

# SEWARD & KISSEL LLP

United States House of Representatives  
Committee on Armed Services  
Subcommittee on Seapower and Expeditionary Forces  
Honorable Gene Taylor, Chairman

Testimony regarding  
Maritime Administration  
Title XI Loan Guarantee Program  
March 15, 2007

Submitted by  
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OPENING STATEMENT

Chairman Taylor and Members of the Subcommittee on Seapower and Expeditionary Forces, thank you for inviting me to testify this afternoon.

My name is Clayton Cook. I am Counsel to Seward & Kissel LLP, a New York City based law firm founded in 1890 that is an internationally recognized leader in U.S. flag vessel finance.

I served as General Counsel of the Maritime Administration from 1970 through 1973. I was responsible for the legal aspects of the implementation of the Merchant Marine Act of 1970, and for the drafting of the Federal Ship Financing Act of 1972, which governs MarAd's current Title XI program.

These two Acts ushered in the most successful period of commercial shipbuilding in U.S. history. The Title XI program was critical to this shipbuilding success. The Title XI program properly funded and managed could play a similar critical role in the successful financing of the Container and Ro/Ro vessels needed today for our American Marine Highways.

I am here to testify today in support of a properly funded and managed Title XI program. With your permission, I am submitting my printed statement for the record. I will be pleased to answer any questions that you and the Committee Members may have.

Thank you.

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## TESTIMONY

Good afternoon, Mr. Chairman and Members of the Subcommittee. Thank you for inviting me to appear before you today to discuss the Maritime Administration ("MarAd") federal loan guarantee program administered under Title XI of the Merchant Marine Act, 1936, as amended (46 U.S.C. 53701). Your invitation stated that you were particularly interested in my views on the availability of Title XI program guarantees for vessel construction period financing, and more generally, with the Title XI program's desirability for long-term post-delivery vessel financing as compared with that which is available in the commercial market.

I plan to first discuss these two subject matters, and thereafter turn to a more general discussion of the Title XI program and my suggestions for several modest "course corrections."

### 1.0 Construction Period Financing.

The "shipyard risk" associated with a shipyard's successful completion of a vessel under construction is perhaps the most difficult financing problem that vessel purchasers face in any transaction. Financial institutions are loath to assume shipyard risk even when bonding may be available. In situations in which the shipyard has a sufficiently robust parent, the shipyard's parent may provide or guarantee this financing or bonding, and the purchaser's problem can be accordingly solved.

However, there are many excellent, small and medium sized United States shipyards that cannot provide this financing or obtain bonding, or find the impact of bonding on their vessels delivered price prohibitive. These shipyards should be participants in the construction of the Passenger and Ro/Pac ferries needed for transportation on our American Marine Highways. This is the very sort of problem -- for which no adequate private sector solution is available -- which the MarAd Title XI program should address.

MarAd has provided these financing guarantees in the past. However, this is now a market from which MarAd, chastened by its many critics, has itself largely withdrawn. Congress should address this problem by directing MarAd to meet this need by making use of the Title XI program in some fashion. Perhaps this can be done by MarAd in a context of shipyard pre-certification, and MarAd assistance in whatever bonding or re-insurance arrangements may be required. But there is a clear role for a MarAd solution to this problem. It is needed. And, I would suggest that the solution to this problem should be addressed in connection with your Committee's current legislative efforts.

## 2.0 Long-Term Permanent Financing.

There is general agreement upon the need for a national transportation policy that will include the use of our Great Lakes and Ocean Coastal waters. But where are the Container and Roll-on /Roll-off ("Ro/Ro") vessels that will be needed? How is this to be achieved? Many of us believe that the principal problem is the absence of available financing.

In some circles today it is common parlance that there is adequate long term private sector financing available for new vessel construction such that there is no need for the MarAd Title XI program. This is true today, as it has been for many years, in financing new vessel construction for tankers with long term charters with companies like Shell Oil Company and British Petroleum in the petroleum sector. In my law practice, I have been professionally involved in such petroleum sector vessel financing for more than 30 years.

However, this is not true for the new Container and Ro/Ro vessels that are needed in our Great Lakes and Ocean Coastal trades. These vessels have and will cost in the range of \$150 million to \$250 million per vessel. The owners of these vessels will have no long term charters, but will be in "build the ships and customers will come" situations. There will be no 20 year or 25 year vessel financing without a Title XI program or some similar government guarantee or credit support program (except in the very unusual situation of a strong parent company guarantee).

And, this is apparently also true for the less costly fast passenger and light vehicle ferries such as the Lake Express service across Lake Michigan and the Hawaii SuperFerry inter-island projects, which are "build the ships and the customers will come" transactions. Hawaii SuperFerry Chairman John Lehman, and Lake Express President Kenneth Szallai, have each publicly stated that the Title XI program was an essential element of their vessel financing structures.

## 3.0 General Discussion: Current Problems & Solutions.

### 3.1 American Marine Highways.

I believe that everyone in this room today will agree that many of our major Interstate Highways, and their bridge and tunnel connectors, are at or have already materially exceeded their design capacities. We will also agree that the major and ever worsening congestion problems that we are experiencing can no longer be solved by new highway, or bridge or tunnel

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construction. And, at the same time, we see our Great Lakes and Ocean Coastal waterways, our American Marine Highways, empty of the passenger and cargo vessels that might provide a part of the solution to these congestion problems. Where are the vessels and how are we to achieve a solution?

I am here today to testify to the essential role that the MarAd Title XI program has played during the past 35 years in financing Container and Ro/Ro vessels for our existing U.S. flag blue water fleet. And, I suggest to you that with certain minor "course corrections" this same MarAd Title XI "public sector/private sector partnership" can play a similarly important role in providing construction period and long-term permanent financing for the vessels that will be needed in the coming decades to transport our citizens and freight on our American Marine Highways.

We can see clearly before us these available empty "highways." But we also have before us a MarAd Title XI financing guarantee program – a public sector private sector "partnership" program - that can facilitate the private sector financing for the needed vessels, once this program is redirected and refocused with leadership provided by this Congress.

### 3.2 History & Current Program Application.

The MarAd Title XI program was added to the basic Merchant Marine Act, 1936, package when the 1936 Act sponsors recognized that some form of U.S. government credit support would be essential to achieving the 1936 Act objectives. It has been an important element in the financing of large ocean going U.S. flag vessels almost since its 1938 "Mortgage Insurance" beginnings.

Over the years, the Title XI program has been employed in the financing of Great Lakes and Non-Contiguous Trade vessels needed to provide essential national transportation services. As originally enacted in 1938, and as incorporated in the 1970 Act program and redesigned in the Federal Ship Financing Act of 1972, the Title XI program was intended for use in financing vessels employed in essential transportation services in peacetime and that would be available to meet national defense needs in time of war.

It was only in 1972 that MarAd abandoned this policy, and that the Title XI guarantee authority was first used to finance the construction of drilling vessels and other non-transportation assets. I would suggest that your Committee should consider the return of the Title XI program to its original purposes. MarAd should administer the program in a fashion that

will achieve the Congressional policy as stated in the 1936 Act and the 1970 Act, and limit the program use to new vessel construction and closely related objectives.

Consistent with these transportation objectives, Congress should maintain the use of the authority for assisting in the financing of vessel dry docks and shipyard modernization, and Congress should authorize the expansion of the guarantee authority to include the terminal and dockage facilities that will be essential to the expanded Great Lakes and Ocean Coastwise Container and Ro/Ro services. The use of the Title XI program to finance any other non-transportation assets should be strictly limited to Congressionally mandated exceptions to these general rules.

### 3.3 Congressional Funding & Oversight.

I would suggest that the Committee consider a revised MarAd Title XI program that would be authorized and funded for a seven-year or similar period with monies adequate to provide guarantee authority and program administration sufficient to meet current and projected United States national transportation and national security needs, as these needs are identified and defined by Congress. The MarAd Title XI program should “course corrected” with financing guarantees limited to vessel types and services keyed to defined national transportation and national security needs.

MarAd should be directed to revise its “letter commitment” procedures to more closely conform to commercial practice, and should issue letter commitments that include Congressional funding as a condition to the issuance of the Government guarantee. This will greatly facilitate the financing of the new private sector Great Lakes and Ocean Coastal vessel services that are needed. This will also enable MarAd to come before Congress seeking funding for a list of qualified vessel guarantee projects rather than seeking a “blank check” in the annual authorization and appropriations process.

Congress could in this fashion oversee and control the use of the guarantee authority by means of the authorization and appropriations process. Congress should require that MarAd present to Congress the projects that MarAd has approved (conditioned upon Congressional appropriations) as a part of the MarAd yearly requests for Title XI authorization and funding. This would enable Congress oversight in assuring that the Title XI guarantee authority is being used to fulfill Congressionally mandated goals.

#### 3.4 National Transportation "Start Up Services" & Lease Financing.

Title XI program financing regulations, such as those governing debt equity ratios and working capital, should be examined and revised to confirm their suitability to meeting the needs appropriate to a national transportation "Start Up Services" program. For many new ventures in the decade following the enactment of the 1970 Act, vessel leasing was the vessel financing method of choice. Leasing is particularly attractive to vessel operators in many start up situations because of the need for working capital and the inability of such start ups to make full use of federal income tax vessel depreciation deductions. As a contribution to the process of developing the outlines for such a "Start Up Services" program, I will be submitting for the record a paper that I have prepared that explores the uses of the MarAd Title XI program, and of MarAd's capital construction fund ("CCF") tax deferral program, in this context.

#### 4.0 Thank You & Concluding Thoughts.

I have appreciated this opportunity to appear before you to testify in response to your invitation of March 9<sup>th</sup>. My Seward & Kissel colleagues and I look forward to working with your Committee in any way in which we can assist you in your efforts to develop policies that will enable the United States to achieve and maintain:

"a merchant marine (1) sufficient to carry its domestic water-borne commerce . . .; (2) capable of serving as a military and naval auxiliary in time of war or national emergency; (3) owned and operated as vessels of the United States by Citizens of the United States; (4) composed of the best-equipped, safest and most suitable types of vessels and manned with a trained and efficient citizen personnel; and (5) supplemented by efficient facilities for building and repairing vessels"

as mandated by Section 101 of the Merchant Marine Act, 1936, as amended (46 U.S.C. 50101).

Thank you for your time and attention.

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March 9, 2007

Mr. H. Clayton Cook, Jr.  
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Dear Mr. Cook,

You are invited to testify before the Subcommittee on Seapower and Expeditionary Forces of the House Armed Services Committee at an oversight hearing on the Federal Ship Financing Guarantee Program, also known as Title XI Loan Guarantees, on Thursday, March 15, 2007, at 2:00 pm in room 2212 Rayburn House Office Building. The Administrator of the Maritime Administration will testify to the subcommittee during the first panel of the hearing, and I respectfully request that you testify in the second panel, along with other witnesses from the maritime industry.

Due to your significant experience in the maritime industry, both in government service and the private sector, the subcommittee is interested in your views on the Title XI Loan Guarantee Program. In particular, the subcommittee would like your views on the advantages and disadvantages for ship owners who seek ship construction mortgages under the Title XI provisions, and to explain the challenges, if any, ship-owners face when seeking mortgages exclusively through the commercial market.


Committee Rule 13 provides that witness statements must be delivered to the committee at least 48 hours in advance of the hearing to facilitate distribution to the members. Therefore, it is requested that 50 copies of your prepared statement be delivered to Mr. Jason Hagadorn in room 2340 Rayburn House Office Building by the morning of Tuesday, March 13, 2007. In addition, consistent with the House rules requirement to make materials from hearings electronically available to the general public, Committee Rule 13 requires that witness statements be provided to the committee in electronic form. This request may be satisfied by a transmittal via e-mail to [jason.hagadorn@mail.house.gov](mailto:jason.hagadorn@mail.house.gov).

Finally, Rule XI, Clause 2(g) of the Rules of the House of Representatives requires that all non-governmental witnesses testifying before the House include in their written testimony a curriculum vitae and a disclosure of the amount and source (by agency and program) of each federal grant (including subgrants) and contract (including subcontracts) that the witness and/or the organization has had with the federal government for the past three fiscal years. Please include this information in your prepared statement.

I appreciate your willingness to appear before the subcommittee and look forward to your testimony. Should you have any questions, please contact Will Ebbs on the committee staff at (202) 226-6305.

With kind regards, I am

Sincerely



GENE TAYLOR

Chairman

Seapower & Expeditionary Forces Subcommittee

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