHER STATE ON THE FIRST  
32 TWO HUNDRED THIRTY THOUSAND DOLLARS OF THE PURCHASE PRICE.

33 (8) EXCEPT AS OTHERWISE PROVIDED HEREIN, THIS SUBDIVISION SHALL NOT BE  
34 DEEMED TO LIMIT ANY OTHER EXEMPTION, EXCLUSION OR CREDIT IN THIS ARTICLE  
35 RELATING TO A VESSEL.

36 S 2. Section 1118 of the tax law is amended by adding new subdivision  
37 13 to read as follows:

38 (13) IN RESPECT TO THE USE WITHIN THE STATE OF A VESSEL, AS DEFINED IN  
39 SECTION TWENTY-TWO HUNDRED FIFTY OF THE VEHICLE AND TRAFFIC LAW, UNTIL

40 THE FIRST OF THE FOLLOWING EVENTS OCCUR:

41 (A) THE USE OF SUCH VESSEL WITHIN THIS STATE BY THE PURCHASER THEREOF  
42 FOR A PERIOD IN EXCESS OF NINETY CONSECUTIVE DAYS;

43 (B) THE DATE UPON WHICH SUCH VESSEL IS FIRST REQUIRED TO BE REGISTERED  
44 PURSUANT TO SECTION TWENTY-TWO HUNDRED FIFTY-ONE OF THE VEHICLE AND  
45 TRAFFIC LAW; OR

46 (C) THE DATE UPON WHICH SUCH VESSEL IS SO REGISTERED.

47 S 3. This act shall take effect June 1, 2015 and shall apply in  
48 accordance with the applicable transitional provisions in sections 1106  
49 and 1217 of the tax law.