



The Bottom Line

Business advisers and auditors to the shipping industry

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Risk management in tough times

Risk management has become an increasingly important aspect of global business. A mixture of prudence and optimism, and close attention to risk management, is essential at all times in the shipping industry, but the global economic downturn has accentuated the dangers which lie in wait for the unprepared. To manage risk, it is necessary first to identify it. Here are some points to consider.

Long-term charter party agreements should be money in the bank, but there are potential risks. For example, what is the charterer's reputation, how long is the charter, and how much business is tied up with a particular charterer? The failure of a charterer can start a counter-party domino effect which will have far-reaching consequences for trading partners.

Furthermore, where charters have been fixed at above-market rates, what is the risk that the charterer may not be able to fulfil its obligations, or attempt to renegotiate a lower rate? If the charterer reneges, deliberately or through insolvency, the shipowner will have to find a new charterer most likely at a lower rate in today's market.

There is a risk, too, where the bank or other counter-party owes money under derivative contracts to an owner. The bank or other counter-party may not be able to meet its obligations, and failure to honour the agreement could result in a loss.

And finally, another area of counter-party risk concerns shipyards constructing newbuildings. Assess the ongoing financial viability of both the yard and the associated refund guarantor.

Loan finance availability is currently very restricted, which may lead to an owner's inability to finance newbuildings, resulting in failure of the contract and potential losses to the owner. Shipping companies may also be exposed to interest rate risks on borrowings and to risks from exchange rate fluctuations.

Failure to comply with covenants on existing loans is also a key risk, as banks may call in their loans, threatening the survival of the business.

Where companies have insufficient resources to meet their contractual commitments, liquidity risks arise. Cash generated by trading activities will be insufficient to pay staff, suppliers and other creditors. Companies must



look at their options, including overdraft or other bank facilities, new equity finance, increased trading and sale of assets.

Companies need to be aware of their exposure to fraud. This might include the risk of collusion when charter parties are being arranged, over-priced contracts, and the possibility that supplier discounts for a range of goods and services from bunkers to drydocking may not be passed on in full in return for some kind of kick-back to a member of staff.

While it is impossible to eliminate risk from your business completely, robust risk management will help protect you against the unexpected. Risk management strategies and processes and regularly reviewed risk registers all fall within a strong governance framework.

The starting point of any risk management project is often a risk management workshop, which will provoke debate within the business. By the end, there should be improved understanding, increased transparency and better controls to monitor and manage strategic and operational risk.

Our governance, risk and assurance team helps clients in shipping and beyond in all these areas.

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Benchmarking with OpCost

Data collection for this year's OpCost report, Moore Stephens' unique annual ship operating costs benchmark tool, is now well under way; the 2009 edition promises to be bigger and better than ever before.

OpCost is firmly established as an industry benchmarking tool, and is extensively quoted and used as an authoritative source throughout the shipping sector. Last year's report contained, for the first time, a table showing a proportional representation of the total operating costs of the main vessel types, based on vessel age. In all, OpCost 2008 embraced a total of 23 vessel types and sizes, covering twelve different cost categories and attendant analysis.

This year we are hoping to expand the number of vessel types covered and are aspiring to include categories for offshore vessels, LNG and LPG carriers, and container ships above 4,000 teu. Of course our ability to increase the range of vessels is largely dependent on input from shipowners and operators. We continue to receive data from major shipping businesses on an annual basis for inclusion in OpCost, and we are actively seeking still more contributions.

Data sent will be treated as strictly confidential, and contributors to the database receive copies of the report free. To submit your data or to reserve a copy of OpCost 2009, please email:

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Progress through learning

The Institute of Chartered Shipbrokers (ICS) is in the business of providing the shipping industry with highly qualified professionals. It is approaching its centenary year, but it continues to move with the times and today it is the only internationally recognised professional body which represents shipbrokers, ship managers and ship agents throughout the world.

ICS Director Alan Phillips explains, "The ICS continues to expand, both in terms of its international presence and its syllabus. We have 24 branches in key shipping areas, and roughly 3,500 individual and 120 company members. We will shortly open a new branch in Kenya, and others in Houston and Denmark later in the year. In addition, we have our Distance Learning Centres, the most recent of which is that established at Odessa, in the Ukraine.

"We have come a long way since the days when the ICS was just an organisation for shipbrokers. Our expanded syllabus now covers port and terminal management, for example, and the offshore service and ship finance sectors.

"We believe it is in the best interests of individuals, of their employers, and of the shipping industry in general to have a properly qualified workforce, and a proper system of recognising such qualifications. Education and training is becoming increasingly important with globalisation, and this year no fewer than 1,465 students sat a total of 3,504 papers in 84 exam centres around the world. There is enormous peer pressure to secure professional qualifications in today's shipping industry, and the ICS will continue to develop along the lines that industry demand dictates."



ICS Director – Alan Phillips

The ICS will celebrate its centenary in 2011. Moore Stephens has not been its auditor for anywhere near as long, but the two organisations have enjoyed a very good relationship for a number of years. Alan Phillips says, "What we are looking for from an auditor is a firm that is knowledgeable about our industry, which is responsive and proactive, and which is able to give us the advice we need, when we need it. We need a firm that will enable us to go the membership at the end of each year with a set of proper accounts which is complete, accurate and entirely transparent. And that is what Moore Stephens enables us to do."

The Seajacks Kraken wakes

Julian Wilkinson, head of the Moore Stephens shipping team in London, and Dubai-based, John Adcock, head of Moore Stephens Middle East, were among the guests who attended the recent naming ceremony of the specialist self-propelled lift-boat Seajacks Kraken at Lamprell Energy's Hamriyah Shipyard in Dubai.

The Seajacks Kraken will shortly be shipped on a heavy-lift vessel to Nova Scotia where, in May, she will start a five-month stint under charter to ExxonMobil Canada as an accommodation and construction support vessel at the Sable Island complex.

A sister vessel to the Seajacks Kraken, the Seajacks Leviathan, is scheduled for completion at the Hamriyah Shipyard within the next few months and has already been contracted to work as a wind turbine installation unit off the UK coast under charter to Fluor for a fourteen-month period beginning in September 2009, with options to extend.

Julian Wilkinson says, "It is good to see a shipping company in these difficult times building and delivering vessels on schedule and to budget. These are innovative vessels, capable of working in hostile environments, and the nature of the charters which have already been



agreed for the Kraken and the Leviathan underlines just how versatile these newbuildings really are."

Moore Stephens has acted as auditor for Oslo-listed Seajacks since its formation in 2006 by a group of experienced North Sea jack-up managers.

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Confidence shows twelve-month decline

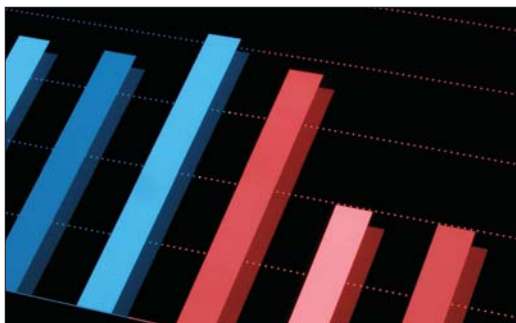
Overall confidence levels in the shipping industry have declined by more than 20% over the past twelve months, according to the latest Moore Stephens' Shipping Confidence Survey.

One year on from the first survey, the average confidence level expressed by respondents, on a scale of 1 to 10, was 5.4, compared to 6.8 in the initial survey in February 2008. But a number of respondents felt that things were likely to improve over the coming twelve months and beyond. The survey also confirmed that there are winners in every downturn. One respondent said, "Cash-rich buyers will be looking at the bargains of the millennium come the summer."

There was also evidence that the economic downturn has caused particular problems for a number of operators. One respondent noted, "The biggest problem for us today, and probably for the next six-to-nine months, is counter-party risk. Every time one operator goes bust it has a domino effect on everyone else".

Charterers were comparatively upbeat, although their increase in confidence in the last four months was still some way behind that recorded twelve months ago. One respondent commented, "Charterers are playing now in the shipping market like a child plays with its doll."

Over the past twelve months, the factors most influencing performance have changed. One year ago, it was ship operating costs, crew supply and tonnage supply that led the way. In the latest survey, it was demand trends, the cost and availability of finance, and competition.



There has been a marked fall over the past twelve months in the number of respondents who expect finance costs to rise. One respondent explained, "The cost of finance is less important than the availability. We are finding it very hard to get the debt side of projects together, but things do seem to be easing."

The fact that confidence levels have not fallen by even more is doubtless due to the fact that shipping is a resilient and innovative industry, and because, even in a depressed world economy, there is still sufficient demand for global trade which can only be transported by sea.

Download a copy of the full report from www.moorestephens.co.uk.

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When is a ship not a ship?

If it looks like a duck, swims like a duck, and quacks like a duck, it probably is a duck. But it appears you cannot say the same about a ship, at least not according to the UK tax authorities.

Seafarers are the last remaining sector of the UK workforce who may be entitled to 100% relief from income tax on their earnings, under the Seafarer's Earnings Deduction (SED) scheme. Seafarers are eligible for SED if they perform the duties of their employment wholly or partly on board a ship, provided they are absent from the UK for an 'eligible period', broadly over 183 days out of the UK within a 365 day period. But it would seem that the relevant legislation – Sections 378 to 385 of the Income Tax (Earnings and Pensions) Act 2003 – is not sufficiently clear on this point, if recent HMRC initiatives are anything to go by.

The SED entitlement of an increasing number of seafarers employed on rig support vessels is being challenged by the tax authorities, despite the fact that such vessels are moving between different offshore installations to perform their primary supply and support functions.



This follows HMRC arguing that floating production storage and offloading (FPSO) vessels are offshore installations and not ships.

The issue has now attracted political attention, which it is hoped might accelerate its successful resolution without the need to refer it to the Tax Commissioners.

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Companies Act update

A number of further changes are coming into force under the Companies Act 2006.

Firstly, there are new time limits for filing accounts for reporting periods beginning on or after 6 April 2008. Private companies will have nine months rather than 10, and public companies six months. Companies that miss their deadline will face higher penalties than before. The penalties increase with the degree of lateness, reaching £1,500 for private companies filing more than six months late, and £7,500 for public companies. These double for second and subsequent late filings.

Another change – a simplification – is that you just need to file by the end of the appropriate month. For example if your private company reporting period ends on 30 June, by 31 March in the following year. You won't be penalised for failing to file by 30 March – what used to be called the "corresponding" date.

A more significant change for some is that medium-sized groups now have to produce group accounts. However, small groups are still exempt from this requirement. The limits have been increased, so if you were medium-sized previously, it is possible you may now be deemed "small" and so could remain exempt. For the record, small groups are those which meet at least two out of three of the following criteria: turnover less than £6.5m net (or £7.8m gross), balance sheet less than £3.36m net (or £3.9m gross) and employee numbers under 50.

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The Bottom Line

Quote

"Wealth is any income that is at least one hundred dollars more a year than the income of one's wife's sister's husband."

H L Mencken

Who to contact

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Profile: Mike Mullen



Mike Mullen graduated from Rutgers University in New Jersey with a bachelor's degree in accounting. He went into practice in 1980, but soon realised that public market clients held more interest for him. So the following year he joined a firm which, some ten years later, was to become a member of Moore Stephens International.

Today, Mike is a principal of MSPC in New York, and an expert in the practical interpretation and application of SEC rules relating to publicly traded companies.

general lack of liquidity. But it's not all bad news. Some deals are getting done.

"Just recently we acted for Arlington Tankers during its successful merger with General Maritime Corporation. Another client, a sale and purchase and ship leasing specialist, successfully completed a record-breaking sale/leaseback transaction in the fourth quarter of 2008."

Away from work, Mike enjoys nothing more than spending time with his wife, Maria, and their three children. The family lives in Cranford, New Jersey, and Mike likes to play golf when he can. He admits to a handicap which is "very high", and says that now winter is turning to spring, he really is going to make time to play more often. He says that every year.

On a recent visit to the UK, Julian Wilkinson and his colleagues took Mike clay-pigeon shooting at Bisley. It was an experience he enjoyed immensely, but he says he can't see it catching on in the US, despite the fact that the rest of the world thinks everyone there has a gun.

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Speaking out

Moore Stephens believes in staying close to the industries which it serves, which is why we continue to participate in shipping industry debate and to speak out on the subject of shipping and finance to international audiences.

The recent Cass Business School, City University London module on 'The Valuation of Shipping Companies and Shares' was led by Moore Stephens' partner Richard Greiner and included presentations by fellow partner David Chopping, on accounting standards, and by corporate finance director, Marcus Graham, on the practical implications of dealing with valuations in the shipping industry.

Richard Greiner also made a presentation on the 'Interpretation of Financial Statements for Shipping Companies' to the recent Cambridge Academy of Transport 'Introduction to Shipping' course, and will deliver a paper in May on 'Budgeting and Cost Control' to the Isle of Man Ship Superintendents' Training Course, an induction programme aimed at seagoing engineering and technical personnel who are intending to come ashore, set up by the Isle of Man International Business School and the Isle of Man Ship Registry.



Also in May, Richard and David Chopping will lead a workshop on 'International Financial Reporting Standards for the Shipping Industry' at the annual Greek Shipping and Finance Conference in Athens, organised by Lloyd's Shipping Economist.

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