Shipping and Offshore
Chapter 11 Cases: Lessons Learned

Marine Money Presentation

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Overview

The highest and best use of chapter 11 is to implement a restructuring transaction that has a critical mass of creditor support.

Use of chapter 11 by companies to coerce principal creditors to support an unfavorable restructuring, rather than to preserve value for all parties, is costly, value destructive and generally fruitless.

Every shipping chapter 11 case filed and maintained without creditor support has ultimately failed, meaning vessels were all sold or returned to secured lenders; cases filed with creditor support have confirmed plans of reorganization.

Consistent with this theme, recent offshore chapter 11 cases that have involved prepetition agreements with creditors and, in certain instances, significant new money investments by existing equity have successfully reorganized.
Case trends

Since 2011, at least seven shipping cases filed and maintained without secured lender support have all failed.

- Failed cases involved 93 vessels in the aggregate.
- Not one vessel was successfully restructured in these cases.
  - Record is now 0-93.
- Marco Polo, Omega, TMT, Winland, Sobelmar, Primorsk and Toisa.
On the other hand, six shipping cases filed with principal creditor support have confirmed a reorganization plan.

- Successful cases have generally involved larger fleets.
- General Maritime, Eagle Bulk, Overseas Shipholding Group, Excel Maritime, Genco and Rand Logistics.
- Even in such cases, existing equity was mostly or entirely eliminated.

Other companies have restructured with creditor support, out-of-court (e.g., Torm I) or through UK schemes of arrangement (e.g., Torm II).
Toisa Limited and its affiliated debtors filed for chapter 11 relief in January 2017, following failed restructuring negotiations with creditors and the arrest of certain vessels.

The company has 46 vessels (including 26 offshore support vessels) and several newbuild contracts, financed by 17 separate bank silos, with more than $1bn of total debt.

Existing equity declined to contribute new money needed to support a reorganization prospect, and the debtors have commenced a sales process for their assets.

The debtors have been in chapter 11 for 18 months and are liquidating assets under court supervision.

No end in sight . . .
Seadrill Limited and its affiliated debtors filed pre-arranged chapter 11 cases with a plan supported by c.97% of senior lenders, c.40% of unsecured bondholders and $1.06bn of new money commitments.

Filing occurred after 1.5 years of prepetition negotiation

Plan confirmed in 7 months!

Restructuring is expected to become effective in early July.

Headline terms:

- Committed $1.06bn new money investment, led by Seadrill’s existing reference shareholder, with other committed parties collectively representing a majority of unsecured bondholders.
- $2.3bn unsecured bonds equitized.
- $5.7bn senior debt reinstated at par, with a 5-year maturity extension and an amortization reduction, including a 2-year amortization holiday.
- Group structure adjusted to protect senior lender collateral and achieve structural separation of various non-consolidated subsidiaries for the benefit of new money investors.
Key takeaways:

- Bank CoCom remained aligned and worked through one set of advisors (White & Case, BAHR and Lazard) throughout the 1.5-year prepetition negotiation with the company and during the chapter 11 cases.

- 97% of the senior lender group signed onto prepetition support agreement (subsequent joinders took this figure to 99.8%).

- Senior lenders made concessions to attract significant new money investment and deleverage the capital structure.

- Unique alignment of interests facilitated deal: banks wanted to be repaid, unsecured bondholders wanted equity upside in reorganized company, and existing equity willing to provide significant new equity capital to offset bondholders’ risk.
Pacific Drilling and its affiliated debtors filed chapter 11 cases in November 2017 after a year of failed prepetition negotiations with secured creditors and the controlling shareholder.

The Debtors are currently participating in a mediation with secured creditors and the controlling shareholder regarding plan terms, including the split of equity in the reorganized company.

While the terms of the mediation are confidential, the controlling shareholder has disclosed publicly that it is prepared to make a new money investment in order to receive some portion of the reorganized company’s equity.

Bidding against bondholder group that also seeks control of the company and to pay off senior creditors.

Senior creditors expect to be paid in full or receive par paper and are supportive of an exit strategy that has the lowest execution risk.

Case has been pending for approximately 8 months.
Other Offshore Cases

- Ultrapetrol (Bahamas) Ltd.: prepackaged case filed on February 7, 2017; plan went effective on March 31, 2017. Existing equity eliminated.

- Tidewater Inc. prepackaged case filed on May 17, 2017; plan went effective on July 13, 2017.

- CGG Holdings (US) Inc.: chapter 11 case filed on June 15, 2017; plan confirmed October 10, 2017. Chapter 11 used to restructure bond debt at US issuer; equity restructuring carried out by French proceeding where existing equity received minimal new equity by participating in a rights offering.

- Expro Holdings US Inc.: pre-arranged case filed on December 18, 2017; plan went effective on February 5, 2018. Existing equity eliminated.

- Ocean Rig: Filed provisional Cayman liquidation on May 22, 2017 and ancillary chapter 15 case; proposed schemes of arrangement sanctioned by the Cayman Court on September 15, 2017 and given full force and effect in U.S. on September 20, 2017.
Why do non-U.S. shipping and offshore companies file chapter 11 without creditor support?

Can be very enticing.

- There is a low threshold for jurisdictional eligibility of non-U.S. ship and offshore owners to file chapter 11.
- Immediate stay of creditor actions (no cash sweeps or vessel arrests).
- Continued use of revenues.
- Affiliated vessel management companies and other non-U.S. affiliates can remain outside of chapter 11, preserving income streams and other assets.
Why do non-U.S. shipping and offshore companies file chapter 11 without creditor support? (cont.)

- Debtors have at least the *theoretical* ability to confirm a chapter 11 plan that modifies loan terms (e.g., maturity date, interest rate and covenants) over the objection of secured lenders.

- This is known as a “cramdown” plan.
Why cases fail without creditor support

Confirmation of a non-consensual (i.e., cramdown) plan is incredibly difficult to achieve. There have been no shipping or offshore cramdown cases during the survey period.

Cramdown requires that the nonconsenting creditors be repaid in full over time.

This means that the nonconsensual, restructured loan must include terms and condition sufficient to protect such lenders against, and compensate them for, the risk of nonpayment and future default, including:

- Tenor
- Rate of interest
- Collateral maintenance and coverage
Secured shipping and offshore loans are “asset based”.

The depreciating nature of the vessel collateral makes it extremely difficult to satisfy the “payment in full” requirement, even with a market rebound.

If a company could satisfy such requirements, it would likely not have filed chapter 11 in the first place.

While offshore cases appear to have a stronger market “rebound” business case, courts have not as of yet confirmed a case on that basis – and it is unlikely they will.
Why cases fail without creditor support (cont.)

Absent agreement, therefore, litigation is unavoidable.

- Cramdown litigation is time consuming, complex, and extremely costly.
- It requires extensive discovery, expert reports, legal briefing and a trial.
- Few equity owners can afford to engage in a protracted legal battle with their principal creditors.
- Pacific Drilling?
In addition, at least one creditor class that is not somehow connected to the company must accept the plan.

- Often misunderstood – a debtor cannot cram down everyone in chapter 11.
- Typically, where secured lenders are undersecured or marginally oversecured, such an accepting class either does not exist, or represents a small fraction of the amount of the overall secured debt.
- This is especially true in a typical secured shipping SPV-type finance structure, which is designed to limit the exposure of vessel collateral to extraneous creditors.
- The absence of such an impaired accepting class is fatal to cramdown.
Summary

- Principal creditor support is needed to confirm a shipping or offshore chapter 11 plan.
- No shipping or offshore debtor has successfully crammed down its secured lenders.
- Owners have not obtained the support of their principal creditors in smaller cases with traditional ship financing capital structures, typically because values and future cash flows cannot support the loan terms necessary to make the reorganization viable.
- Offshore cases have followed the same pattern so far; all successful cases have been prepackaged or prearranged, or equity has been willing to make a significant new money investment.
- The threat of a chapter 11 filing as leverage over secured lenders to do an unfavorable deal out-of-court is largely one of time, expense and value destruction, rather than the ultimate risk of a non-consensual restructuring in chapter 11.
Thank you