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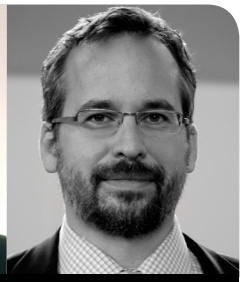
The Fracking Flip: U.S. Domestic Oil Production's Radical Transformation of the North American Tanker Trade

BY KEITH B. LETOURNEAU AND MATTHEW J. THOMAS



KEITH B. LETOURNEAU
PARTNER

MATTHEW J. THOMAS
PARTNER

KLetourneau@BlankRome.com MThomas@BlankRome.com

A flurry of recent economic data and activity suggests that U.S. tanker markets, both Jones Act and international, are riding swift new market currents that were unforeseen just three years ago. On November 14, 2013, the White House announced that the U.S., for the first time in nearly two decades, is importing less foreign oil than we are producing domestically. By the end of FY2014, imported crude oil shipments are expected to fall below 7.0 million barrels per day (bbl/d). As recently as the summer of 2010, imports reached nearly 10.0 million bbl/d. Domestic production is up 39 percent since 2011 and now exceeds 8.0 million bbl/d. The U.S. Energy Information Agency estimates that in 2013, the U.S. became the world's top oil and natural gas producer, exceeding the production of both Russia and Saudi Arabia, and is poised to become the leading crude producer next year. The increase is largely due to the rapid development of advanced drilling techniques, including horizontal drilling and hydraulic fracturing (fracking) in Texas, North Dakota, and Pennsylvania.

In the process, domestic production has flipped the crude oil import market on its head and accelerated the construction of U.S. built tankers for the coastwise trade. The Jones Act mandates that only U.S.-owned, -built, and -flagged vessels carry cargo between points in the U.S. Approximately 42 tankers currently ply the Jones Act trade. At least eleven product tankers, with options for quite a few more, are currently under construction at the Aker Philadelphia and General Dynamics-NASSCO San Diego shipyards, though the first of these are not expected to come on line until 2015. As well, new domestically-built, crude-carrying integrated tugs and barges are under construction. Meanwhile, charter rates for domestic tankers are reaching market peaks.

Yet, while coastwise tanker owners demand ever higher freight rates with domestic production accelerating, charterers are not sitting idle as they consider alternative modes of transport. Unprecedented investments in rail, pipeline, and terminal

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capacity are underway, fueling growth in Gulf Coast refining capacity and bringing new life to East Coast refining centers, where many facilities are better suited to light-shale crudes. The Philadelphia area alone is seeing an unprecedented influx of hundreds of thousands of barrels of Bakken crude every day, bound for local refiners. In addition, although much is made of the U.S. becoming a net exporter of refined products, sourcing products from overseas via foreign vessels remains an important strategic option for charterers.

Looking ahead, the outlook for the U.S. tanker markets hinges not only on the continued domestic production boom, but also on regulatory and political developments in Washington, particularly with regard to the decades-old ban on exporting U.S. crude oil. The 1973 Arab Oil Embargo prompted Congress to pass legislation that bans the export of U.S. crude, except to Canada, with only narrow and largely untested exceptions. In an effort to lift the ban, certain oil industry proponents contend that it has outlived its usefulness, artificially depresses prices, discourages investment in new production, exacerbates the U.S. trade deficit, and violates World Trade Organization export restriction rules. Not all U.S. oil industry businesses support lifting the ban, however. Some domestic refiners urge keeping the ban in place, as domestic crude production has sparked a boom in refinery investment, and lifting the ban could see the spread between U.S. and global prices (the Brent-WTI gap) narrow or disappear. Their unease is understandable; all investors in this sector—shipowners, refiners, terminals, pipelines, and other infrastructure—are struggling to weigh the risks and uncertainty caused by the unpredictable long-term outlook for the U.S. crude export ban.

On January 31, 2014, Congress held the first hearing about the crude export ban in a quarter century. Alaska Republican Senator Lisa Murkowski, Ranking Member of the Senate Energy and Natural Resources Committee, is currently the most vocal proponent of lifting the ban arguing that it adversely affects U.S. productivity and contributes to supply disruptions. Proponents of lifting the ban received a boost in recent days, when Democratic leadership announced that Sen. Mary Landrieu, another supporter of crude exports, was tapped to take over as chair of the Senate Energy and Natural Resources Committee. She and Sen. Murkowski will provide powerful bipartisan Senate leadership on this issue. At the CERA Week Energy Conference in Houston on March 3, 2014, Sen. Murkowski proposed a three-part plan to gradually lift the ban through executive action. Several members of Congress, including Democratic Senators Ed Markey and Robert Menendez, oppose lifting the ban because of the gasoline price effect, and it appears unlikely that Congress will tackle this divisive issue head-on this election year.

The Obama Administration has gone to some lengths to avoid articulating a position, or even acknowledging that it is actively rethinking the ban. However, the Commerce Department

and other officials have worked with individual companies to clarify and apply little-used exceptions to the crude ban. For example, as news outlets have noted in recent days, the Commerce Department appears to have begun licensing shipments of Canadian crude for shipment from U.S. ports, and much attention is being given to how the Administration will apply its "public interest" exception authority to provide for physical swaps of equivalent import and export volumes.

While the clamor for reforming the crude ban has escalated in recent months, calls for reexamining the Jones Act have been more muted. An unintended consequence of the Jones Act is that it costs more to transport crude from Texas to New York than it does from Texas to Canada because of the significant difference in freight rates between U.S. and foreign tankers. Refiners on the East Coast are paying far more to obtain domestic crude from the Gulf Coast than their Canadian counterparts. This has led groups such as the American Fuel and Petrochemical Refiners to call for changes to the coastwise laws; however, there appears to be little interest in Congress or the Administration at this point for such an initiative. While there is always talk about changes to the Jones Act, seeing is believing.

Looking ahead, the outlook for the U.S. tanker markets hinges not only on the continued domestic production boom, but also on regulatory and political developments in Washington, particularly with regard to the decades-old ban on exporting U.S. crude oil.

The exponential growth of domestic oil and gas production is also shifting the landscape of import and export tanker activity. During the past forty years, domestic refiners have imported a substantial amount of crude via tankers to provide feedstocks for their terminals. That demand increased the size of crude tankers and led to an offshore lightering trade in the Gulf of Mexico that employs smaller 70,000 deadweight ton (dwt) tankers to offload crude from 200,000 (and larger) dwt Very Large Crude Carriers ("VLCCs") and carry that imported crude to domestic refineries for conversion. With the advent of domestic fracking, it is conceivable within the next few years for many U.S. refineries to reverse that process in large measure such that they will be refining primarily domestic crude. In 2014, the U.S. is expected to import 3.6 million bbls/d less crude oil by sea than at the import apex in 2005. That equates to an astounding 1.3 billion barrels less per year, or, conservatively, enough crude oil to fill a 200,000 dwt VLCC more than a thousand times every year. This import decline is likely to continue until the U.S. reaches its maximum crude oil productivity.

The net effect is that crude imports will travel elsewhere, and domestically refined products will dominate the export market. Charter rates for foreign-flagged tankers carrying foreign crude sailed in the doldrums for much of last year with too many ships ordered before the recession hit, though a number of companies are investing in a crude market turnaround. Foreign crude carriers enjoyed a tremendous spike in rates at the end of last year, which allowed owners to breathe a sigh of relief; however, expectations in the charter trade are that rates will settle back down this year to levels more akin to 2013. Unless Congress lifts the ban on exporting domestic crude, rather than crude carriers, the U.S. market will demand even more tankers that can carry substantial quantities of refined product. The U.S. is currently exporting more than 3.5 million bbls/d of such products. Charter rates for these product tankers are increasing accordingly.

The rise of domestic crude production is literally changing the course of foreign crude carriers away from North America, while promoting a surge in domestic crude tanker capacity and boosting the export of refined products. In just a few short years, domestic fracking has fundamentally altered the tanker trade to this continent and the shoreside infrastructure that serves it—and it would seem there are more changes to come. ■

Sources: Roll Call – Oil Export Debate Renews Fight Over Protections for U.S. Shipping (4 Feb. 2014); E&E Daily, Energy Policy: White House leaves door open to revising crude export limits (31 Jan 2014); MARAD statistics, United States Flag Privately-Owned Merchant Fleet, 2000-1014; Bloomberg, Oil-Tanker Recovery Trails Market With U.S. Export Ban: Freight by Isaac Arnsdorf (9 Jan. 2014); Tradewinds article, Valero Defends Ban (8 Jan. 2014); Bloomberg, Unforeseen U.S. Oil Boom Upends Markets as Drilling Spreads by Asjylyn Loder (8 Jan. 2014); Oil & Gas Journal, Murkowski: Ban on US crude oil exports should end soon by Nick Snow (8 Jan. 2014); Reuters, Lisa Murkowski Urges Review of Oil Exports Ban by Valerie Volcovici (7 Jan 2104); Law 360, US Trade Gap Narrows as Exports Hit $195B, Oil Imports Drop edited by Philip Shea (7 Jan. 2014); U.S. Energy Information Administration (EIA), U.S. crude oil production on track to surpass imports for first time since 1995 (26 Dec. 2013); Bloomberg, Oil Industry May Invoke Trade law to Challenge Export Ban (5 Nov. 2013); Journal of Commerce, Could Crude Oil Put the Jones Act into Play? By Peter Tirschwell (30 Oct. 2013); EIA, U.S. expected to be largest producer of petroleum and natural gas hydrocarbons in 2013 (4 Oct. 2013); EIA, Oil and gas industry employment growing much faster than total private sector employment (8 Aug. 2013); Reuters, Analysis: Shale oil storm blows U.S. tanker trade out of doldrums by Anna Louie Sussman (1 Jul. 2012); EIA, A number of western states increased oil production since 2010 (21 May 2013); EIA, Abundant U.S. Supply, low demand could cut dependence on liquid fuel imports (17 Apr. 2013); Reuters, Analysis – Texas oil sails to Canada, refiners fume over tanker law by Jonathan Leff and David Shepard (1 May 2013).

Recent Developments in Pre-Judgment Attachments in New York, Maritime and Otherwise

BY THOMAS H. BELKNAP, JR.

THOMAS H. BELKNAP, JR.
PARTNER
TBelknap@BlankRome.com

Following is a brief discussion of some of the more notable recent developments in the New York attachment and garnishment arena. Some of the developments relate to Rule B maritime attachments, and others relate more broadly.

Controlling Law in Rule B Alter Ego Attachments

A recent decision from the Second Circuit Court of Appeals clarified two important points primarily relating to alter ego attachment actions. As many are aware, a plaintiff may obtain a Rule B attachment where it is asserting a "valid *prima facie* maritime claim" against a party who cannot be "found" within the district, but who has an attachable interest in property located within the district. This issue of whether a plaintiff has a valid *prima facie* maritime claim has caused confusion in some cases where the underlying claim is subject to foreign law and will be litigated or arbitrated in a foreign proceeding. In such case, whose law controls the inquiry of whether an attachment is warranted?

That question was answered by the Second Circuit in *Blue Whale Corp. v. Grand China Shipping Development,* 722 F.3d 488 (2d Cir. 2013), which held that the inquiry is actually a two-pronged one, breaking down into whether the claim is "maritime" and whether it is "*prima facie* valid." The first prong is a procedural question—*i.e.,* is the claim within the subject matter of the U.S. federal courts. Thus, federal law always controls that question—*i.e.,* if the claim would be maritime within the meaning of federal maritime law, then it is a maritime claim irrespective of how it may be classified under the foreign law governing the merits of the dispute.

The second prong, however, raises a substantive issue because the ultimate question is whether the claim, as pled, states a valid cause of action under the law that controls the merits of that claim. In many cases, the governing law will be clear from, for instance, a choice of law clause in the governing contract. With an alter ego claim, however, the analysis is not so simple. In such a claim, the plaintiff is contending that a third party—*i.e.,* not the party to the contract or the party actually committing the tort—should have its "corporate veil" pierced because it is no more than the alter ego of the primary defendant. What law should govern such a claim—particularly in the typical situation where the plaintiff and defendant are from different foreign countries and the dispute involves a foreign-flagged vessel carrying cargo to and from foreign ports?

In *Blue Whale,* the Second Circuit concluded that a choice of law clause in the contract should not control, because an alter ego claim is not strictly a claim under the contract but involves the separate question of when one party should be liable for another's obligations. The court also rejected the notion that federal maritime law should always govern the question. Instead, the Second Circuit ruled, a court must conduct a choice of law analysis "by ascertaining and valuing points of contact between the transaction and the states or governments whose competing laws are involved." *Id.* (quoting *Lauritzen v. Larsen,* 345 U.S. 571 (1953)).

In *Blue Whale,* the points of contact implicated no particular jurisdiction, and the court thus weighted most heavily the plaintiff's choice of forum coupled with the situs of property in the forum, and found that federal maritime law should apply. In other situations, however, it is not difficult to see how the analysis could weigh more heavily in favor of another jurisdiction's alter ego law.

Attachment of New York Correspondent Accounts

We have seen a number of recent cases where the plaintiff has sought to attach U.S. dollar funds maintained by a defendant at a foreign bank with a correspondent banking relationship with a New York bank. The premise of the attachment is that that foreign defendant has an attachable property interest in its "share" of its bank's funds maintained with the correspondent in New York.

Thus far, however, we are aware of no decision accepting this argument, and several have rejected it. In *Toisa Ltd. v. PT Transamudra Usaha Sejahtera,* 13 cv 1407 (Sept. 20, 2013) (JMF), the court issued a ruling from the bench concluding that a defendant has no attachable interest in a correspondent's New York account. That ruling relied on a similar conclusion reached by the district judge in *Lauritzen Bulkers A/S v. JIT Int'l Corp. Ltd.,* 13 cv 3982 (Aug. 9, 2013)(WHP), which considered such an attempt essentially analogous to EFT attachments, which had been barred in *Shipping Corp. of India Ltd. v. Jaldhi Overseas Pte Ltd.,* 585 F.3d 59 (2d Cir. 2009).

In *Toisa* the plaintiff sought to rely on *Cargill Financial Services Int'l, Inc. v. Bank Fin. and Credit Ltd.,* 896 N.Y.S.2d 317 (1st Dep't 2010), in support of its position that a defendant had an attachable interest in correspondent funds. *Cargill* involved a claim against a foreign bank itself, and the plaintiff attempted to attach its correspondent account in New York. The court found that the evidence supported such an attachment, but ruled that the district court had not abused its discretion in vacating the attachment since the evidence also established that the funds were held "for the benefit" of third-party customers who used the account to transact foreign business in U.S. currency. This ruling, the plaintiff in *Toisa* argued, supported the conclusion that those third-party clients must themselves have

an attachable interest in the funds. The *Toisa* court rejected this argument, however, concluding that a correspondent bank's holding funds "for the benefit" of customers was not the same as saying they had a property interest in them. Instead, the *Toisa* court relied on earlier rulings in *Sigmoil Resources, N.V. v. Pan Ocean Oil Corp.,* 234 A.D.2d 103 (1st Dep't 1996), and *Sidwell & Co., Ltd. v. Kamchatimpex,* 166 Misc. 2d 639 (Sup. Ct., N.Y. Cty 1995), which had rejected similar attempts to attach funds in a correspondent bank's account. As the *Sigmoil* court noted:

> Neither the originator who initiates payment nor the beneficiary who receives it holds title to the funds in the account at the correspondent bank. *Id.* at 104.

Property Subject to Attachment Under State Law

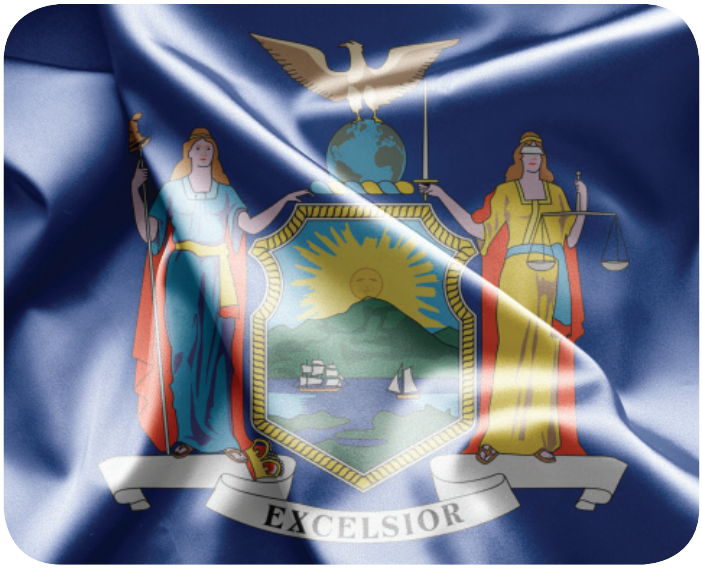
Maritime plaintiffs tend to think only of Rule B when they think of attachment in the U.S., but most states provide their own attachment remedies that may apply in a given case as well. New York is no exception and allows for attachment of a defendant's property in a number of different circumstances. Grounds include where the defendant is a foreign corporation not qualified to do business in the state; where the defendant, with intent to defraud creditors, has hidden or disposed of property or removed it from the state; or where the action is to enforce a foreign judgment.

Another ground that commonly arises in the maritime context is the attachment in aid of arbitration pursuant to C.P.L.R. § 7502(c). That provision allows a party to seek an attachment where it can show that "the award to which the applicant may be entitled may be rendered ineffectual without such provisional relief." Such an attachment may be sought irrespective of whether the arbitration arises under state law, the Federal Arbitration Act, or the New York Convention.

An attachment order issued under New York law can in some instances cast a wider net than one issued under Rule B—particularly where the defendant is subject to the jurisdiction of the New York courts. In *Hotel 71 Mezz Lender LLC v. Falor,* 14 N.Y.3d 303 (2010), the New York Court of Appeals, the state's highest court, noted the distinction between cases where attachment is sought solely to obtain security for a claim and cases where attachment is sought to obtain *quasi in rem* jurisdiction—*i.e.,* to litigate the merits of the dispute against attached property. In the latter category of case, due process concerns dictate that "the following black letter principle must be adhered to: 'where personal jurisdiction is lacking, a New York court cannot attach property not within its jurisdiction.'" *Id.* at 311.

But, "where the court acquires jurisdiction over the person of one who owns or controls property, it is equally well settled that the court can compel observance of its decrees by proceedings *in personam* against the owner within the jurisdiction." *Id.* at 312. Where the court has jurisdiction over the defendant, in other words, it "has jurisdiction over that party's tangible or intangible property, even if the *situs* of the property is outside New York." *Id.*

Where that property consists of a debt, courts have held that "the obligation of the debtor…clings to and accompanies him wherever he goes." *Id.* at 315 (citing *Harris v. Balk,* 198 U.S. 215 (1905) (overruled on other grounds). Thus, if a garnishee owing money to the defendant can be served in New York, that debt can be attached even if the garnishee resides outside the state. The *Hotel 71* court determined that this same rule applies to "uncertificated ownership interests" and thus authorized the attachment of a defendants' interest in several limited liability companies located outside New York where the defendant had submitted to New York jurisdiction as a term of the guaranty under which he was being sued.



The decision in *Mishcon de Reya NY LLP v. Grail Semiconductor, Inc.,* 2011 WL 6957595 (S.D.N.Y. 2011), helps illustrate how a New York court's attachment power may be effectively used. There, the parties entered an agreement by which the plaintiff was to provide certain legal services to the defendant. The agreement provided for arbitration of disputes in New York. Disputes arose, and the plaintiff commenced arbitration and also sought an attachment in aid of arbitration. The property to be attached was a patent owned by the defendant. The defendant opposed the attachment on the grounds that the court lacked jurisdiction over the property since, under New York law, a patent is located where its owner is domiciled—in this case, California.

The court rejected this argument, relying on *Hotel 71*, and concluded that the attachment was valid because the court had jurisdiction over the defendant on the basis of its having agreed to arbitrate disputes under the agreement in New York. Importantly, the *Grail* court rejected the defendant's narrow

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interpretation of *Hotel 71* to suggest that the defendant had to be physically located in New York in order to be subject to attachment of its property outside the state. To the contrary, the court held, the defendant merely needs to be subject to jurisdiction here. *Id.* at n.7.

Koehler and the Separate Entity Rule

Courts have uniformly held that New York attachment rules do not permit a party to obtain a pre-judgment attachment of a defendant's foreign bank account merely because the bank happens to have a branch in New York. Under the so-called "separate entity rule," courts treats each branch of a bank as a separate entity for attachment purposes even if they are all part of the same corporate entity. See *Allied Maritime, Inc. v. Descatrade SA,* 620 F.3d 70, 74 (2d Cir. 2010) (citing cases).

Many thought that the separate entity rule was done away with in post-judgment execution cases after the New York Court of Appeals' decision in *Koehler v. Bank of Bermuda,* 12 N.Y. 3d 533 (2009), which held that a judgment creditor could obtain an order directing a garnishee to turn over property located outside New York so long as the garnishee is subject to jurisdiction here. The cases considering this issue since *Koehler,* however, have been split. Compare *JW Oilfield Equipment, L.L.C. v. Commerzbank AG,* 764 F. Supp. 2d 587 (S.D.N.Y. 2011) (holding separate entity rule did not apply in post-judgment turnover action) with *Shaheen Sports, Inc. v. Asia Inc. co., Ltd.,* 2012 WL 919664 (S.D.N.Y. 2012) (holding separate entity rule does apply).

On January 14, 2014, the Second Circuit Court of Appeals certified this issue for appeal to the New York Court of Appeals in *Tire Engineering and Sistribution L.L.C. v. Bank of China Ltd.,* 740 F.3d 108 (2d Cir. 2014), so perhaps we will have a definitive answer on this question in time for the next issue of *Mainbrace*!

Conclusion

Provisional remedies are a powerful tool and can mark the difference between success and failure in a case. Parties are accustomed to thinking about whether there is property subject to attachment in a given jurisdiction, but in New York, at least, some powerful attachment remedies become available merely because the defendant is subject to jurisdiction here. A party may be subject to New York jurisdiction for many reasons: because it does business here; because it has registered with the Secretary of State; or because it has agreed to litigate or arbitrate disputes in New York. In such cases, it may be well to consider whether there are other attachment remedies available, even if the defendant has no known property in the state. ■

The Evolving Ballast Water Conundrum

BY JONATHAN K. WALDRON, JEANNE M. GRASSO, AND PATRICIA M. O'NEILL

JONATHAN K. WALDRON
PARTNER
Waldron@BlankRome.com

JEANNE M. GRASSO
PARTNER
Grasso@BlankRome.com

The U.S. Environmental Protection Agency ("EPA") recently issued long-awaited guidance regarding the coordination and interplay between the compliance date extensions the U.S. Coast Guard is issuing for ballast water management discharge standards and the EPA's approach to the same under the new Vessel General Permit for Discharges Incidental to the Normal Operation of Vessels ("2013 VGP"). Despite the Coast Guard's authority—and willingness—to grant extensions to its implementation schedule, the EPA confirmed that the implementation date for the 2013 VGP ballast water management standards would not be extended to match those granted by the Coast Guard. While the Coast Guard and EPA maintain a purportedly collaborative approach to addressing ballast water management challenges, the EPA's recent policy represents a split between the co-regulators' respective enforcement approaches. As such, the EPA's divergence with the Coast Guard's policy means that even with a Coast Guard extension, vessel owners/operators will not be in compliance with the 2013 VGP, unless they either install a Coast Guard-authorized Alternative Management System ("AMS"), which may need to be replaced in five years, or they do not discharge ballast water in a U.S. port, thus creating an untenable conundrum for those desiring to be in compliance.

By way of background, on June 21, 2012, the Coast Guard's Ballast Water Discharge Standard Final Rule went into effect, creating new compliance requirements for U.S.-flag and foreign-flag vessels equipped with ballast tanks operating in U.S. waters. In order to discharge ballast water into U.S. waters, vessels are required to use an approved ballast water management method in accordance with a phased-in schedule based on their ballast water capacity. Vessels have five options to comply, none of which are likely practical at this time: (1) installing a Coast Guard type-approved ballast water management system ("BWMS"); (2) installing an AMS; (3) using water from the U.S. public water system; (4) using shoreside reception facilities; or (5) not discharging ballast water in U.S. ports. Alternatively,

vessel owners and operators may request from the Coast Guard an extension to the implementation schedule under certain conditions as there are no Coast Guard type-approved BWMSs—and no guaranty that the AMSs on the Coast Guard's authorized list will ultimately be type-approved.

The other part of the ballast water compliance equation is the EPA's 2013 VGP, effective December 19, 2013, which has its own ballast water discharge standards that are similar, but not identical, to the Coast Guard's standards. In response to industry requests for the EPA to delay its implementation schedule as did the Coast Guard, the EPA issued an "Enforcement Response Policy for EPA's 2013 Vessel General Permit" on December 27, 2013. Unlike the Coast Guard, the EPA refused to extend the implementation date for the 2013 VGP ballast water management requirements to match the extensions granted by the Coast Guard, but rather took a "low enforcement priority approach," leaving vessel owners/operators in a compliance conundrum. Thus, despite being in compliance with the Coast Guard requirements, vessel owners/operators would not be in compliance with the 2013 VGP.

To qualify for the EPA's "low enforcement priority policy," vessel owners/operators must have received an extension from the Coast Guard and must be in compliance with all provisions of the 2013 VGP. In exercising its enforcement discretion, the EPA has stated that it will consider, among other factors, that there is no Coast Guard type-approved technology available. The EPA further explained that although the Coast Guard's decision to grant an extension of the implementing regulatory schedule for the required technology on a particular vessel will be considered by the EPA in enforcement decisions, it is not binding.

Regarding EPA enforcement, where a vessel has received an extension from the Coast Guard and is in compliance with all other provisions of the 2013 VGP except the ballast water discharge limits, the EPA may "take into account" the circumstances under which the Coast Guard issued the extension. In these circumstances, the EPA will "consider such violations of the 2013 VGP ballast water numeric discharge limit a low enforcement priority." The enforcement policy, however, does not apply if there are other VGP non-compliances (without further elaboration) or to situations of "grossly excessive ballast water discharges or those that may present an imminent and substantial endangerment, criminal violations…" "Grossly excessive ballast water discharges" and "imminent and substantial endangerment" clauses are not defined in the policy letter and present even more ambiguity as to what circumstances would lead the EPA to enforce violations of the 2013 VGP.

The EPA's approach here, and failure to act consistent with the Coast Guard, leaves vessel owners/operators with a few options, none of which are desirable: (1) install a Coast Guard authorized AMS, which may need to be replaced in five years if it does not get Coast Guard type-approval in the interim; (2) apply for an individual National Pollutant Discharge Elimination System ("NPDES") permit for each vessel as an alternative to the 2013 VGP, which could take months and be extremely costly while the EPA sorts out how it will handle such applications as EPA regions typically issue individual permits for land-based facilities for coverage in that particular region; or (3) enter into a consent decree following a violation of the 2013 VGP, which would set forth requirements for compliance going forward, but subjecting the vessel owner/operator to possible administrative, civil, or even criminal sanctions.

In summary, the EPA enforcement policy creates a conundrum for vessel owners/operators seeking a viable compliance option. Despite being granted an extension from the Coast Guard, a vessel owner/operator still finds itself in violation of the EPA's 2013 VGP, and is therefore subject to potential enforcement by the EPA and possible citizen suits. Non-compliance could also have significant negative commercial implications if considered in charterer vetting inspections and vessel evaluations. Non-compliance could also lead to possible violations of existing charter party provisions or other commercial agreements that do not allow knowing or intentional regulatory or other violations. And, finally, non-compliance could pose issues with respect to insurance coverage and disclosures for publicly traded companies. While the EPA claims that VGP violations will be a low priority, the bottom line is that low or non-enforcement does not equal compliance—a conundrum indeed. ■

Patricia O'Neill is an associate in Blank Rome's Washington, D.C. office. [PONeill@BlankRome.com]

Blank Rome WELCOMES

21 Attorneys to the Firm's West Coast and New York Offices

Blank Rome LLP is pleased to announce that twenty-one attorneys, including five partners along with professional staff from the law firms of Margolis & Tisman LLP and Finestone & Richter, joined the Firm on February 1. As a result of these additions, the Firm has significantly expanded its Los Angeles office, established an office in San Francisco, and enhanced its New York office.

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2029 Century Park East
6th Floor
Los Angeles, CA 90067
424.239.3400

601 Montgomery Street
Suite 2030
San Francisco, CA 94111
415.986.2144

JOINING FROM MARGOLIS & TISMAN

Michael ("Mike") B. Margolis, Partner

CORPORATE LITIGATION GROUP

424.239.3839 (Los Angeles)
MMargolis@BlankRome.com

Mr. Margolis has more than 30 years of experience representing clients in a variety of disputes, including trade secrets, unfair competition, and misappropriation of intellectual property; fraud; international joint ventures; employment matters; real estate; lender liability; and class actions and other complex commercial cases. In addition to his dispute resolution practice, he counsels businesses and business owners on a wide range of international and domestic issues. Mr. Margolis is conversational in Mandarin Chinese.

Stephen E. Tisman, Partner

LABOR AND EMPLOYMENT AND CORPORATE LITIGATION GROUPS

212.885.5581(New York)
STisman@BlankRome.com

Mr. Tisman focuses his practice on complex corporate and employment litigation and on employment and corporate business matters for domestic and international clients. He also represents senior executives in a variety of industries, including financial services, insurance, and pharmaceuticals in litigated and contractual matters. Mr. Tisman has litigated in virtually all of the courts of New York and in state and federal courts throughout the U.S. He has practiced before state and federal administrative agencies and has brought and defended arbitrations before the American Arbitration Association, the New York Stock Exchange, and the Financial Industry Regulatory Authority and its predecessor, the National Association of Securities Dealers.

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Timothy J. Martin, COUNSEL, CORPORATE LITIGATION GROUP
Adam W. Schorr, COUNSEL, CORPORATE, M&A, AND SECURITIES GROUP
Linda M. Toutant, COUNSEL, CORPORATE LITIGATION GROUP
Shirley M. Kong, ASSOCIATE, CORPORATE LITIGATION GROUP

SAN FRANCISCO

Naki Margolis Irvin, COUNSEL, CORPORATE LITIGATION GROUP
Robert M. Lieber, COUNSEL, LABOR AND EMPLOYMENT GROUP
Kimberly L. Owens, COUNSEL, LABOR AND EMPLOYMENT GROUP

NEW YORK

Valerie D. Ringel, COUNSEL, LABOR AND EMPLOYMENT GROUP
James F. Parver, COUNSEL, CORPORATE LITIGATION GROUP

JOINING FROM FINESTONE & RICHTER

Jeffrey R. Richter, Partner

CORPORATE, M&A, AND SECURITIES GROUP

424.239.3870 (Los Angeles)
JRichter@BlankRome.com

Mr. Richter advises public and private companies ranging from start-ups to well-established corporations on a wide variety of business matters involving mergers and acquisitions, general corporate and commercial transactions, securities law, and dispute resolution. He has more than 40 years of experience involving the sale of assets, the sale of capital stock or other securities, mergers and related transactions relating to the transfer of control of corporate or other entities, and representing buyers and sellers in connection with transactions for small, mid-cap, and large businesses. He also provides counsel to tax-exempt organizations, including public charities and educational institutions.

William Finestone, Partner

TAX, BENEFITS, AND PRIVATE CLIENT GROUP

424.239.3868 (Los Angeles)
WFinestone@BlankRome.com

Mr. Finestone concentrates his practice in the area of trusts and estates, with particular emphasis on estate and tax planning and estate and trust administration. He has more than 40 years of experience in the preparation of wills, revocable and irrevocable private trusts, charitable trusts, durable powers of attorney for financial and healthcare matters, and business succession planning. He advises clients on estate and trust administration matters involving probate and non-probate procedures as well as the resolution of disputes involving wills and trusts. In tax planning matters, Mr. Finestone advises clients in the areas of United States, California, and international transfer tax planning; corporate, partnership, and individual income tax planning; and property taxation.

ATTORNEYS JOINING MR. RICHTER AND MR. FINESTONE IN LOS ANGELES

Eric F. Edmunds, Jr., COUNSEL, CORPORATE LITIGATION GROUP
Mark Kalisch, COUNSEL, CORPORATE, M&A, AND SECURITIES GROUP
Nancy B. Lamell, COUNSEL, CORPORATE, M&A, AND SECURITIES GROUP
Christopher Tesar, COUNSEL, CORPORATE, M&A, AND SECURITIES GROUP
John J. Waller, Jr., COUNSEL, CORPORATE LITIGATION GROUP
Susan A. Wolf, COUNSEL, CORPORATE, M&A, AND SECURITIES GROUP
Arthur P. Yoon, COUNSEL, CORPORATE, M&A, AND SECURITIES GROUP

Matthew J. Thomas Joins Blank Rome's Maritime, International Trade, and Public Contracts Group

Matthew J. Thomas

WATERGATE

600 New Hampshire Avenue NW
Washington, DC 20037

202.772.5971(Voice)
202.772.1672 (Fax)

MThomas@BlankRome.com

Matthew J. Thomas has joined Blank Rome's Washington, D.C. office as a partner in the maritime, international trade, and public contracts group.

Mr. Thomas has more than twenty years of experience in maritime and international trade regulation and government affairs, representing leading shipowners, energy and trading companies, ports, P&I clubs, shipyards, and marine terminal operators.

He works extensively in the areas of trade sanctions and export controls, particularly with fast-moving Iran policies and related banking and insurance matters. His OFAC sanctions work has included issues as diverse as delisting blocked parties, licensing for Cuban oil spill recovery services, Libyan rebels' supplies, and piracy ransom payments. He also represents major energy and trading companies with regard to export controls, customs, and maritime regulation for U.S. crude and petroleum products. In addition, he acts as regulatory counsel for leading container carriers and marine terminal operating companies, and guides global offshore energy companies in maritime and export compliance matters.

Throughout his career, Mr. Thomas has built strong relationships with U.S. government officials, trade associations, and the local legal and lobbying community. He guides international businesses in their dealings with the Departments of State, Treasury, Commerce, Transportation, as well as independent regulatory agencies and Congress.

Prior to joining Blank Rome, Mr. Thomas was a maritime attorney at Am Law 100 and 200 firms; served as the Assistant General Counsel for International Affairs at the Federal Maritime Commission; and worked as a federal lobbyist.

Mr. Thomas is admitted to practice in the District of Columbia. He received his Juris Doctor and Bachelor of Arts from the University of Virginia. Mr. Thomas is a member of the Connecticut Maritime Association, and a member and past President of the Maritime Administrative Bar Association in Washington, D.C. ■

Congress Funds the Agencies and Looks Ahead to FY2015

BY JOAN M. BONDAREFF

JOAN M. BONDAREFF
OF COUNSEL

Bondareff@BlankRome.com

For the first time in many years, Congress actually enacted 12 appropriation bills to fund the Federal Government through September 30, 2014. This was done in the Consolidated Appropriations Act, 2014 (Pub.L. 113-76). As a result, the federal maritime and transportation agencies have the budgets they need to get some important work done. The following is a summary of the key provisions of the FY2014 budget. A forecast of where Congress is going this year in regards to major maritime legislation will be included in the conclusion of this article.

Highlights of the FY2014 Budget Agreement

Congress enabled the passage of the Consolidated Appropriations Act by first passing the Bipartisan Budget Act (Pub.L. 113-67). The Bipartisan Budget Act established the overall funding limits for the federal government for 2014-2015. The Budget Act also represents the first time in four years that Congress has actually passed a budget agreement. The budget was negotiated between Senator Patty Murray (D-WA) and Cong. Paul Ryan (R-WI), the respective chairs of the Senate and House Budget Committees. As the two leaders have publicly stated, they worked off the art of the possible, not what they knew they couldn't reach agreement on.

From the levels set in the budget agreement, the appropriation committees could perform their jobs—funding the federal government at least for FY2014. Below are some of the highlights of the Consolidated Appropriations Act.

THE DEPARTMENT OF TRANSPORTATION

- $600M for capital investments in surface transportation infrastructure—the so-called TIGER grants—to fund infrastructure projects of regional and national significance, including a set-aside of $35M for planning grants.

U.S. MARITIME ADMINISTRATION:

- $186M for the Maritime Security Program to preserve the U.S. flag merchant fleet;
- $38.5M for the subsidy cost of title XI loan guarantees for shipbuilding; and
- $16M for the U.S. Merchant Marine Academy and $11.3M for the state maritime academies.

Infrastructure projects at ports are eligible for the TIGER program and, on average, have received about 10 percent of the funding to date. Setting aside money for planning grants is a new allocation for the TIGER program. Finally, funding the title XI program represents a new infusion of cash for the shipbuilding loan guarantee program. With a subsidy amount of 10 percent, this will enable the Maritime Administration to fund close to $400M in new shipbuilding loans. With a new (Acting) Administrator at the helm of the Maritime Administration, one hopes that the title XI program is resuscitated and the cumbersome review procedures streamlined.

THE DEPARTMENT OF HOMELAND SECURITY

FEMA:

- A total of $1.5B for grants, contracts, and cooperative agreements, including $466.3M for the State Homeland Security ("HLS") Grant Program, $600M for the Urban Area Security Initiative, and $100M for port security grants.

Ports, with the support of the American Association of Port Authorities ("AAPA"), successfully fought back against the Administration's proposal to consolidate all HLS grants into one block grant to states, fearing they might not get their fair share from state agencies. Although $100M is considerably less than the $400M authorized for these grants in the Maritime Transportation Security Act of 2002, at least it gives ports a separate bucket to shoot at.

U.S. Coast Guard:

- A total of $1.375B for acquisition, construction, and improvements, including the cost of production of the 7th National Security Cutter ("NSC") and the contract for long-lead time materials for the 8th NSC. (Huntington Ingalls has the contract for long-lead time materials for the 7th NSC.)

Admiral Papp, Commandant of the Coast Guard, has hinted that he is looking to fund the 8th (and final) NSC in the FY2015 budget, continue work on the Offshore Patrol Cutter, and perhaps start work on a new icebreaker in the FY2015 budget. (As reported in *Seapower Magazine* on January 24, 2014.) With the Coast Guard's newly released Arctic Strategy, it makes sense to look at its icebreaking capabilities. (For a copy of the Strategy, see: www.uscg.mil/seniorleadership/DOCS/CG_Arctic_Strategy.pdf.)

Customs and Border Protection ("CBP"):

- A total of $10.6B for security, enforcement, and investigations, including $351M for border security fencing and $805M for air and marine operations. This budget will enable CBP to add 2,000 more agents at U.S. ports of entry. (And they say we don't spend enough on border security!)

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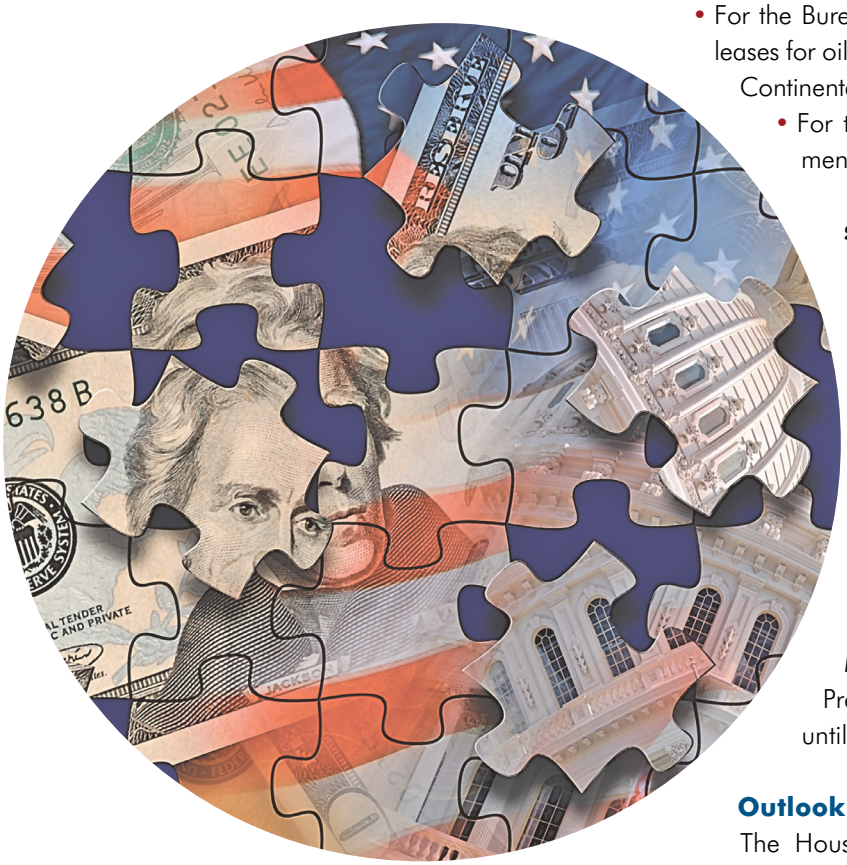

THE DEPARTMENT OF DEFENSE

U.S. Navy:

- A total of $15B for shipbuilding and conversion of naval vessels, to remain available until obligated until September 30, 2018, provided no funds for construction are spent in a foreign yard.

U.S. Army Corps of Engineers:

- A total of $1.656T (from the Harbor Maintenance Trust Fund) to remain available until expended for the construction of river and harbor, flood and storm damage reduction, shore protection, and restoration. The Secretary of the Army may initiate up to four new construction starts (three for navigation, one for environmental restoration), provided the Secretary sends Congress a report on out-year funding for the new starts.

THE ENVIRONMENTAL PROTECTION AGENCY

- $20M in clean diesel engine or Diesel Emissions Reduction Act ("DERA") grants.

These grants can be used by private companies and public transit agencies to purchase new diesel engines or to upgrade existing ones and are funded through a coalition of regional and nonprofit entities. (For more information on the DERA Program, see www.epa.gov/diesel/grantfund.htm.)

THE DEPARTMENT OF THE INTERIOR

- For the Bureau of Ocean Energy Management: $166.8M for leases for oil and gas, other minerals, and energy on the Outer Continental Shelf ("OCS").
- For the Bureau of Safety and Environmental Enforcement: $122.7M for regulation of activities on the OCS.

SUMMARY OF THE FY14 BUDGET AGREEMENT AND OUTLOOK FOR FY2015

Now that agencies have budgets that last through FY2014, they can begin to plan, issue contracts, and begin to award grants. The Department of Transportation ("DOT"), Department of Homeland Security ("DHS")/ Federal Emergency Management Agency ("FEMA"), and Environmental Protection Agency ("EPA") all have grant-making authority.

The White House will submit its FY2015 budget request to Congress the first week of March 2014. In the meantime, Congress sent the President a clean bill raising the debt limit ceiling until March.

Outlook for Other 2014 Congressional Actions

The House-Senate Conference on the Water Resources Development Act ("WRDA"), which funds port dredging and maintenance, is still underway despite this author's predictions it would be wrapped up by now. Cong. Bud Shuster, Chairman of the House Transportation and Infrastructure ("T&I") Committee, admitted (at a recent Bloomberg Government conference) that it's been "slow going." The passage of funding for the Army Corps of Engineers, above, may have taken some pressure off this Conference.

On February 11, 2014, the House T&I Committee ordered reported H.R. 4005, the "Coast Guard and Marine Transportation Act of 2014," with a manager's amendment. The amendment included new cargo preference requirements. We will address these amendments in detail in a separate advisory. Any urgent maritime problem that needs a legislative fix should be addressed in this major maritime legislation, which Congress usually passes every two years.

Chairman Shuster and the Administration have both begun work on principles for the next surface transportation bill. The current law—Moving Ahead for Progress in the 21st Century Act, commonly referred to as MAP-21—expires this coming September. The main issue for reauthorization is how to fund the Highway Trust Fund. Congress balked last time and is very reluctant to get near an increased gas tax, especially in an election year. In fact, both Chairman Shuster and Chairman Barbara Boxer (of the Senate Environment and Public Works Committee)

have written off the gas tax increase as a funding solution for "MAP-22." Other options include use of repatriated overseas revenues and a user fee based on vehicle miles travelled (or "VMT"). It will be up to the Ways and Means Committee in the House and the Senate Finance Committee to determine how to fund the next round of surface transportation projects.

While the surface transportation bill is largely focused on roads and bridges, there is an increasing focus on a national freight network. The current freight network, which is under review at the DOT, is limited to highways and needs to be expanded to include ports. Even the President in his State of the Union Address identified the need to upgrade our ports. After all, how do goods come into and out of the U.S., except through our ports?

This year is an election year, so it remains to be seen how many difficult issues the 113th Congress will address before the election. Hope is higher for actions on controversial issues, such as taxes and tax reform, during the lame duck session—both post-election and before the new Congress is sworn in. This may provide the window needed to pass a Coast Guard authorization bill, a new surface transportation bill, and even perhaps some type of immigration reform bill.

Finally, the Bipartisan Budget Agreement, with its cap on FY2015 spending, will facilitate Congressional passage of FY2015 appropriation bills. We may see a return to the passage of 12 appropriation bills as we did in FY2014. ■

If You Want Contribution, Get the Third Party Released

BY JEFFREY S. MOLLER

JEFFREY S. MOLLER
PARTNER

Moller@BlankRome.com

The maritime version of "Murphy's Law" can be a potential trap for participants in maritime tort litigation. The decision of the 11th Circuit Court of Appeals in *Murphy v. Florida Keys Electric Co-op Assoc., Inc.,* 329 F.3rd 1311 (11th Cir. 2003) enunciated the rule that in order to preserve the right to pursue third parties for tort "contribution," a party must negotiate a release of those third parties when settling the underlying claim brought by the tort victim. The law enounced by the *Murphy* court was based upon the proportionate fault rule existing in the maritime law and the *pro rata* credit rule established by the U.S. Supreme Court in *McDermott, Inc. v. AmClyde, et al.,* 511 U.S. 202 (1994). The logic of this version of Murphy's Law is that a settling tortfeasor is, per *McDermott,* deemed to have paid the tort victim only in accordance with the settlor's own proportionate share of fault. The settlement extinguishes the rights (and needs) of non-settling tortfeasors to pursue the settlor because it coincidentally limited the non-settlors' liability—despite the doctrine of "joint and several liability"—to their own proportionate faults. The *Murphy* case held that unless the release negotiated between the settlor and the tort victim also releases the tort

The decision of the 11th Circuit…in *Murphy*…enunciated the rule that in order to preserve the right to pursue third parties for tort "contribution," a party must negotiate a release of those third parties when settling the underlying claim brought by the tort victim.

victim's claims against the non-settlors, the settlor is presumed to have paid only for its proportionate share and cannot seek contribution from others.

This rule has subsequently been adopted by the Fifth Circuit Court of Appeals in *Ondimar Transportes Maritimos v. Beatty Street Properties, Inc.,* 555 F 3rd 184 (5th Cir. 2009). The Fifth Circuit has also gone so far as to say that a formal assignment of claims from the tort victim to the settlor would not remedy the situation. See also, *Lexington Insurance Company v. S.H.R.M. Catering Services, Inc.,* 2009 US. App. Lexis 9447 (5th Cir. 2009).

Recall that the *McDermott v. AmClyde* case arose from a situation where one of the named defendants to a lawsuit had settled, but the case continued on against remaining named defendants. The question was how much settlement credit should be afforded to the remaining defendants. Given the existence in U.S. maritime law (since the *Reliable Transfer* case) of a tort system of proportionate fault, the Supreme Court decided in *McDermott* that the verdict against the remaining defendants would not be reduced simply by the dollar amount paid by the settlor, but would be reduced instead by the proportion of fault eventually attributed to the settlor by the fact finder, be it judge or jury. This rule made it unnecessary for the non-settling defendants to keep alive their cross-claims for contribution against the settlor, thereby assuring that the settling defendant had terminated its involvement in the lawsuit with finality. At the same time, the tort victim would get fair compensation.

The 11th Circuit Court in *Murphy* recognized that if, under *McDermott,* the settling defendant is deemed to have only paid his proportionate share or fault, he can have no reason to seek

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contribution from others. The right to contribution is purely and primarily a creature of the maritime law rule of joint and several liability, under which the plaintiff is free to collect the entirety of its verdict from any one of the tortfeasors who proximately caused his harm. If a tortfeasor is forced by that rule to pay for more than its proportionate share, the right of contribution exists to allow him to collect contribution from the other tortfeasors in accordance with their determined shares. But the *McDermott* presumption means that the paying entity is not entitled to contribution because it did not pay more than his fair share.

There are various ways in which this rule can hurt the unwary, particularly in situations where, for one reason or another, all potential tortfeasors cannot be joined by the victim in one action. For example, where a cargo owner is bound per the terms of a bill of lading to bring an action against the carrier in a foreign arbitration forum, potential additional tortfeasors such as the loading or discharging stevedores, packaging companies, or truckers could not be brought into the arbitration forum against their will. If the cargo owner and carrier effect a settlement, the carrier may have hopes of bringing suit at a later date to recover some portion of the settlement amount it was required to pay to the cargo owner. Unless the carrier obtains a release of the cargo owner's claims against the prospective contributors, however, the carrier will be presumptively deemed to have paid to the cargo owner only an amount relative to its (the carrier's) own proportionate fault. The carrier could not, therefore, sue a loading stevedore or trucker for contribution, even if the carrier obtained a formal legal assignment of the cargo owner's claims. Another example might be a Jones Act claim brought by a seaman for personal injury suffered during the course of his employment. If such action is brought in a federal district court in which other potential contributors are not subject to jurisdiction, the vessel owner/employer cannot expect to later obtain contribution from any third parties unless the seaman has released his/her claims against them, indicating that the vessel owner paid for not only its own proportionate share of fault, but also additional amounts on behalf of other tortfeasors.

Of course, contribution's fraternal twin cause of action is indemnification. Neither *Murphy, Ondimar,* nor *McDermott* serve to forbid the pursuit of indemnification from an unreleased non-settlor, and there would seem to be no logical reason why those rules should be extended. (Of course, the famous words of Justice Oliver Wendell Holmes, Jr. to the effect that "the life of the law has not been logic; it has been experience" might counsel against relying upon logical extension.) The theoretical basis of the right of indemnification differs greatly from that underlying the right of contribution. A settling tortfeasor might be forced to pay the full amount of a claim by virtue of its relationship with the claimant and might have a contractual or quasi-contractual right of full indemnification from a third party. In such a case, the payor would not be limited to a mere contribution claim and would not be deemed or presumed to have paid only in accordance with its own proportionate fault. Maritime law recognizes several types of indemnity, both contractual and quasi-contractual and, in tort, via the so-called active/passive construct. For example, a vessel owner might be liable to a seaman for injuries arising as a result of an unseaworthy condition on the vessel. If that condition was caused to occur by the failure of an expert stevedore or contractor to live up to its warranty of workman-like performance, the vessel owner could seek indemnification from the stevedore or contractor without having secured a release for them from the seaman.

Therefore, if one should find oneself in a situation of wanting to recover monies paid in the settlement from parties that were not able to be drawn into the initial claim process, one could assert claims for indemnification even if the third parties had not been released by the original claimant. Seeking indemnity would, in this instance, be a way to avoid the effect of the maritime law's version of Murphy's Law. ■

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HOUSTON +.713.228.6601	OFFICE PHONE	MOBILE PHONE	EMAIL
Michael K. Bell	+1.713.402.7630	+1.713.385.7630	MBell@BlankRome.com
Keith B. Letourneau	+1.713.402.7650	+1.713.398.8129	KLetourneau@BlankRome.com
Douglas J. Shoemaker	+1.713.402.7645	+1.713.446.7463	DShoemaker@BlankRome.com
Mitchell R. Machann	+1.713.402.7635	+1.713.816.3717	MMachann@BlankRome.com
Wm. Tracy Freeman	+1.713.402.7636	+1.713.724.0870	WFreeman@BlankRome.com
David G. Meyer	+1.713.402.7654	+1.713.289.4289	DMeyer@BlankRome.com

NEW YORK +1.212.885.5000	OFFICE PHONE	MOBILE PHONE	EMAIL
John D. Kimball	+1.212.885.5259	+1.973.981.2106	JKimball@BlankRome.com
Richard V. Singleton II	+1.212.885.5166	+1.732.829.1457	RSingleton@BlankRome.com
Thomas H. Belknap, Jr.	+1.212.885.5270	+1.917.523.4360	TBelknap@BlankRome.com
Alan M. Weigel	+1.212.885.5350	+1.860.334.7431	AWeigel@BlankRome.com
William R. Bennett III	+1.212.885.5152	+1.646.393.7847	WBennett@BlankRome.com
Jeremy A. Herschaft	+1.212.885.5254	+1.504.236.9726	JHerschaft@BlankRome.com
Lauren B. Wilgus	+1.212.885.5348	+1.732.672.7784	LWilgus@BlankRome.com

PHILADELPHIA +1.215.569.5500	OFFICE PHONE	MOBILE PHONE	EMAIL
Jeffrey S. Moller	+1.215.569.5792	+1.215.630.0263	Moller@BlankRome.com

WASHINGTON, DC +1.202.772.5800	OFFICE PHONE	MOBILE PHONE	EMAIL
Jeanne M. Grasso	+1.202.772.5927	+1.202.431.2240	Grasso@BlankRome.com
Gregory F. Linsin	+1.202.772.5813	+1.202.340.7806	Linsin@BlankRome.com
Matthew J. Thomas	+1.202.772.5971	+1.301.257.6369	MThomas@BlankRome.com
Jonathan K. Waldron	+1.202.772.5964	+1.703.407.6349	Waldron@BlankRome.com
Patricia M. O'Neill	+1.202.772.5825	+1.609.760.2566	PONeill@BlankRome.com

Blank Rome Maritime is ranked top tier in Shipping for Litigation, Regulatory, and Financing in *Chambers USA* and recognized as a leading maritime law firm in *Who's Who Legal*.
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