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Shipping needs a boardroom clean-up

Why I think that the Eagle Bulk lawsuit raises serious questions of corporate governance that could be a tipping point in companies' future conduct

THE civil lawsuit filed in New York last week by a shareholder of Eagle Bulk Shipping alleges serious breaches of fiduciary duty and waste by current and former directors and officers of the company.

The merits of the lawsuit will be judged in the Southern District Court of New York, but the suit contains a large amount of financial information that has been extracted from the financial and other information filed by the company with the US Securities and Exchange Commission.

This information contains details of the remuneration packages that the chairman, Sophocles Zoullas, and the other defendants received in 2008, 2009 and 2010.

Allegedly, the total compensation received by the defendants amounted to \$65.8m, or approximately 60% of the combined net income of the company for the same three-year period.

During this period, Eagle Bulk's share price fell from \$34 to \$5, a drop of 85%, or put another way, the company's market value has fallen from \$2,127m to \$153.9m. Moreover, on Thursday last week the shares closed even lower, at \$2.46.

I will leave it to our readers to make their own judgement of these facts.

In public companies, corporate governance requires management to run the companies for the benefit of the shareholders who have invested in them, and not to line the pockets of management at their expense.

Where are the banks that have lent vast amounts of debt to Eagle Bulk? Did they not see the huge amounts paid to the directors while the company was breaching its loan covenants?

This suit opens the door for other shareholder lawsuits which will look more closely at what has been going on in other public shipping companies. It will likely be a Pandora's box, which in Greek mythology is a jar that contained all the evils of the world.

This is a tipping point in the ability of shipping companies to raise public equity capital in the future. It requires all public shipping companies to take stock of their own practices and will differentiate those that can show proper corporate governance from those that cannot.

It also means that future IPO documents and the attached bye-laws need to be written to protect the shareholders' interests and not to allow sponsors and their selected management to siphon money from the company, or trade at will with related companies, or pay management fees to family and friends without a full disclosure and prior approval of a board of directors that is not simply composed of family or cronies.

The law firms that have produced these documents need to change their ways, and the investment banks and stock brokers that have peddled these companies to unsuspecting investors need to also worry about their possible liabilities.



Eagle Bulk chairman Sophocles Zoullas: details of the remuneration packages received in 2008, 2009 and 2010. During this period the company's share price fell from \$34 to \$5.

What were, or are, the analysts doing to properly examine the financial statements of the companies they cover, the make-up of their boards and the propriety of any "insider" transactions?

The shipping industry faces enough problems in overtonnaged markets and vast shipbuilding capacity. It does not need the public image that the Eagle Bulk lawsuit creates.

If the industry can respond to reducing external pollution from its ships it needs to clean up all internal pollution from its management and operations.

To start this process, the following is a shortlist of things that need to be changed:

- Boards of directors should have at least 50% independent non-executives and all board decisions must have a majority approval with no casting vote.
- The compensation committee, governance committee and the audit committee must be made up of all independent non-executive directors.

• The company needs to fully disclose all commissions or fees relating to the sale or purchase of any ships and the chartering of any ships, naming all the recipients and particularly those with any relationship to management. The practice of simply stating the net cost or benefit to the company is not sufficient.

• Where shipmanagement is contracted out to companies with any direct or indirect relationship to any of the company's directors or officers, the full details of those arrangements and particularly the management fees need to be approved by a majority of the board and disclosed in the company's financial statements.

• Any contracts between the company and any company directly or indirectly related to any director or officer of the company must be approved by a majority of the board, independently verified as to cost or value and shown in the company's financial statements.

• No director, executive or non-executive will be allowed to act in the same capacity for any other shipping company, public or private, that is the same business sector as the company.

The issue of proper corporate governance is not going away.

Now that the SEC and other regulatory authorities have been given a peek into Pandora's Box, the door to criminality looms closer. ■

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