



The Bottom Line

Business advisers and auditors to the shipping industry

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Shipping looking sexy?

Shipping has been riding high for long enough for it to look sexy to investors who normally prefer to invest in things they understand.

It has come onto the radar of private equity and it looks attractive to small investors through stock market listings. Not just a few tanker plays and not just New York, but 2006 saw even small bulk carrier companies shine in the US and other bulker operators looking at the small cap AIM market in London. Investment was the shipping story of 2006, backed by banks desperate for a piece of the action giving money away with lower and lower rates and easier and easier terms. Entering 2007, shipping still looks sexy, despite the weak dollar and a sense of wonder amongst the greybeards that good times can roll on for so long.

What can we expect for 2007?

A wobbly dollar will give everyone the jitters, but in the end, no-one ever got rich betting long-term against the dollar. And even if it falls sharply, the consequences may not be bad for shipping, as a lower dollar could lead to more trade, rather than less.

Pain for banks. If shipping markets slip sharply, and no-one with a history book would bet they won't, then the banks will suffer. Never in the history of human lending have they lent so much, to so many, for such low returns, and some will come unstuck when freight incomes drop and cash flow tightens.

More stock market activity. In New York, if the US authorities move to water down regulation and the Sarbanes-Oxley requirements, which they have promised to do. In London, if they don't. New company listings are coming to London, with its lighter touch regulation and its more common sense approach to corporate governance. Shipping is almost mainstream now, and will follow. It won't be long before Uncle Sam rediscovers the virtues of laissez-faire, after which money may well flow back across the Atlantic again.

More non-financial regulation. The European Union is desperate to stitch a network of regulation and central planning around shipping, and it will succeed to an extent. That will distort competition in some areas, such as short-sea trades, and push up operating costs in others. Air pollution legislation is only now beginning to bite globally but when enforcement begins seriously in the US, and the EU sets about lowering emission limits, owners will again face cost and innovation hurdles.



More taxation. Europe's finance ministers have begun to realise the size of the tax breaks they have given to shipping. Expect moves to harmonise (for which read tighten) tonnage tax regimes and tax breaks, followed by movement of shipowners back to the less taxing climes from which they so recently returned.

Freight futures. Freight futures disappointed cynics by not creating enough major disasters for players during 2006, but also disappointed the prophets of paper trading by failing to achieve the wide acceptance and growth predicted by the people who sell them. For 2007 they will remain both a threat and a promise, while many in shipping still need to understand them.

Finally, consolidation. Stick thin models have been banned from Italy's fashion shows, and in shipping big is also becoming the way to look. Expect more takeovers of small shipowners by larger ones, more mergers of management companies, and at least one P&I club merger. Big is beautiful, and in the right light, even the old dame which is shipping still looks attractive.

Happy New Year.



The Bottom Line

Recognising newbuilding contracts

When you say "financial instruments", people think you mean things like interest rate swaps. Some realise it also covers more basic items, like debtors. Not many would realise it might mean newbuilding contracts.

Simplest scenario. Sign contract. Wait. Make the odd payment. Take delivery. Accounting for that is easy. The contract itself gives rise to no accounting entries, although it will be disclosable. As payments are made, sometimes including interest payments on finance, they are treated as assets under construction. On delivery, the vessel appears in the accounts.

But not all companies take delivery. A company may enter into a newbuilding contract believing the value will rise before delivery and intending, or maybe even just hoping, to sell on before delivery at a profit. The contract is a financial instrument.

Similarly, a company may receive an offer that is too good to turn down. That's more difficult. If it happens once it may have no impact. Twice? Three times? Over how many years? When it becomes the company's "practice" then all such contracts become financial instruments.

And why does it matter if we say a newbuilding contract is a financial instrument? Under IFRS, that contract has to be stated at its fair value at each balance sheet date. Gains and losses may need to be recognised on vessels you haven't even got yet.

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Pelican runs wet and dry

To many people in shipping, combination carriers (OBOs) were one of those theoretically good ideas which were the devil to make work in practice. But to Pelican Shipping they are a source of good returns. Abel van Staveren, finance director of Pelican, is happy to say that as the only OBO operator in the world still operating its fleet as it was designed to, with alternate wet and dry legs, the recent market has been more than kind.



"We operate a fleet of twelve OBOs," explains Abel, "and six suezmax product tankers. We are agents for SKS, which is the tanker division of the Kristian Gerhard Jebsen Skipsrederi Group. We were a pioneer of OBO trades and are the only company that have ordered

OBOs in the last 15 years. They are giving us good service. We were also a pioneer of suezmax product tankers, and that is a growing business."

Pelican is based in central London because, Abel explains, "We are close to the main tanker brokers and at the centre of the market. Our fleet operates mainly on Atlantic trades so London is a good location to operate from." Abel describes Pelican running as a lean and mean machine, with twelve people for all the chartering, operations and accounting functions. "With the team so close in an open plan office we feed from each other and we can react quickly to the market and exceed our customers' expectations," he says. "That gives us an edge and our ability to react quickly is a key success factor for Pelican. But as the whole team is stretched most of the time, everything that is not directly chartering or operations tends to end up being part of the finance function. It keeps life interesting."

Pelican and SKS have some interesting plans for the future. In addition to the current six new suezmaxes, two more are being delivered next year and Abel is not

standing still either. "For the last year and a half, I've been spending fifty per cent of my time on group finance and business development projects, and from January I'm moving to Singapore to do that full time for the Jebsen group of companies," he explains.

Dutch-born Abel joined Pelican direct from Moore Stephens, where he trained as an accountant. "I'm from a shipping background and had some commercial shipping experience when I bumped into a Moore Stephens audit team," he explains. "I saw what they were doing and liked the idea, so I joined them in London as a trainee, and I qualified as an accountant there. Then I joined Pelican and have had nearly six years here."

Moore Stephens is the auditor, tax consultant and payroll agent for Pelican, and Abel says that what he appreciates is that he can rely on his advisors being proactive. "There is always new regulation, so we have to rely on our advisors to keep us on our toes. One of the other key attractions of Moore Stephens is their knowledge of the industry. We work to very tight audit deadlines but, as Moore Stephens understands the industry so well, their team can come in and can take up queries with operations or with chartering directly. There are no silly questions and they have the professional respect of everyone, which makes them unique. It certainly makes my life easier."

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Moore news

Moore clients

David Anstis is leading an assignment in which Moore Stephens is advising the UK arm of major Norwegian shipping group Wh Wilhelmsen on accounting for vessel leasing. The group is moving a number of its car carriers to the UK company. David will also be lead partner for three new audit clients:

- Hong-Kong-listed bulk carrier specialist Pacific Basin which has appointed Moore Stephens to audit its UK agency company;
- the UK arm of Epic Shipping, which, amongst others, manages ro-pax vessels; and
- the UK business of Belgian freight forwarder, Confreight, which has operations in eighteen countries.

Moore Stephens has also been appointed international auditor to major river-sea company Volga-Balt.

The group operates around 600 river and short sea vessels, mainly in Russian and CIS rivers and coastal trades. Mike Simms is the engagement partner.

Moore speaking

Moore Stephens' experts continue to be in high demand as speakers. David Chopping, technical partner, will be speaking on Accounting for Derivatives at the Lloyd's Shipping Economist inaugural conference on Freight Derivatives, set for 26 February 2007 in London.

And Gavin Stoddart will be speaking at a UKTI conference on Russia and the Baltic States in London on 27 March 2007. He will cover the financial and tax regimes relevant to western Russia, Latvia, Estonia and Lithuania.



International growth continues

Moore Stephens International Limited has jumped two places to 11th in the 2006 International Accounting Bulletin World Survey of accounting networks.

Network firms' fee income increased by some US\$200 million to US\$1,545 million, a growth rate over the last two years of over two thirds, making Moore Stephens International the world's fastest growing network from 2004 to 2006, while headcount is now some 17,500 partners, principals and staff.

Richard Moore, Senior Partner of Moore Stephens LLP and Chairman of Moore Stephens International, said "As the world gets smaller, so it becomes more complicated. The Moore Stephens International network enables us to realise clients' international aspirations or cross-border objectives, particularly on issues such as local and international compliance, tax planning and international business structures.

"Our 2005 growth was due mainly to developments in North America. Our 2006 growth has largely been due to expansion in Europe. The last two years have been very busy and a great deal has been achieved. However, the more progress we make, the more it seems needs to be done and I am certain that the next two years will be even busier as we continue to develop further into our chosen markets".

Pensions Regulator tries his arm

The continuing fiasco of the UK's inability to manage pensions has taken a new turn, one which international shipping groups need to watch. Britain's newly-formed Pensions Regulator is threatening to issue a statutory notice attempting to force the foreign parent group of a UK company to make extra contributions to its UK pension fund.



In an effort to protect the rights of members of defined benefit pension schemes, the Pensions Act 2004 created the Pensions Regulator, who has wide ranging powers to force companies to fund their pensions schemes adequately.

As many UK firms are running

pension deficits, the main focus of the Regulator's efforts are to ensure that these firms agree clear and reasonable plans with the trustees of the pensions schemes to pay down the deficit by agreement. However, if no such agreement can be made, the Regulator can issue a contribution notice, which is a legally enforceable debt on the company. Going further, if the Regulator sees that the company involved is not financially secure or is unable to sort out the pension deficit, it can look beyond the company to its parent group and issue a Financial Support Direction. Effectively, the group has to bail out the pension shortfall of the weaker member.

In what looks set to be a test case, the Pensions Regulator has put Bermuda-registered Sea Containers on notice that it may issue a financial support direction requiring the group to pay \$254m into its UK pension

schemes. The move is against the background of Sea Containers sheltering in US Chapter 11 bankruptcy protection and moves by the company to treat its UK pension scheme shortfall in line with other creditors.

The proposed Financial Support Direction will break new ground and will become a test case on whether or not the UK Pensions Regulator can enforce payments to a UK pension from an overseas group. Shipping companies with international structures and which have defined benefit pension schemes for UK employees should keep a weather eye on this process. Prudence would point to a good hard look at the current pensions scheme, an assessment of its deficit, and a plan agreed with trustees to remedy the shortfall, if any. Otherwise expect the Pensions Regulator to come knocking, armed with powers to attach UK assets and also pursue payment from overseas group companies.



Quote

"The impressive European coastline and the characteristics of the European peninsula, as it is called in the Green Paper, are not fully exploited and, we believe, open major options for a substantial increase in waterborne transport and for increased business opportunities for our shipping industries,"

Fotis Karamitsos, director for logistics, innovation, co-modality and maritime transport at the EC's directorate-general for energy and transport explaining part of the rationale for a wide-ranging European maritime policy.

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Profile: Bill Beach



Bill Beach came to insolvency the hard way. He was working as an accounts manager for a firm that went broke, and when the mess had been sorted out the receiver offered him a job. He accepted, and took the first step on the road to becoming an insolvency specialist. Today, he is a director of Moore Stephens' Corporate Recovery.

Bill joined Moore Stephens in 1994. Today, he handles a wide range of insolvency work, including shipping business. The shipping

business mainly involves the appointment of Moore Stephens by maritime law firms as receivers in cargo disputes. The amounts at issue can be substantial. One such appointment, several years ago, involved millions of dollars tied up in oil cargoes on a number of vessels in the Middle East. More recently, it was cargoes of wheat and rice bound for Iraq that were at the heart of a dispute in which Moore Stephens was appointed.

Although it is Moore Stephens' pedigree in the shipping industry that is responsible for its appointment in such cases, Bill admits that there is nothing significant, or scientific, about his own involvement. "I just happened to answer the phone," he says. He adds, "Nine times out of ten, the shipping industry tends to sort out its own problems and, on those rare occasions when it can't, we are there to help."

Bill explains that general corporate recovery work tends to be cyclical, in as much as it follows the fortunes of the economy, with roughly a couple of years' time-lag. "If you read in the newspapers that we have just come out of recession," he says, "we reckon we are just about to go into one." These days, with our closeness to Europe, a lot of corporate recovery work involves cross-border insolvency, both within Europe and further afield. "We have UK insolvency law," he says, "and we have European insolvency law, and any number of other jurisdictions outside those areas. It can be complex and challenging, and there will be a continuing demand for people who are experienced in this area of business."

When he isn't crossing borders with his expertise, Bill likes to spend time at home with his family, in Kent. He and his wife have a son and a daughter who are, respectively, at university and taking A Levels. Bill is a big sports fan - cricket, football, rugby - but these days he confines himself to watching rather than actively participating.

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Research beefed up

Moore Stephens' shipping team's research capability has been boosted with the employment of Nikolaos Georgosopoulos as a research analyst.



Nikos is Greek and to no-one's surprise he comes from a shipping family. His father was a captain and now works for a shipping firm in London, while his brother is a shipbroker. Nikos studied International and European Relations in Greece and then moved on to

gain an MSc in Shipping, Trade and Finance from the Cass Business School.

His ambition is to develop a deeper knowledge of ship finance, while at Moore Stephens he will be heavily

involved in managing OpCost benchmarking data and helping the shipping team with background information on the sector as well as specific projects.

The research team also plan to roll out further benchmarking tools to help companies in shipping compare different aspects of their performance with industry-wide best practice and averages.

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We believe the information in Bottom Line to be correct at the time of going to press, but we cannot accept any responsibility for any loss occasioned to any person as a result of action or refraining from action as a result of any item herein.

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