Throughout the market cycles, lawyers who craft loan agreements and the host of ancillary paperwork have always been an integral part of the process of ship finance, even if their names may not appear in documents. In turbulent times, the legal aspects of ship finance are elevated to headline status in the shipping space. 2008's Britannia Bulk demise, involved the triad of loan agreements on owned vessels, Forward Freight (FFA) and bunker hedging positions, and extensive time-charter commitments. In early January shipping's trade press has featured seemingly daily coverage of freight operator Armada's travails in Singapore and New York courts. In the wake of all this activity, the important work of finance lawyers is highly visible.

A sign of the times can be seen from recent communications from U.S. lawyers Blank Rome (with maritime teams in New York and Washington, D.C.), whose recent newsletter to clients devotes considerable ink to "Chapter 15" Bankruptcy filings. Such a filing was made in the Britannia Bulk matter, during November 2008. Blank Rome Partner Jeremy Harwood, describes Chapter 15, added to the U.S. Bankruptcy Code in 2007 to enable liquidators in non-U.S. bankruptcies to file a petition in the U.S. court, saying: "The sensible purpose was to allow the foreign representative to marshal all the assets of the debtor for the main, 'home' bankruptcy case for equal pro rata distribution, rather than to allow U.S. creditors to obtain more than their fair share in a 'piecemeal' fashion." Harwood and Partner Thomas Belknap, Jr. also discuss "Rule B Attachments"- where money moving through the U.S. banking network can be attached by claimants. Indeed, numerous attachments were filed against Britannia Bulk (prior to the Chapter 15 filing). Harwood explains: "The little heard of Chapter 15 is likely to become as familiar as the term "Rule B" in admiralty circles. It effectively shuts down Rule B and other pre-judgment and post-judgment collection efforts throughout the U.S. in one fell swoop."

Out of the spotlight, teams of lawyers have been negotiating intensively with banks and borrowers to shore up credit agreements, following the collapse of the drybulk market in late 2008. The initial reported news has been encouraging. Listed company Eagle Bulk Shipping (Nasdaq "EGLE") reached a late December (2008) deal with its lender, Royal Bank of Scotland (RBS), amending covenants concerning requisite loan to value ratios and company net worth, among others, in its USD 1.35 Billion facility. In early January, 2009, Oceanfreight (also Nasdaq listed) reached announced that it had reached an agreement with Nordea concerning loan to asset value on its USD 325 Million facility.

Good legal work requires a keen commercial sense of what a client (and counterparties) are trying to accomplish. Mark Russell, a London-based partner at Stephenson Harwood (SH) described the outcomes of recent finance negotiations as follows: "The solutions inevitably have been of a pragmatic nature, and generally have resulted in lenders and borrowers compromising to reach a solution that each can live with."

In "normal" times, when asset markets, freight rates and prices of the cargoes are relatively calm, the legal side of finance, though tightly intertwined with banking, is generally taken for granted. But, in times like 4Q 2008, "…attention has been focused on

certain boiler plate provisions in loan documentation which historically have not generated much interest," said Russell. In particular, he pointed to market disruption clauses in loan agreements, which he labeled as "exhaustively analyzed," adding that "loan to value covenants have also been looked at very carefully…"

At Norton Rose (NR), the commercially driven approach was also evident, in conversations with three Partners in the Banking department- Richard Howley, Harry Theochari and James Stonebridge. The NR team identified market disruption and valuation provisions as "the most problematic…for financial institutions." At Watson Farley Williams (WFW), London-based Partner Nigel Thomas expressed concern about the fractious nature of bank syndicates, telling Janes: "You can see, however, where the 'fault lines' will appear from the market's retreat to bilateral and small club deals (the only ways anything is being done at all). All of the traditional provisions of syndicated lending dealing with majority decisions, individual bank costs and performance etc. will come under intense scrutiny."

When discussion the market disruption clauses in new transactions, the NR team said: "both financial institutions and borrowers have had a common interest in coming to a fair and practical agreement now that it is clear that these scenarios can occur." The partners added that: "..in crafting a solution, parties tend to recognize that the relevant disruption event does have to have a "market" connotation," explaining further that market disruption clauses cannot "just be used because a lender has a different cost base to others within the syndicate." WFW's Nigel Thomas offered the view that "…banks are tinkering with boilerplate provisions in loan agreements and looking to find, in tried and tested provisions of loan agreements, the reason for their current predicament." His colleague Mike Vernell added: "We have seen some, limited examples of lenders trying to craft new solutions to the use of screen rates to determine cost of funds." He cautioned, however, that such efforts to "tinker with the fundamentals of euromarket documents" have not been successful, saying, "Most, if not all, have proved unsatisfactory as banks have tried to mask a wish to lend based on their own, actual cost of funds behind a veneer of objectivity."

The NR partners offered a menu for crafting solutions to the knotty problems of market disruption clauses in the context of multiple lenders in syndicated facilities. According to the team, "Solutions tend to involve combinations of, amongst others, agreeing (a) thresholds as to the number of financial institutions (or their relevant proportion of the facility) affected by the disruption event, (b) differentials between the cost of funds of affected lenders and the BBA rate and (c) the level of detail related to the disruption event that must be provided.

Turning to the difficulties with provisions related to asset values, the NR partners described the impact of the sharp dropoffs in vessel prices (as much as 50% in some cases) between the Summer of 2008 and the end of the year. They told Janes: "Reduced valuations and, in certain circumstances, inability to obtain valuations, has provided difficulties both in relation to deliveries of vessels and in connection with the usual operation of minimum value clauses," suggesting that, while lenders and borrowers

continue to discuss values, "for the most part financial institutions are taking a practical approach to this issue and allowing time to see where assets values are likely to move next year."

Veteran bankers and lawyers in any transportation market will always compare present industry circumstances to past ups and downs. WFW partners Thomas and Vernell described a market dynamic that differs from that of previous cycles explained that previous cycles did not play out against the backdrop of an overall credit crunch. They told Janes: "What is quite clear is that the swashbuckling of seizing assets days are largely gone- this will be much more the era of insolvency regimes."

The NR team described a similar view of the landscape on this voyage through the cycles, where listed companies feature more prominently than in the past. They told Janes: "The flight to public markets is also likely to change the nature of how financial institutions deal with problem loans and bankruptcy situations. This is because traditionally there have been many shipping companies that have sought, or been eligible for, bankruptcy. This time around bankruptcy protection has much greater prominence and therefore financial institutions will need to be very careful about the actions they take. They will have to consider whether their worldwide interests could be affected by being held in contempt of court (or any similar adverse ruling) for taking enforcement action in breach of bankruptcy protection orders."

Potentially, the changed market dynamic has important implications for the contour of bank lending going forward. Reed Smith's Rymer first described the backdrop- the growth of low margined large syndicated loans, reflecting industry consolidation, also pointing out that bank lending had moved to "…a focus on specific charter/employment backed transactions or near corporate lending." Echoing the notion that a bigger and more corporate shipping industry will profoundly impact how adverse situations are handled, the WFW Partners described some of the specifics that they are expecting: "Shipping groups are too big to clear up any major problems by arresting and selling ships at auction or through bank controlled SPVs. This time around, we will see Chapter 11, administration and equivalent insolvency arrangements used far more widely."

The NR lawyers talked another possibility- the development of a market for trading loans. They told Janes: "Whether the involvement of a secondary market in purchasing distressed loans from the financial institutions becomes a feature of the maritime sector remains to be seen. Clearly, it could have a significant impact and would represent a change to the previous cycle." They cautioned: "Arguably, if the selling down of a debt did become a regular feature, this could compound the problems of certain companies who may also have more layers of debt and more complex capital structures than in the previous cycle."

Complexity, whether in the actual structure, or in the sheer size of large syndicates, will have further implications, according to Nigel Thomas from WFW. Thomas, whose experience includes acting in deals where finance took the form partnership and project structures, suggested: "Another feature will be far more jockeying for position between

rival banking syndicates, swap providers and other creditors. The development of more 'corporate credit' facilities within the shipping sector means it will be much more difficult for individual banks or clubs/ syndicates to 'do their own thing'. Expect to see creditor committees and all other features of corporate insolvencies."

RS's Rymer picked up on the theme of how complexities might be handled, when Janes asked about the evolution of structures. He suggested that: "We will also see financing players coming in who have something to offer where other financiers can not/ do not- not quite 'vulture' but perhaps 'supra vulture', for example lenders who are not only financiers but traders."

WFW cautioned that: "As stories of 'vulture funds' grow, and some actually come into being, a reluctance to allow unfettered sell down of loan participations will harden- probably together with requests to include clauses expressly dealing with consequences for banks which fail to perform." Mike Vernell said that specific measures could include "…rights of cancellation, termination of ongoing commitment fee payments (and possibly even clawback of fees paid but 'unearned')."

Such predictions of airborne predators notwithstanding, existing problems are being sorted. In December, 2008, one New York equity analyst, Cantor Fitzgerald, hailed Eagle Bulk's successful amendment of its RBS agreement, writing to clients: ": "…we suggest this agreement between EGLE and their lenders could be a bellwether arrangement for other companies in the sector." SH's Mark Russell told Janes: "We also expect to see a significant number of restructurings following the collapse in the freight rates and related second hand values in many markets. Conversations with bankers indicate that they will try to work with their borrowers to work their way out of the down cycle rather than in enforcing rates and forcing sales of assets, but time will tell whether this proves to be the case." NR's partners prefaced their views by referring to the broader financial markets, saying: "You would assume that financial institutions are likely to be more interested in workouts and restructurings in this cycle on the basis that the balance sheets of a number of such institutions are already badly affected by the credit crunch and they may be keen not to crystallize a loss unless it is certain that it cannot be prevented." But, sometimes the markets overtake the wants of their participants. The NR team, continuing, offered: "That said, we anticipate more insolvency filings in the maritime sector as workouts and restructuring are often dependent on raising further funding, which is very difficult in the current climate.

Reed Smith's Rymer echoed a similar view of banks trying to work things out, telling Janes: "In view of the across the board difficulties I imagine that banks will seek to be supportive as far as possible, since there is little alternative market for them to go to with the vessels." But Rymer was clear that banks would not simply be bystanders to their clients' difficulties, adding: "That said, banks will identify certain borrowers with 'bad' overall management which they will want to change, and further in particular where the liquidity crisis continues or deepens certain banks may have no alternative but to enforce upon default and to realize the assets to the extent possible." He concluded by alluding to cooperative spirit, and said: "But, as before, to the extent possible, banks will seek to

manage out matters in a quiet and confidential manner, albeit that this will be more difficult in relation to the mega facilities."

The Norton Rose team of Thoechari, Howley and Stonebridge offered further thoughts regarding valuation issues, from the shipowner perspective. They said that: "Market disruptions and valuations are the main issues for borrowers too at present but borrowers are likely to very keen to discuss the valuations provisions in greater detail in future transactions. In this context, we anticipate that borrowers will wish to be very clear as to exactly when minimum value clauses will be tested and to ensure that panels of approved valuers are fixed regularly updated depending upon their willingness to supply values."

Rymer (who had risen to partner in Richards Butler, which merged with Reed Smith in 2007) opined: "Hence, I see a move towards more bilateral 'fewer vessel' and more specific facilities with an emphasis on the direct technical and commercial management offered beyond the immediate long term charter employment (and counterparty risk) which may be on offer."

Looking forward and beyond conventional bank lending, Janes asked the law firms what deal structures might emerge after the ongoing shake-outs occurring, especially in drybulk. SH says, "…we expect to see more structured finance solutions during the first half of 2009. These might include tax based leasing, sale and leasebacks or other off balance sheet structures." WFW's Nigel Thomas offered noted that: "The fleet financings, with a strong revolving credit element, will likely be a casualty of the market. Banks won't participate in large syndicates and will want certainty above all else. The holy grail will be export finance agency supported deals- and preferably funded in large part by them, rather than just guaranteed."

Norton Rose says: "The increased risk associated with lower asset valuations is likely to lead to a significant reduction in leverage that will be made available by senior lenders and this could provide opportunities in the mezzanine market." According to NR, the sector was active in the early/ mid 1990's, with transactions where "…mezzanine lending <was provided> on a second mortgage basis but with higher spreads." A further look into the crystal ball suggests that: "..today's higher margins could incentivize such lending."

Law firms are reacting to the changed market circumstances and prospects through different forms of organizations. SH's Russell added: "As a response to these changes, we have established a cross group restructuring team, consisting of finance lawyers, litigation lawyers and insolvency lawyers."

At Reed Smith, Partner Nick Shaw, Global Practice Group Leader in the Shipping Group, described his firm's efforts: "In terms of workouts we have been training our people up. A number of our partners were around dealing in workout situations in the last recession and passing on that knowledge and fine tuning our processes to take immediate action has been key to date and will stand us in good stead in 2009." His colleague Philip Rymer mentioned that Reed Smith held a well attended workshop for bankers, late in 2008, and has followed this up with a series of breakfast meetings and targeted workshops for

bankers. He said: “We have a restructuring and workouts team with unrivalled previous experience comprising finance and litigation lawyers that is already in place and active, not least in delivering information to the market.”

The NR team told Janes: “Given the current climate, we have formed a core group drawing on our shipping, litigation and insolvency practices that can deal with both restructuring and insolvency assignments.” The team is already active, with NR saying: “We are currently acting for the administration of Britannia Bulk plc, one of the largest and most high profile corporate failures to do data in the shipping sector as result of the worsening market conditions in late 2008.”

Reed Smith’s Shaw has been closer to the epicenter of the ongoing turmoil in the FFA markets <<<see JTF???? >>>. The FFA contracts, swap instruments transacted in a daisy-chain fashion where one hiccup can reverberate down a chain of buyers and sellers, have put cash flows at already strained entities into further jeopardy. Shaw said: “We have a large team of people working on restructuring FFA positions with various defaulting or potentially defaulting parties and then drafting netting agreements, assignments and novations involving multi parties and 3rd Party companies on occasions.” His partner Philip Rymer also explicitly mapped out a closer link, going forward, that he sees between traditional shipping bankers and the FFA market. Rymer told Janes, “Banks will focus on trading activity around FFA’s and understanding (and controlling) this- since they are now seeing the losses and/ or obfuscation of results that may be experienced in this regard- and otherwise how an owner/ borrower manages its business looking beyond the asset and its immediate employment/ counterparty risk.”

Shaw concluded by describing his team’s sometimes frenetic work to Janes: “In the present market, the key is to be able to think fast and act quickly in order to preserve at least some of the liquidity in your clients’ positions. This can mean getting on planes as soon as a party looks likely to default and trying to hammer out a deal at short notice.”

The lawyers’ role is vital. WFW’s Nigel Thomas finished his interview by saying: “Our message to the banks is that now, more than ever, you need to know what is in your documents, and why. But, even then, no document can substitute for a close, on-ongoing and thorough relationship with a customer.”