Lawyers rejig as bubble bursts

Facing a big gap from lost contract enforcement work, law firms are turning to offering sanctions and anti-corruption advice

New York maritime law firms will be intently focused on collecting unpaid bills for their clients in light of this year's troubled freight markets. The sanctity of the contract in shipping has never been weaker, according to Blank Rome partner Jeremy Harwood.

"The lack of commercial morality is extraordinary. Companies are saying: 'If the deal goes bad, we'll just walk away.'" he told *Fairplay*, lamenting: "It hasn't always been this way in shipping."

"It's a really serious problem and you can't say it's geographic," Harwood continued, meaning it's not just an Asian issue. "If Europeans don't want to pay, they're not going to pay. We're facing the same problems with US corporations," he added.

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Rule B cases a day in NY's Southern District Court when activity peaked. Now it's less than one

The contract enforcement dilemma has been exacerbated by the 2nd Circuit's 2009 decision to ban maritime Rule B attachments of electronic funds transfers (EFTs) in New York. Eighteen months on, this landmark ruling is still weighing on local law firms.

"It's like when Elvis died – you remember where you were the day you heard about it," said Seward & Kissel partner Bruce Paulsen.

Rule B EFT cases inflated a bubble of activity in the Southern District Court of New York. In 2H08-1H09, it saw up to a dozen maritime cases filed each day. Today, filings typically average less than one a day. The lost legal work hasn't been replaced.

The impact of lost fees has largely hit niche New York firms that once depended on high-volume Rule B

Brokers benefit from diversity

Local shipbrokers broaden services by tapping finance link

The world's tonnage is almost entirely owned in Europe and Asia, so what does a shipbroker in America's tri-state cluster (New York, New Jersey, Connecticut) bring to the table? The answer is access to capital, via the public markets of New York and the vast sums controlled by Manhattan's private-equity firms and hedge funds.

"There is tremendous opportunity for brokers in New York," Jacq Pierot Jr & Sons principal Bob Pierot told *Fairplay*. "There's a lot of creativity in terms of financial structures in this market, allowing us to tap into unique projects."

Close proximity to these capital sources allows a tri-state brokering firm to not only offer more options on the S&P front, but to diversify its services.

"The majority of the US brokers have a diversified base," Compass Maritime projects and finance MD Basil Karatzas told *Fairplay*. He noted that a typical tanker S&P broker in Piraeus may be closer to the decision-maker, but "they don't have the listed companies, private equity funds and joint ventures [in Greece], so we have a more diversified base of business, which makes our cash flow more predictable".

Karatzas maintained that the diversified model of US firms such as Compass is more value-added for shipping clients "because it offers a greater breadth of services". He noted that "brokers based in Greece are doing business in only one part of the market".

The world-leading supply of private-equity capital in New York has yet to have a dramatic effect on shipping, but it has definitely played a role. New

[Photo: Greg Miller]

'If demand doesn't improve, owners or their banks will crack'

Basil Karatzas

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filings for the majority of their revenues. According to Watson, Farley & Williams senior associate Neil Quartaro: "We're seeing some of the firms that previously relied on that work looking for other profit centres and expanding their practice into areas that wouldn't normally be considered maritime, such as immigration."

Asked what the new business focus is for New York's larger, more diversified firms, attorneys speaking to *Fairplay* cited sanctions advice – on both Iran and Somalia – piracy and a rising level of concern over the Foreign Corrupt Practices Act (FCPA).

"Sanctions and piracy have kept us busy," said Paulsen. On sanctions, he noted that "whether it's Iran or Somalia, you're dealing with the same people [the US Office of Foreign Assets Control]". He reported that owners, brokers, insurance companies and banks were "all concerned about their exposure to Iran sanctions".

Jim Hohenstein, who heads the US admiralty practice of Holland & Knight, said: "In terms of Iran sanctions, there is a real overlay between the US and EU rules, so there's a lot more advice being provided to a lot more shipping entities on the effect of those sanctions and the interplay between them."

Losing out: work for the Southern District Court of New York has not been replaced
[Photo: Greg Miller]

Meanwhile, the FCPA was repeatedly noted by New York lawyers. "There's an increasing awareness of the anti-bribery and anti-corruption issue," said Hohenstein. "Clients are much more concerned about their compliance programmes. It's a tough issue for US-based clients, given the *modus operandi* in a lot of places in the world."

"There has been a huge upsurge in government enforcement of the FCPA," reported Al Yudes, head of the New York office of Watson, Farley & Williams.

As a result, said Yudes, "clients have more interest in ensuring that their contractual relationships have coverage in them for the FCPA, to make sure they won't run afoul of the law through the actions of some local agent or representative". F

York Maritime chairman Peter Shaerf estimated that private equity did more than $2Bn in shipping asset deals last year.

The problem is that shipping distress deals have failed to materialise, leaving primarily market-rate deals for private equity – although that dynamic could change if rates remain depressed.

Another component of broker diversification is vessel valuations, which are required by banks on an annual (or more frequent) basis. "This used to be a small part of the business, but I've put a lot of emphasis on growing it. It's now more important," said Karatzas.

A challenge to this business emerged for a brief period after the 2H08 financial crisis, when the absence of S&P deals made it very difficult for brokers to offer defensible valuations. While the S&P market is far from free flowing, there are currently enough last-done deals to assuage that issue.

"Now you have 'last done'," said Karatzas, although he noted that there remains a difficulty in determining whether that benchmark price qualifies as a market transaction or whether it was partially driven by a seller's distress. "The sale prices are now very much transaction-specific," he explained.

It's too soon to tell how regional shipbrokers will fare in 2011. After a difficult period in 2008-09, activity picked up last year. However, Karatzas noted that last year's S&P deals were dominated by older, cheaper ships sold to Asian buyers, not new tonnage.

This year's broker activity will depend on whether rates can recover. If not, there may be major shifts in ownership ahead.

"There is potential for a catastrophic situation we have not seen since 2008," said Karatzas. "If demand doesn't improve, some owners, or their banks, will crack." F