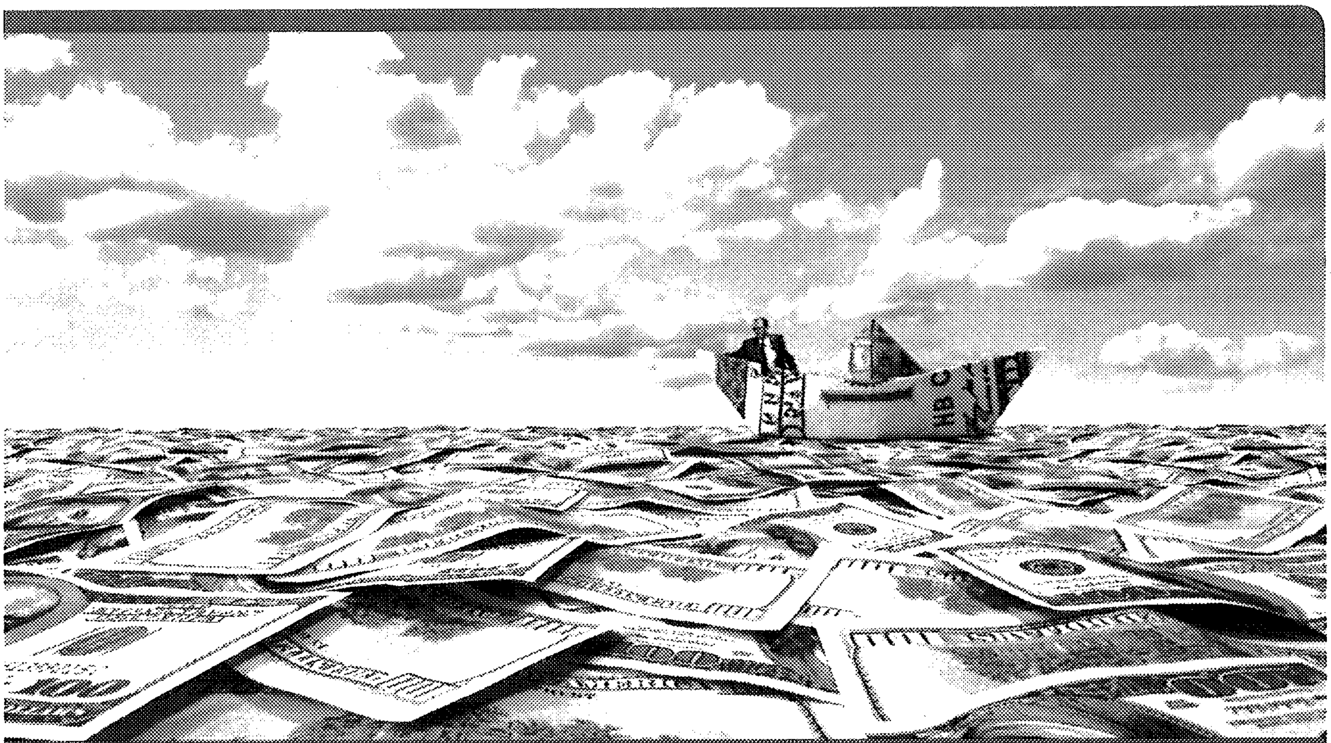

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It's TIME TO CHANGE the Capital Construction Fund program for the better

Program's restrictions limit value for Gulf of Mexico OSV operators, builders

By H. Clayton Cook, Jr., of Counsel, Seward & Kissel LLP

Title XI Loan Guarantees and Capital Construction Fund (CCF) tax deferrals are all that remain of the 1936 and 1970 Merchant Marine Act programs that were intended to support U.S. operators in international trades. The 1970 Act CCF program was intended to create opportunities for U.S. operators in international trades by "leveling the 'tax' playing field." Its Congressional sponsors believed it to be the most important of the Nixon Administration 1970 Act legislative proposals.

U.S.-based offshore service vessel owner-operators and Gulf of Mexico shipyards serve what is perhaps the most robust of the U.S. maritime sectors, and account for as many as two-thirds of the U.S. Maritime Administration (MarAd) CCF program agreements. MarAd has ruled that the CCF program financed offshore support and platform supply vessels (OSVs) are CCF "qualified agreement vessels" and that OSV services from U.S. locations, in essentially domestic trades, are CCF "permissible operations."

However, if an OSV owner-operator wishes to compete with foreign-registered OSVs at non-domestic locations, MarAd regulations deny this "permissible" characterization, and treat these services as "nonqualified operations" that require the payment of liquidated damages." And, if CCF funding was used in the construction of the OSV, or within one year after the shipyard sale, the shipyard, the initial purchaser, the current owner (and all of the vessel owners in the chain of title) can be held liable for these liquidated damages payments at any point during the OSV's 20-year useful life.

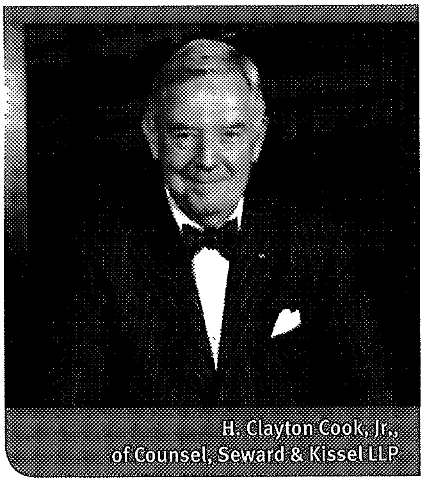
U.S.-based OSV owners provide services in the Gulf of Mexico and at locations around the world. When Shell Oil Company calls to request PSV services for a project in Indonesia, the owner delivers—if it wishes to remain a preferred provider. But, the U.S. owner will be subject to MarAd "liquidated damages" if the PSV to be used has been financed with MarAd CCF monies. So the OSV owners may need to forego CCF program use in order to maintain needed business flexibility. These liquidated damages provisions have also limited participation in the CCF program by Gulf Coast OSV shipyards because of owner reluctance to purchase vessels that cannot be moved to foreign operations without an exposure to MarAd liquidated damages.

And, these are the very Gulf Coast shipyards and vessel owners for which MarAd should be facilitating CCF program use, to finance new Gulf Coast vessel construction for OSV owners that are in expansion mode as they move their vessels between U.S. and international operations to maximize vessel employment opportunities.

MARINE LOG currently lists U.S. Gulf Coast shipyards as having more than 60 PSVs under construction or under contract and scheduled for construction. It does not appear that a single one of these PSV projects is using MarAd CCF financing. And, several major Gulf Coast shipbuilders advised me that they cannot use the CCF program to fill out vessel series or otherwise for their own accounts, because of these liquidated damages provisions.

OSV owners and shipyard interests, and MarAd CCF program interests, are best served when the OSV owner is allowed to manage its vessels in a fashion that will maximize the owner's return on its investment. If an owner withdraws a CCF financed vessel from a U.S.-based Gulf of Mexico service for more profitable employment elsewhere, one must assume that if the Gulf of Mexico need remains, the owner will use its CCF program funds to build a replacement vessel for the U.S. based need.

MarAd could solve this liquidated damages problem with an internal rulemaking as part of the current Department of Transportation, Retrospective Review of Regulations program. There are significant opportunities for our U.S. OSV owners in a changing Gulf of Mexico situation and in other markets worldwide. An "unfettered" CCF program would allow our U.S. owner-operators to build vessels to meet these. MarAd should act to remove this liquidated damages impediment to CCF program use and encourage U.S. shipbuilders and OSV owners the full use of this proven funding mechanism. ■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About the author

H. Clayton Cook, Jr. is completing a decade of service as Seward & Kissel's U.S. flag special counsel. Clay began his professional career in New York City with Sullivan & Cromwell. He then served as Sun Oil Company's senior tax counsel prior to his appointment as General Counsel of the U.S. Maritime Administration. At MarAd, Clay oversaw the drafting of the regulations and contract forms implementing the Merchant Marine Act of 1970, and the drafting of the Title XI program Federal Ship Financing Act of 1972. He was MarAd's lead representative in the Internal Revenue Service negotiations and drafting of the 1970 Act CCF joint tax regulations. And he served as Deputy U.S. Delegation Chief in the negotiations for the U.S./U.S.S.R. 1973 Maritime Agreement.

Clay has advised clients in the construction, ownership and financing of more than $4 billion in U.S. built vessels for the Jones Act and U.S. international trades. His work has included CCF use in a variety of vessel leveraged lease financings, in achieving the first two U.S. "pure shipyard" CCF awards, and in the development of a computer methodology for "benefits sharing" projects for the Navy's DUV program that is now protected under U.S. Patent No.: US 8,010,431 B1.

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