

MARITIME CABOTAGE



May 16, 2006

**BEFORE THE
UNITED STATES DEPARTMENT OF HOMELAND SECURITY
UNITED STATES COAST GUARD**

Docket No. USCG – 2005 - 20258

Vessel Documentation: Lease financing
for Vessels Engaged in the Coastwise Trade

Comments of the Maritime Cabotage Task Force

These comments are submitted on behalf of the Maritime Cabotage Task Force (MCTF), a coalition of more than 400 members that supports the economic, security, environmental and safety benefits that accrue from the Jones Act and other cabotage laws. MCTF members include American labor, carriers, shipyards, marine equipment manufacturers, trade associations, defense interests and others. We appreciate the opportunity to comment on this very important subject.

As indicated in comments made previously in related dockets,¹ proper administration of the lease financing provision is vitally important to assuring the continued integrity of the legal

¹ See MCTF comments in Docket Nos. USCG 2001-8825, and MARAD-2003-15171.

requirement that vessels authorized to operate in U.S. domestic trades must genuinely be controlled by American citizens. The lease financing provision permits American carriers to obtain financing for their domestic vessels from banks, leasing companies or other financial institutions regardless of their nationality. While this provision was intended to increase the availability and reduce the cost of capital for Jones Act vessels, Congress also clearly intended to retain the requirement that American citizens must control the operation and use of such vessels. Nothing that has happened since initial adoption of the lease financing provision in 1996, nor since that provision was amended in 2004, suggests that Congress would be any less committed to American citizen control over these maritime assets.

This proceeding will establish the final regulatory framework for allowing non-U.S. citizens to lease finance vessels eligible to operate in U.S. domestic trades. Clear regulatory guidance and administrative procedures on this subject are essential. The absence of clear regulatory standards between 1996 and 2004, which stemmed in part from ambiguities in the law prior to 2004, led to abuse of the lease financing provision in certain cases. These abusive transactions, if left unchallenged, could have established a template for de facto non-citizen control over the domestic maritime industry. As we learned from these efforts, vigorous enforcement by the Coast Guard of U.S. citizen ownership and control requirements is essential to maintaining confidence in the integrity of these requirements, which in turn is vital to American security and trade interests, and in fostering continued investment in the Jones Act fleet.²

² In that vein, because of concerns over potentially abusive transactions involving mortgage financing of coastwise vessels, *e.g.*, where the foreign mortgagee may provide financing at non-market rates and terms in exchange for direct or indirect economic control over the vessel, the pending Coast Guard authorization bill includes explicit authority for the Coast Guard to investigate the “mortgagee” of a Jones Act vessel. *See* Conf. Rept. No. 109-413 on H.R. 889, Sec.308.

Amendments made to the lease financing provision by the Coast Guard and Maritime Transportation Act of 2004 (2004 Act) eliminated these ambiguities, and made clear the circumstances under which non-citizens may and may not lease finance Jones Act vessels. This proceeding implements those amendments.

In general, we commend the Coast Guard for proposing rules that faithfully track and apply the new statute, and that are logically organized and easier to apply than prior rules. To be eligible for lease financing, a vessel must not only meet the criteria established in prior law, *i.e.*, that it can be documented, meets U.S. build requirements, and is properly demise chartered to a U.S. citizen. In addition, as a result of the 2004 Act and as properly included in the proposed rules, the vessel owner now must certify that it meets certain objective criteria set forth in the statute. Thus, the owner must certify that it –

- Is a leasing company, bank or financial institution;
- Owns, or holds the beneficial interest in, the vessel solely as a passive investment;
- Does not operate any vessel for hire and is not affiliated with any person that operates any vessel for hire; and
- Is independent from, and not an affiliate of, any charterer of the vessel or any other person who has the right, directly or indirectly, to control or direct the movement or use of the vessel.

The first two criteria, as further clarified by the definitions, explicitly establish that non-citizen control over the “use, operation or management” of the vessel is not permitted. The “control” that is relevant in this regard is thus not just over the technical operations of the vessel. It is over the economic use and management of the asset. If and to the extent there was any doubt

about that issue under prior law, the new statute, as faithfully implemented in the proposed rules, fully resolves that issue.

Further, the proposed rules also properly track two absolute prohibitions set forth in the statute. A non-citizen, even if it qualifies as a leasing company and intends to own a coastwise vessel solely as a passive investment, may not do so if it either –

(a) Directly or indirectly through an affiliate operates any vessel for hire. This absolutely prevents non-citizen shipping companies operating vessels for hire from entering domestic trades through the lease financing provision; or

(b) Is affiliated with any charterer or any other person who has the right, directly or indirectly, to control or direct the movement or use of the vessel that is being lease financed. This prevents circuitous arrangements by which non-citizen shipping interests would seek to enter domestic trades through a strawman U.S. citizen vessel operator.

Annual certification that these criteria continue to be met is required by the statute, and is properly included in the proposed rules. This will maintain a practical check that the lease financing provision is not being abused.

We offer suggestions for three relatively minor technical changes to the proposed rules that would clarify and be fully consistent with the statute. First, it should be clarified in the definition of “Affiliate” that the fact that a person is *not* named as being part of the same consolidated group in reports filed at the Securities Exchange Commission or the Internal Revenue Service is not proof of non-affiliation. As a practical matter, the affiliation test would be applied in most instances to non-citizen entities that would not likely be reporting to U.S. securities or tax authorities. Subsection (2) of the definition should thus be revised to read:

(2) Named as being part of the same consolidated group in any report or other document submitted to (A) the United States Securities and Exchange Commission or Internal Revenue Service, or (B) any comparable agency of a foreign government that requires or permits the identification of persons that are directly or indirectly controlled by, under common control with, or controlling another person.

Second, the term “Sub-charter” is defined in the proposed rule in a manner that appears designed to prohibit a lease financing owner from claiming that one of its affiliates can “Sub-charter” a vessel because that person would not be considered a “charterer” of the vessel. While the validity of such an argument is doubtful, the initial and annual certification requirement does not reference a sub-charter, leaving open at least the possibility that someone could make the argument. To preclude such a claim, the phrase “including but not limited to a person using the vessel through any form of sub-charter” could be added to the end of subsection 68.65(a)(1)(iv).

Third, a demise charter of a lease financed vessels (or barge), by definition, transfers control over the vessel to the charterer. Any sub-charter of a lease financed vessel that is a demise charter would likewise transfer control to the sub-charterer. MCTF submits that in most cases the parties to such a sub-charter can and should be required to submit a copy of the sub-charter to the Coast Guard *before* the sub-charter becomes effective. The relevant portions of subsection 68.70(d) and 68.75(d) should be amended to read –

. . . the charterer must file a copy of the sub-charter and amendments to the sub-charter with the Director, National Vessel Documentation Center, no later than 10 days before the effective date of the sub-charter absent good cause shown, and the sub-charterer

Finally, it appears that the proposed rules properly treat grandfathered vessels, *i.e.*, those whose owners can not make the certifications required under new subsection 68.65, but which had (in most cases) been documented under the lease financing provision prior to enactment of the 2004 amendments. MCTF would oppose granting or denying a vessel coastwise privileges in a manner that is inconsistent with the statutory terms providing grandfather rights, as such a

determination would undermine the integrity of the legislative process. As noted, MCTF is not aware of any inconsistencies or discrepancies in this regard, but reserves the right to object should it appear in a given case that the statutory grandfather provisions are not being faithfully implemented and maintained.

Respectfully submitted,

A handwritten signature in black ink that reads "Philip M. Grill". The signature is written in a cursive style with a large, looping initial "P".

Philip Grill
Chairman
Maritime Cabotage Task Force