

**DEPARTMENT OF TRANSPORTATION****Maritime Administration****46 CFR Part 298**

[Docket No. MARAD-98-3468]

RIN 2133-AB32

**Putting Customers First in the Title XI Program****AGENCY:** Maritime Administration, Transportation.**ACTION:** Final rule.

**SUMMARY:** The Maritime Administration (MARAD) is issuing this final rule which amends certain provisions of the existing regulations implementing Title XI of the Merchant Marine Act, 1936, as amended ("Act"). This rule amends existing regulations by simplifying existing administrative practices governing the following areas: the ship financing guarantee process; and standards for evaluation and approval of applications. These changes will make the entire process easier for applicants.

**EFFECTIVE DATE:** This final rule is effective on August 21, 2000.

**FOR FURTHER INFORMATION CONTACT:** Linda W. Reaves, Financial Analyst, Office of Ship Financing, Maritime Administration, Room 8122, 400 Seventh Street SW., Washington, DC 20590. Telephone 202 366-1899.

**SUPPLEMENTARY INFORMATION:** Title XI of the Act authorizes the Secretary of Transportation (Secretary) to guarantee debt issued for the purpose of financing or refinancing: (a) the construction, reconstruction, or reconditioning of U.S.-flag vessels or eligible export vessels built in United States shipyards, and (b) the construction of advanced shipbuilding technology and modern shipbuilding technology of a general shipyard facility located in the United States. MARAD administers financial assistance under Title XI of the Act in the form of obligation guarantees for all types of vessel construction and shipyard modernization and improvement, except for fishing vessels. The part of the Title XI program related to fishing vessels is administered by the National Oceanic and Atmospheric Administration of the U.S. Department of Commerce, ("NOAA"), pursuant to NOAA regulations, which appear at 50 CFR part 253. The Title XI program enables applicants to obtain long-term financing on terms and conditions that may not otherwise be available. Applications for obligation guarantees are made to the Maritime Administration (we, us, or our), acting under authority delegated by the

Secretary, to the Maritime Administrator. Once an applicant submits a Title XI application to us and prior to execution of a guarantee, we must, among other things, make determinations of economic soundness of the project, and the applicant's financial and operating capability.

**National Performance Review**

In response to a 1993 recommendation from Vice President Gore's National Performance Review team, President Clinton issued Executive Order 12862, September 11, 1993, calling for a revolution within the Federal government to change the way it does business by putting customers first and striving for a customer-driven government that matches or exceeds the best service available in the private sector. In October 1997, the National Performance Review team reported that Federal agencies, implementing the Executive Order, had launched a massive effort to improve governmental service and had made a noticeable difference.

On December 1, 1997, in a memorandum to heads of Operating Administrations and Departmental offices at the United States Department of Transportation, Secretary of Transportation Rodney E. Slater urged all Departmental offices and heads of Operating Administrations to ask their customers what is important to them in the kinds and quality of services they want and what is their level of satisfaction with existing services. Secretary Slater emphasized that it is "this customer feedback that will be the basis for improving, revising, adding, or deleting standards when it makes sense and, ultimately, for helping us become a more customer focused DOT."

**Plain Language**

Executive Order 12866 and the President's memorandum on plain language in government writing of June 1, 1998, require each agency to write all rules in plain language. The Department of Transportation and MARAD are committed to plain language in government writing; therefore, this final rule is written in plain language. This final rule is written in plain language for easier understanding and does not change the substance of the proposed rule published at 64 FR 44152 (August 13, 1999), except as explained in the Discussion of Public Comments and the Rulemaking Text Section. Our goal is to improve the clarity of the regulation.

**Advance Notice of Proposed Rulemaking**

An advance notice of proposed rulemaking (ANPRM), published on February 17, 1998 (63 FR 7744), solicited comments on ten sets of questions which were grouped into the following categories:

- The standard application Form MA-163, including the requirement for vessel plans and specifications.
- The requirements for information on the applicant's and/or operator's qualifications.
- The requirements for financial information and certain financial tests.
- The requirements for information on economic soundness and the economic soundness criteria.
- The inclusion in the Title XI regulations of the provisions of Maritime Administrative Order (MAO) No. 520-1, Amendment 2.
- The documentation requirements for a closing on a commitment to guarantee obligations.

Our consideration of comments received in response to the categories above concerning the application form and closing documents were published separately in a **Federal Register** Notice dated July 30, 1998 (63 FR 40690). The other comments received from nine commenters on the ANPRM were reviewed and taken into consideration in preparation of a notice of proposed rulemaking discussed below. These comments, in general, dealt with applicant and operator qualifications, financial requirements, and economic soundness.

**Notice of Proposed Rulemaking**

In response to customer feedback on the ANPRM, we published a notice of proposed rulemaking (NPRM) on August 13, 1999, in the **Federal Register** (64 FR 44152). The NPRM reflected all comments received in response to the ANPRM. MARAD is now issuing this final rule concerning Title XI program administration which reflects consideration of all comments received in response to the NPRM.

**Discussion of Public Comments and Rulemaking Text**

The discussion that follows summarizes the comments submitted to MARAD by six commenters on the NPRM, states why particular recommendations/suggestions have or have not been adopted and the rationale therefore. Note that where the first letter of one or more words is capitalized, that term is defined in § 298.2 Definitions. The discussion also notes where

proposed changes have been adopted to the Title XI regulations and the rationale therefore, and where relevant, states why particular recommendations/suggestions have not been adopted. Additionally, we have made clarifications throughout 46 CFR Part 298 for easier understanding and to more fully express implications. Such clarifications do not change the substance of the regulations. We have rewritten the entire part 298 in plain language. The following sections have only plain language and no substantive changes from the existing part 298: §§ 298.10 Citizenship; 298.17 Evaluation of applications; 298.26 Lease Payments; 298.27 Advances; 298.37 Examination and audit; 298.39 Exemptions; 298.40 Defaults; and 298.42 Reporting Requirements—financial statements.

We have adopted the following changes to Obligation Guarantees regulations at 46 CFR Part 298. The amendments are summarized as follows:

#### *Section 298.1 Purpose*

This section has been modified to advise that “you” and “we” have been used throughout in writing this part in plain language. You and your refer to the applicant for Title XI assistance unless we note or imply otherwise. We, us, and our refer to the Maritime Administration, the Secretary of the Maritime Administration, or the Secretary of Transportation.

#### *Section 298.2 Definitions*

Section 298.2 is intended to provide convenient reference to the meaning of significant terminology used in part 298. The definitions, as follows, are based principally on statutory derivations:

“Advanced Shipbuilding Technology” is changed in order to include other modernization elements which are not previously listed in the definition and which contribute to a shipyard’s efficiency or productivity.

“Guarantee Fee” is changed to delete the reference to an annual fee and continuing Guarantees. In accordance with the Act, the regulations now require that the guarantee fee for the entire term of the financing be paid in advance at the initial funding of the transaction, with no refund in the event the Obligations are retired early.

“Indenture Trustee” is changed to increase the amount of combined capital and surplus an indenture trustee must have to at least \$25,000,000 as the current amount of \$3,000,000 is not adequate.

“Shipyard Project” is a defined term added to this section which was not previously proposed in the NPRM.

Shipyard Project refers to either Advanced Shipbuilding Technology or Modern Shipbuilding Technology.

#### *Section 298.3 Applications*

In § 298.3 of the NPRM, we proposed to modify certain provisions to reflect current practices and procedures and to clarify certain provisions. Additionally, we proposed to delete the priority given to applications from general shipyard facilities formerly in 298.3(e) that have engaged in naval vessel construction and that have pilot projects for shipyard modernization and vessel construction because all the funds previously appropriated to the Department of Defense and transferred to the Department of Transportation for the Title XI program have been expended.

One commenter recommended that MARAD not eliminate the provision that gives priority for processing applications from General Shipyard Facilities that have engaged in naval vessel construction. The commenter stated that Congress adopted this element when it enacted the National Shipyard Initiative in recognition of the need to sustain the defense shipbuilding industrial base and the basis for the priority and the procedure are just as valid today as they were when Congress enacted the National Shipbuilding Initiative. Additionally, the commenter stated that the mere fact that all existing funds that the Department of Defense (DOD) transferred to MARAD has been expended does not justify the elimination of the procedure.

**MARAD Response:** We believe that the President’s plan for the National Shipbuilding Initiative (NSI) is to assist the shipbuilding industry to compete internationally. The NSI was also planned as a transitional program structured to assist in the transition from naval to commercial markets. The NSI regulations provide that in making loan guarantee commitments using funds provided under the NSI, priority shall be given to applications from shipyards that have engaged in naval vessel construction. This provision does not apply to other funds appropriated to the Title XI program. Funds appropriated for the NSI from DOD for this transitional period did not extend beyond 1998, and all such funds have been expended.

Therefore, this priority provision has no application. MARAD’s elimination of priority given to applications from shipyards that have engaged in naval vessel construction is consistent with the plans of the NSI to facilitate the transition period, permitting funds appropriated to expire in five years, and therefore not intended as an ongoing

priority. Because Title XI financing continues to be available for shipyard modernization and export vessels, Title XI assistance to the shipbuilding industry to compete internationally continues. If Congress elects to appropriate additional funds or DOD transfers funds, if required, a priority processing procedure could be reimplemented without an inordinate undertaking by us. Therefore, we have adopted our proposal to eliminate the priority provision to General Shipyard Facilities of this section.

We have adopted, as proposed in the NPRM, under this section a change to reflect that only two sets of documentation must be submitted to us for review.

This section is also changed to delete the provision that, if an applicant does not claim a Freedom of Information Act (FOIA) exemption at the time an application or amendment is filed, we will not oppose any subsequent request for disclosure pursuant to FOIA. Deletion of this provision reflects actual agency practice, which is to allow a request for exemption under FOIA at any time.

Also, this section is changed to clarify that priority will be given for processing applications for vessels capable of serving as United States naval and military auxiliary in time of war or national emergency.

Finally, this section was modified to change the word “financing” to “refinancing” to clarify the provision that states that we will give priority processing for applications that request financing construction of equipment or vessels less than one year old as opposed to the “refinancing” of existing equipment or vessels that are one year old or older.

#### *Section 298.11 Vessel Requirements*

Under § 298.11 of the NPRM, we proposed to: (1) Clarify that the vessel must be constructed in the United States; (2) provide that we may contact the shipyard to request that it submit additional technical data, backup cost details, and other evidence if we have insufficient data; (3) delete the last sentence of paragraph (c) which is redundant with the last sentence of paragraph (a) of this section, and (4) conform the regulations to our present practices which permit a U.S.-flag constructed vessel to meet the highest classification standard of the American Bureau of Shipping or of a classification society other than the American Bureau of Shipping so long as the society meets the inspection standards of the United States Coast Guard.

In response to the NPRM, one commenter requested that MARAD not modify the provision of paragraph (c) of § 298.11 to conform to MARAD's present practice which permit a U.S.-flag constructed vessel to meet the highest classification standard of the American Bureau of Shipping or of a classification society other than the American Bureau of Shipping (ABS) so long as the society meets the inspection standards of the United States Coast Guard. The commenter stated that statute and the Title XI regulations require A-1, ABS classification and that these provisions refer to another standard, not another society.

**MARAD Response:** We disagree with the commenter's interpretation that the existing provision provides that ABS is the only acceptable classification society for U.S.-flag vessels. We had previously made a review of this provision and based on the results of our review interpreted the provision to permit a U.S.-flag constructed vessel to meet the highest classification standard of a classification society other than the ABS so long as the society meets the inspection standards of the United States Coast Guard. Hence, we adopted the practice of permitting other classification societies. We have considered the commenter's position; yet, we affirm our position to permit other classification societies. Because the phrase "or other such standards as may be approved by the United States Coast Guard" does not specify "ABS" standards, we do not believe another society is precluded. Therefore, as proposed in the NPRM, the regulations are being modified to clearly permit a U.S.-flag constructed vessel to meet the highest classification standard of a classification society of ABS or other classification society so long as the society meets the inspection standards of the United States Coast Guard.

Section 298.11 is changed, as proposed in the NPRM, to clarify that the vessel must be constructed in the United States. This section is also revised to provide that we may contact the shipyard to request that it submit additional technical data, backup cost details, and other evidence if we have insufficient data.

Additionally, this section is changed to clarify that all Vessels other than Eligible Export Vessels must be documented under U.S. registry.

#### *Section 298.12 Applicant and Operator's Qualifications*

We concur with comments that too much information is requested in this section, particularly with respect to the applicant's existing vessels, and certain

background data. Therefore, this section has been modified to reduce the information required. With respect to the suggestion that we utilize the endorsement of industry associations, the regulations do not preclude our consideration of such an endorsement when evaluating the applicant's and/or operator's qualifications.

A paragraph is added to this section to reflect the MAO 520-1 provision requiring that an operator's historical performance record be considered in evaluating operating ability.

#### *Section 298.13 Financial Requirements*

In the NPRM, we did not propose any changes to this section, as suggested by a commenter to the ANPRM, to eliminate the requirement for a waiver in order for foreign items to be included in Actual Cost. Our interest is in promoting a shipbuilding industry including both shipyards and suppliers. Therefore, it would be inappropriate to permit wholesale use of foreign items in Title XI financings when comparable items are available from U.S. suppliers. We believe such a practice would have an adverse impact on the U.S. shipbuilding industry as a whole. However, request for waivers to include foreign items have not been unreasonably withheld, so that the no-foreign content requirement without a waiver has not had a negative impact on the shipyards or shipowners. Therefore, we will continue to review inclusion of foreign items on a case-by-case basis. A correction was made in this section to state that in deciding whether to grant a waiver for foreign components and services you must submit a certification that the "domestic" item is not of sufficient quality. The existing regulations inadvertently refer to the "foreign" item.

We believe that the current inclusion of the illustration in this section of how the cost of foreign components of the hull and superstructure may be used to satisfy an applicant's equity requirements is unnecessary and confusing. Therefore, we are deleting the illustration and the one sentence which refers to the illustration in existing § 298.13(a)(2)(i).

The reference to guarantee fees in existing paragraph (a)(2)(iv) is deleted as guarantee fees are eligible for inclusion in Actual Cost.

We have adopted our proposal to permit, in the case of Eligible Export Vessels, financial statements that are not reconciled to U.S. generally accepted accounting principles (GAAP) if a satisfactory justification is provided concerning the inability to reconcile.

We further adopted the proposed change to eliminate the requirement for a debt amortization schedule and sources and uses statement, and to incorporate current financial definitions.

We have adopted the proposal to eliminate the special financial requirements set forth in this section due to the restrictive nature of the covenants that accompany these requirements and the fact that companies have not elected this alternative in the recent past. In order to make clear that there is only one set of financial requirements, the word "primary" before financial requirements is deleted here and later in the regulation under § 298.35.

#### *Section 298.14 Economic Soundness*

Under § 298.14 of the NPRM, we proposed to reduce or eliminate information required under this section. We proposed to add a new paragraph which differentiates between applications for vessel financing and shipyard modernization projects.

We proposed to clarify the criteria used for economic soundness finding by including provisions of MAO 520-1 relating to economic soundness.

We also proposed requirements concerning the ability of the project to service its debt at the time of delivery which will be based on market conditions at that time, and that primary consideration shall be given to operating cash flow.

One commenter stated that the requirement for a detailed breakdown of estimated daily operating expenses needs to be clarified and that it would be inappropriate to require a detailed breakdown of individual salaries and wages as this would be unduly cumbersome and cover proprietary information that would need to be protected from Freedom of Information Act (FOIA) requests. The commenter further stated that all that should be required is an aggregate cost of salary for the shipyard.

**MARAD Response:** The daily operating expense information requested for a Title XI application is information that is necessary for us to make an assessment of cash flow for the project. The application does not request individual wages and salaries but an item of expense for wages. With respect to disclosure of proprietary information, the applicant can assert a claim of exemption from disclosure under a FOIA request of any proprietary information submitted in connection with the company's application. We do not believe that providing a breakdown of estimated daily operating expenses

would be unduly cumbersome as this type of information is typically prepared for the company's own projections in the initial planning stages of its proposed project. Therefore, we have not eliminated the requirement to provide us with a detailed breakdown of daily operating expenses.

We have adopted the NPRM's proposed changes to § 298.14. We recognize that much of the information requested under § 298.14 was developed for applications from companies involved in a liner service. We have taken steps to simplify the regulations by reducing or eliminating requested information. Specifically, certain paragraphs under this section requesting information on expenses, have been deleted and are replaced by a new paragraph which will encompass all expenses. The new paragraph differentiates between applications for vessel financing and shipyard modernization projects.

We have not added a requirement to the economic soundness section concerning the applicant's financial strength because the existing requirements of § 298.13, Financial Requirements, already require us to make certain determinations concerning the financial position of the ultimate transaction credit.

In order to clarify the criteria used for economic soundness findings, we adopted the NPRM's proposal to include in this section the provisions of MAR 520-1 relating to economic soundness. Specifically, we have modified this section to include requirements concerning the ability to service debt at the time of delivery which will be based on market conditions at that time, and that primary consideration shall be given to operating cash flow. To enable us to analyze cash flow, the applicant is requested to provide a five-year forecast of operating cash flow.

#### *Section 298.15 Investigation Fee*

As proposed in the NPRM, this section is revised by correcting the reference to the filing fee to \$5,000.

#### *Section 298.16 Substitution of Participants*

As proposed, this section is revised to delete the last sentence which references an annual guarantee fee.

#### *Section 298.18 Financing Shipyard Projects*

Under § 298.18, we proposed to eliminate from the initial criteria for Guarantee approval, consideration of whether Guarantees will aid in the transition of a shipyard from naval to commercial shipbuilding.

One commenter stated that the proposed elimination of the weighted consideration given for transitioning from naval to commercial shipbuilding is totally inconsistent with the goals of the National Shipbuilding Initiative and is inconsistent with the emphasis that DOD and the Navy have placed on major shipbuilders to transition back to commercial shipbuilding.

*MARAD Response:* We proposed to eliminate one of the factors in considering Guarantees for financing Advanced or Modern Shipbuilding Technology. We disagree with the commenter that our proposal to eliminate the initial criteria to financing Advanced or Modern Shipbuilding Technology projects to aid in transitioning from naval to commercial shipbuilding is inconsistent with the goals of the National Shipbuilding Initiative (NSI). It is our position that promoting the growth and modernization of the U.S. merchant marine and U.S. shipyards in general also assists in sustaining the defense shipbuilding base as the workforce and facilities for defense and commercial shipbuilding are to some extent interchangeable. Therefore, we do not believe that elimination of the initial criteria provision of whether the Guarantee will aid in the transition from naval shipbuilding to commercial ship construction would have an adverse effect on the defense shipbuilding base. Therefore, as proposed, we are eliminating the provision in our regulations requiring applications for Advanced or Modern Shipbuilding Technology projects to aid in transitioning from naval to commercial shipbuilding.

#### *Section 298.19 Financing Eligible Export Vessels*

We have made a conforming change not previously proposed under this section to eliminate the entire paragraph referencing use of funds transferred from DOD to the Title XI program. As discussed under § 298.3, funds transferred from DOD to the Title XI program have been expended and therefore regulations regarding such funds have no application.

We have adopted, as proposed, under this section to make a modification by deleting the reference to the Export-Import Bank of the United States to now refer to the Inter-agency Country Risk Assessment System since the Export-Import Bank's risk assessments are reflected in the Inter-agency Country Risk Assessment System.

#### *Section 298.20 Term, Redemptions and Interest Rate*

We have adopted, as proposed, under this section, to clarify that for multiple vessels the maturity date of the Guarantees may be less than but in no event more than twenty-five years from the date of delivery from the shipyard of the last of multiple vessels but that the amount of the Guarantees shall relate to the depreciated actual cost of the multiple vessels as of the date of the Closing.

#### *Section 298.21 Limits*

We have adopted, as proposed, under this section, to specify that no foreign, federal, state or local taxes, user fees, or other governmental charges shall be included in Actual Cost. Additionally, we have changed the reference to the Federal Ship Financing Account to the Credit Reform Financing Account to reflect the current account title for deposits held by us with respect to moneys received in connection with construction contracts.

#### *Section 298.22 Amortization of Obligations*

We have adopted, as proposed, to replace the parenthetical phrase "straight line basis" with the phrase "level principal" to reflect our current terminology. Additionally, other references to "straight line basis" in this section have been changed to "level principal". Reference to "level debt" amortization in this section have been changed to "level payment" to reflect current finance terminology.

#### *Section 298.23 Refinancing*

We have adopted, as proposed, under this section to clarify our position regarding the refinancing of debt on Advanced or Modern Shipbuilding Technology. Refinancing of non-Title XI debt on Advanced or Modern Shipbuilding Technology is not permitted. Additionally, we have eliminated the reference to "mortgage insurance" or "contracts of insurance" in this section and throughout this part, including § 298.43 as we no longer issue mortgage insurance and all loans financed with mortgage insurance have expired.

#### *Section 298.24 Financing a Vessel More Than a Year After Delivery*

We proposed to delete § 298.24 because we believed there is no current authority for us to finance facilities and equipment related to marine operations.

Two commenters objected to the proposed deletion of § 298.24. The commenters believed that deletion of this section is not warranted and our

reasoning is an incorrect statement of our authority.

**MARAD Response:** We have reconsidered our proposal to delete § 298.24 and have determined that we may finance facilities and equipment related to marine operations under limited circumstances. Based on our interpretation of the Act, we have revised this section to clarify the provisions for issuing Guarantees to finance older vessels and using Title XI debt proceeds to finance vessels or facilities and equipment related to marine operations.

#### *Section 298.30 Nature and Content of Obligations*

We have adopted, as proposed, under this section, to clarify that an indenture trustee is not required under our documents.

#### *Section 298.31 Mortgage*

We have adopted, as proposed, to correct that, except for Eligible Export Vessels, a mortgage must be filed with the United States Coast Guard's National Vessel Documentation Center. The existing regulations require, except for Eligible Export Vessels, that the mortgage be filed with the United States Coast Guard at the Vessel's port of record.

#### *Section 298.32 Required Provisions in Documentation*

Proposed § 298.32 regarding the furnishing of insurance and a performance bond remain unchanged. Under the current Title XI regulations, the Secretary may waive or modify the performance bond requirement, upon determining that the shipyard or manufacturer of Advanced or Modern Shipbuilding Technology has sufficient financial resources and operational capacity to complete the project. In instances where sufficient resources cannot be demonstrated, our interests as a guarantor must be fully protected. Furthermore, inasmuch as § 298.21 provides for performance bond premiums to be included as an item of Actual Cost and therefore financeable up to a maximum of 87½ percent, we find that the bonding requirement does not constitute an inordinate out of pocket expense.

We have adopted as proposed to modify § 298.32 to delete the word "annual" in this section in reference to citizenship filing requirements. The citizenship requirements for the Title XI program were modified by a final rule which was published in the **Federal Register** and became effective on September 8, 1997, which no longer required the filing of annual citizenship

affidavits for the Title XI Obligors. Additionally, we have clarified that with respect to Shipyard Projects, the contract must contain provisions for making periodic payments for the work in accordance with an agreed schedule, submitted by the "contractor". The existing regulations only make reference to a "shipyard" containing this provision in its contract for construction of a vessel.

#### *Section 298.33 Escrow Fund*

We have adopted, as proposed, to modify this section to conform to the documentation in the general provisions of the new security agreement.

#### *Section 298.34 Construction Fund*

Under § 298.34, we proposed to clarify the requirements regarding the construction fund and to eliminate the current redundancies of this section regarding withdrawals and deposits, the procedure for which is described in § 298.33.

One commenter believes that we should eliminate the requirement for a construction fund and disburse to the Obligor the bond proceeds applicable to cost already paid equaling 87.5% or 75%, as applicable. Basically, the commenter stated that there is no statutory authority for the construction fund set out in the proposed § 298.34 and that in Section 1108 of the Merchant Marine Act, 1936, (the Act) Congress intended for all payments for eligible costs to be shared 12.5% or 25% by the Obligor through payment of equity and 87.5% or 75% out of the Title XI guaranteed bond proceeds. The commenter further stated that MARAD has consistently misinterpreted Section 1108 of the Act and required payment by the Obligor of 12.5% or 25% of the entire cost of the project up front before any payment out of the bond proceeds thereby increasing the cost of the project to the Obligor because the cost of equity is indisputably greater than the cost of debt. The commenter stated that because this interpretation does not comport with the Act, MARAD had to create a device called the Construction Fund in order to deposit bond proceeds that could not be deposited in the escrow fund due to the explicit language of Section 1108 but also could not be paid to the shipbuilder or to reimburse the Obligor because of MARAD's incorrect requirement for payment of 12.5% or 25% of the entire cost of the project prior to any disbursement of the escrow fund.

**MARAD Response:** We disagree with the commenter's assertion that we have no statutory authority for creation of the Construction Fund. Section 1104A(c)(1)

of the Act provides that "The security for the guarantee of an obligation by the Secretary under this title may relate to more than one vessel and may consist of any combination of types of security." Section 1103(c) of the Act requires the Obligor to provide 12.5% or 25% equity in the project. It is entirely consistent with the statutory requirement that the applicant have all of its equity raised before the issuance of a commitment to guarantee. To provide us with the assurance that this equity is available for the project and not diminished, we require that the Obligor expend its 12.5% or 25% on the project before our collateral is at risk. This is analogous to a downpayment requirement when purchasing a significant asset. In addition, with the applicant funding the equity up front, the applicant has the greatest incentive to make the project a financial success.

The commenter also indicated that our funding requirements result in a higher cost to the applicant as the cost of equity is greater than the cost of debt. If we were to adopt the funding mechanism proposed by the commenter, we would require that any unused equity funds be placed in non-risk type of investment similar to those utilized by the Escrow and Construction Funds. In this case the earnings on the equity would approximate the earnings on the debt and therefore there would not be a greater cost by utilizing the full amount of the equity funds before utilizing the Title XI proceeds. We believe that requiring the Obligor to provide the initial expenditures for the project is in the Government's best interest and the Construction Fund accomplishes this goal.

We believe that it is in the best interest of the Government to require the initial expenditures for the project to be provided by the Obligor and therefore would need a mechanism such as the Construction Fund to accomplish this goal. Therefore, we are not accepting the commenters proposal to eliminate the Construction Fund.

#### *Section 298.35 Title XI Reserve Fund and Financial Agreement and Financial Agreement*

We proposed to modify § 298.35 entirely. We proposed to delete the provision regarding financial covenants for companies meeting the special financial requirements because this provision had not been elected by applicants in the recent past. The references to an applicant being governed by either the section 12 or section 13 requirements are deleted and all companies will be subject to the same two sets of covenants. The first set

of covenants, the primary covenants, is to apply to all companies regardless of their financial condition and the second set of covenants, referred to as supplemental covenants, is to apply to only those companies that do not meet the specific financial conditions.

One commenter stated that the covenant regarding restriction on mergers or sales (a primary covenant) is unduly restrictive and needs to be clarified to ensure that we do not consent only when the integrity of a loan would be jeopardized by the sale or merger.

**MARAD Response:** The Title XI Reserve Fund and Financial Agreement requires our consent prior to the Obligor entering into a merger or sale. The purpose of requiring our consent prior to a merger or sale is to allow us the opportunity to do a due diligence review of the transaction to determine whether or not the transaction would have an adverse effect or impose unacceptable risk to the Government. To accomplish this review, each merger or sale must be analyzed on a case-by-case basis prior to effectuating the transaction. Therefore, we believe that our review and prior consent are warranted, and we have not modified this provision.

One commenter provided comments on a proposed provision of the Title XI Reserve Fund and Financial Agreement dealing with the restriction the Agreement places on the Obligor with respect to payment of dividends. The commenter believes that the dividend restrictions are excessively restrictive to well capitalized Sub-Chapter S corporations or Limited Liability Companies (LLCs) who qualify as "strong" companies (positive working capital and debt to equity ratio less than 2 to 1), whose tax liabilities flow through to their owners and thus may require "tax dividends" to those owners to reimburse them for payment of said liabilities.

**MARAD Response:** The purpose of the dividend restriction is to provide further assurance that funds are available for payment of principal and interest due on the Obligations. We recognize the unique tax situation of sub-chapter S corporations and LLCs and, when we deem appropriate, we consent to dividend payments for tax purposes. We do not believe an amendment to the dividend provision is necessary as special provisions are negotiated in the Title XI Reserve Fund and Financial Agreement to address these situations on a case-by-case basis. Therefore, we have not modified this section to reduce the restrictions with respect to the payment of dividends.

Additionally, we have adopted, as proposed, to modify this section in its entirety. The section regarding financial covenants for companies meeting the special financial requirements has been deleted in its entirety pursuant to the discussion above in § 298.13. The references to a Title XI company being governed by either section 12 or section 13 company are deleted and all Title XI companies will be subject to the same two sets of covenants. One set of covenants will be imposed regardless of the company's financial conditions (primary covenants) and the second set of covenants will only apply if the company does not meet the specific financial conditions (supplemental covenants). Also, we have deleted the paragraph in the existing regulations referring to dividend restrictions applicable to companies who are parties to an operating-differential subsidy contract because we no longer issue operating-differential subsidy contracts and have no plans to resume.

#### *Section 298.36 Guarantee Fee*

We have adopted, as proposed, to delete the word "annual" in describing the Guarantee fee. The Guarantee is no longer required annually but is now a one-time fee due upon issuance of our guarantee. In the NPRM we inadvertently proposed to delete in paragraph (e) of this section, the provision stating that the Guarantee fee is non-refundable. Section 1104 A(e)(4) of the Act provides that the Guarantee fee is not refundable. Accordingly, we have included a statement the Guarantee fee is non-refundable.

We proposed to include in this section, a statement that "In calculating the present value used in determining the amount of the Guarantee Fee to be paid, MARAD will use a discount rate based on information contained in the "Department of Commerce's Economic Bulletin Board annual rates". In order to reflect the current source for the discount rate, we have changed this statement to provide that "In calculating the present value used in determining the amount of the Guarantee Fee to be paid, we will use a discount rate based on information contained in the "President's annual Budget".

#### *Section 298.41 Remedies After Default*

We have adopted, as proposed, to delete that Security proceeds to us will be applied to guarantee fees as there will be no guarantee fees due because all guarantee fees are now paid concurrently with the issuance of Obligations.

#### *Section 298.43 Applicability of the Regulations*

We have deleted the reference to "contracts of insurance" and "mortgage contracts" because we no longer issue "contracts of insurance" or "mortgage contracts" and all such loans previously insured have expired.

#### **Rulemaking Analyses and Notices**

##### *Executive Order 12866 and DOT Regulatory Policies and Procedures*

We have reviewed this final rule under Executive Order 12866 and have determined that it is not a significant regulatory action under section 3(f). It is also not significant under DOT Regulatory Policies and Procedures (44 FR 11034; February 26, 1979). Due to the limited economic impact of this final rule, no further analysis is necessary. These amendments are intended only to simplify and clarify the procedural requirements for obtaining Guarantees, principally to expedite the process for our review of applications. The intended effect is to encourage the construction of ships in U.S. shipyards both for the domestic and the Eligible Export Vessel programs and the modernization and improvement of U.S. general shipyard facilities by improving Title XI program administration.

##### *Regulatory Flexibility Act*

The Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*) requires MARAD to determine whether this final rule will have a significant economic impact on a substantial number of small entities. Although a substantial number of Title XI applicants may meet the United States Small Business Administration's criteria for small entity, these amendments to part 298 simplify and clarify the procedural requirements for obtaining loan Guarantees under the Title XI ship financing program. These simplifications and clarifications will merely expedite our application review process. While the simplified procedures will enhance customer service, these procedures will not result in a significant economic impact. Therefore, we certify that this final rule will not have a significant economic impact on a substantial number of small entities.

##### *Executive Order 13132*

We have analyzed this rulemaking in accordance with the principles and criteria contained in Executive Order 13132 ("Federalism") and have determined that it does not have sufficient federalism implications to warrant the preparation of a federalism summary impact statement. The

regulations have no substantial effects on the States, or on the current Federal-State relationship, or on the current distribution of power and responsibilities among the various local officials. Therefore, consultation with State and local officials was not necessary.

#### *Executive Order 13084*

We do not believe the revised regulations evolving from this final rule will significantly or uniquely affect the communities of Indian tribal governments when analyzed under the principles and criteria contained in Executive Order 13084 ("Consultation and Coordination with Indian Tribal Governments"). Therefore, the funding and consultation requirements of this Executive Order would not apply.

#### *Paperwork Reduction Act*

This rulemaking contains requirements that have been approved previously by the Office of Management and Budget (Approval No. 2133-0005, 2133-0012, and 2133-0018).

#### *Unfunded Mandates Reform Act*

This final rule does not impose unfunded mandates under the Unfunded Mandates Reform Act of 1995. It does not result in costs of \$100 million or more to either State, local, or tribal governments, in the aggregate, or to the private sector, and is the least burdensome alternative that achieves the objectives of the rule.

#### *Regulation Identifier Number (RIN)*

The Department of Transportation assigns a regulation identifier number (RIN) to each regulatory action listed in the Unified Agenda of Federal Regulations. The Regulatory Information Service Center publishes the Unified Agenda in April and October of each year. You may use the RIN contained in the heading of this document to cross-reference this action with the Unified Agenda.

#### **List of Subjects in 46 CFR Part 298**

Loan programs-Transportation, Maritime carriers, Mortgages, Reporting and recordkeeping requirements, Vessels.

Accordingly, 46 CFR part 298 is revised to read as follows:

### **PART 298—OBLIGATION GUARANTEES**

#### **Subpart A—Introduction**

Sec.

- 298.1 Purpose.
- 298.2 Definitions.
- 298.3 Applications.

#### **Subpart B—Eligibility**

- 298.10 Citizenship.
- 298.11 Vessel requirements.
- 298.12 Applicant and operator's qualifications.
- 298.13 Financial requirements.
- 298.14 Economic soundness.
- 298.15 Investigation fee.
- 298.16 Substitution of participants.
- 298.17 Evaluation of applications.
- 298.18 Financing Shipyard Projects.
- 298.19 Financing Eligible Export Vessels.

#### **Subpart C—Guarantees**

- 298.20 Term, redemptions, and interest rate.
- 298.21 Limits.
- 298.22 Amortization of Obligations.
- 298.23 Refinancing.
- 298.24 Financing a Vessel more than a year after delivery.
- 298.25 Excess interest or other consideration.
- 298.26 Lease payments.
- 298.27 Advances.

#### **Subpart D—Documentation**

- 298.30 Nature and content of Obligations.
- 298.31 Mortgage.
- 298.32 Required provisions in documentation.
- 298.33 Escrow fund.
- 298.34 Construction fund.
- 298.35 Title XI Reserve Fund and Financial Agreement.
- 298.36 Guarantee Fee.
- 298.37 Examination and audit.
- 298.38 Partnership agreements and limited liability company agreements.
- 298.39 Exemptions.

#### **Subpart E—Defaults and Remedies, Reporting Requirements, Applicability of Regulations.**

- 298.40 Defaults.
- 298.41 Remedies after default.
- 298.42 Reporting requirements—financial statements.
- 298.43 Applicability of the regulations.

#### **Subpart F—Administration [Reserved]**

**Authority:** 46 App. U.S.C. 1114(b), 1271 *et seq.*; 49 CFR 1.66.

#### **Subpart A—Introduction**

##### **§ 298.1 Purpose.**

This part prescribes regulations implementing Title XI of the Merchant Marine Act, 1936, as amended, governing Federal ship financing assistance (46 App. U.S.C. 1271 *et seq.*). This part uses "you" and "we" throughout. You and your refer to the applicant for Title XI financing assistance unless we note or imply otherwise. We, us, and our refer to the Maritime Administration, the Secretary of the Maritime Administration, or the Secretary of Transportation, as applicable.

##### **§ 298.2 Definitions.**

For the purpose of this part:

*Act* means the Merchant Marine Act, 1936, as amended (46 App. U.S.C. 1101 through 1294).

*Actual Cost of a Vessel or Shipyard Project* means, as of any specified date, the aggregate, as determined by us, of all amounts paid by or for the account of the Obligor on or before that date and all amounts which the Obligor is then obligated to pay from time to time thereafter, for the construction, reconstruction or reconditioning of such Vessel or Shipyard Project.

*Advanced Shipbuilding Technology* means:

(1) Numerically controlled machine tools, robots, automated process control equipment, computerized flexible manufacturing systems, associated computer software, and other technology for improving shipbuilding and related industrial production which advance the state-of-the-art; and

(2) Novel techniques and processes designed to improve shipbuilding quality, productivity, and practice, and to promote sustainable development, including engineering design, quality assurance, concurrent engineering, continuous process production technology, energy efficiency, waste minimization, design for recyclability or parts reuse, inventory management, upgraded worker skills, and communications with customers and suppliers; and

(3) Other elements contributing to a shipyard's efficiency or productivity assisting it to more effectively operate in the shipbuilding industry.

*Citizen of the United States* means a person who, if an individual, is a Citizen of the United States by birth, naturalization or as otherwise authorized by law or, if other than an individual, meets the requirements of Section 2 of the Shipping Act, 1916, as amended (46 App. U.S.C. 802), as further described at 46 CFR 221.3(c).

*Closing* means a meeting of various participants or their representatives in a Title XI financing, at which a commitment to issue Guarantees is executed, or at which all or part of the Obligations are authenticated and issued and the proceeds are made available for a purpose set forth in section 1104(a) of the Act, or at which a Vessel is delivered and a Mortgage is executed as security to us or a Shipyard Project is completed and a Mortgage or other security is executed to us.

*Commitment Closing* means a meeting of various participants or their representatives in a Title XI financing at which a commitment to issue Guarantees is executed and the forms of the Obligations and the related Title XI



documents are also either agreed upon or executed.

*Depository* means a bank or other financial institution organized and doing business under the laws of the United States, any State or territory thereof, the District of Columbia or the Commonwealth of Puerto Rico that is authorized under such laws to exercise corporate trust powers, is a member of the Federal Deposit Insurance Corporation, and accepts deposits for purposes of implementing the program authorized by Title XI of the Act; but in the case of an Eligible Export Vessel can also mean, with our specific approval of foreign branches, but not the foreign subsidiaries, of such United States financial institutions.

*Depreciated Actual Cost of a Vessel or Shipyard Project* means the Actual Cost of the Vessel or Shipyard Project, as defined in this section (less a residual value of 2½ percent of United States shipyard construction cost or, in the case of Shipyard Project, a residual value as appropriate), depreciated on a straightline basis over the useful life of the Vessel or Shipyard Project as determined by us, not to exceed twenty-five years from the date the Vessel or Shipyard Project was delivered by the shipbuilder or manufacturer or, if the Vessel or Shipyard Project has been reconstructed or reconditioned, the Actual Cost of the Vessel or Shipyard Project depreciated on a straightline basis from the date the Vessel or Shipyard Project was delivered by the shipbuilder or manufacturer to the date of such reconstruction or reconditioning, on the basis of the original useful life of the Vessel or Shipyard Project, and from the date of said reconstruction or reconditioning on a straightline basis and on the basis of a useful life of the Vessel or Shipyard Project determined by us, plus all amounts paid or obligated to be paid for the reconstruction or reconditioning, depreciated on a straightline basis and on the basis of a useful life of the Vessel or Shipyard Project determined by us.

*Documentation* means all or part of the agreements relating to an entire Title XI financing which must be furnished to us, irrespective of whether we are a party to each agreement.

*Eligible Export Vessel* means a Vessel constructed, reconstructed, or reconditioned in the United States for use in world-wide trade which will, upon delivery or redelivery, be placed under or continued to be documented under the laws of a country other than the United States.

*Eligible Shipyard* means a private shipyard located in the United States.

*General Shipyard Facility* means:

(1) For operations on land, any structure or appurtenance thereto designed for the construction, repair, rehabilitation, refurbishment, or rebuilding of any Vessel, including graving docks, building ways, ship lifts, wharves and pier cranes; the land necessary for any structures or appurtenances; and equipment necessary for the performance of any function referred to in this definition; and

(2) For operations other than on land, any Vessel, floating drydock, or barge constructed in the United States, within the meaning of § 298.11(a), and used for, or a type that is usually used for, activities referred to in paragraph (1) of this definition.

*Guarantee* means the contractual commitment of the United States of America, represented by us, endorsed on each Obligation, to make payment to the Obligor or an agent, upon demand, of the unpaid interest on, and the unpaid balance of the principal of such Obligation, including interest accruing between the date of default and the date of payment.

*Guarantee Fee* means the fee payable to us in consideration for the issuance of the Guarantees.

*Indenture Trustee* means a bank with corporate trust powers, or a trust company, with a capital and surplus of at least \$25,000,000, which is located in and organized and doing business under the laws of the United States, any State or territory thereof, the District of Columbia or the Commonwealth of Puerto Rico, which has duties under the terms of a Trust Indenture, entered into with the Obligor, providing for the issuance and registration of the ownership and transfer of Obligations, the disbursement of funds held in trust by the Indenture Trustee for the redemption and payment of interest and principal with respect to Obligations, demands by the Indenture Trustee for payment under the Guarantees in the event of default and the remittance of payments received to the Obligees. Pursuant to our specific authorization, the Indenture Trustee may also authenticate the Guarantees.

*Letter Commitment* means a letter from us to you, setting forth specific determinations made by us with respect to your proposed project, as required by the Act and regulations of this part, and stating our commitment to execute Guarantees, subject to compliance by you with any conditions specified therein.

*Maritime Administration* means the agency created within the Department of Transportation by Reorganization Plan No. 21 of 1950 (64 Stat. 1273), amended

by Reorganization Plan No. 7 of 1961 (75 Stat. 840), as amended by Public Law 91-469 (84 Stat. 1036).

*Modern Shipbuilding Technology* means a technology to be introduced into the shipyard that is comprised of the best available proven technology, techniques, and processes appropriate to advancing the state-of-the-art of the applicant shipyard, or exceeds the best available processes of American shipbuilding, and that will enhance its productivity and make it more competitive internationally.

*Mortgage* means a first Preferred Mortgage on any Vessel or a first mortgage with respect to a Shipyard Project.

*Obligation* means any note, bond, debenture, or other evidence of indebtedness, as defined in section 1101(c) of the Act, issued for one of the purposes specified in section 1104(a) of the Act.

*Obligee* means the holder of an Obligation.

*Obligor* means any party primarily liable for payment of principal or of interest on any Obligation.

*Paying Agent* means any Person appointed by the Obligor to pay the principal of or interest on the Obligations on behalf of the Obligor.

*Person* means any individual, estate, foundation, corporation, partnership, limited partnership, joint venture, association, joint-stock company, trust, unincorporated organization or other acceptable legal business entity, government, or any agency or political subdivision thereof.

*Preferred Mortgage* means:

(1) In the case of a mortgage on a Vessel documented under United States law, whenever made, a mortgage that—

(i) Includes the whole of a Vessel;

(ii) Is filed in substantial compliance with 46 U.S.C. 31321;

(iii) Covers a documented Vessel or a Vessel for which an application for documentation has been filed that is in substantial compliance with the requirements of 46 U.S.C. Ch. 121 and the regulations prescribed under that Chapter by the United States Coast Guard; and

(iv) Is otherwise in compliance with the provisions of Chapter 313 of Title 46 of the U.S. Code.; and

(2) In the case of a mortgage on an Eligible Export Vessel, whenever made, a mortgage that—

(i) Constitutes a mortgage that is established as security on an Eligible Export Vessel under the laws of a foreign country;

(ii) Was executed under the laws of that foreign country and under which laws the ownership of the Vessel is documented;



(iii) Is registered under the laws of that foreign country in a public register at the port of registry of the Vessel or at a central office;

(iv) Otherwise satisfies the requirements of 46 U.S.C. 31301(6)(B) to constitute a Preferred Mortgage; and

(v) Has us as the mortgagee, or such other mortgagee as is permitted by the applicable foreign law and approved by us.

*Related Party* means as that term is defined by generally accepted accounting principles outlined in paragraph 24 of Statement of Financial Accounting Standards No. 57, Related Party Disclosures.

*Secretary* means the Secretary of Transportation, acting by and through the Maritime Administrator, Department of Transportation, the Maritime Administrator or any official of the Maritime Administration to whom is duly delegated the authority, from time to time, to perform the functions of the Secretary of Transportation or the Maritime Administrator, Department of Transportation.

*Secretary's Note* means a promissory note from the Obligor to the Secretary in an amount equal to the aggregate amount of the Obligations, which is issued simultaneously with the Guarantees.

*Security Agreement* means the primary contract between the Obligor and the Secretary, providing for the transfer to the Secretary by the Obligor of all right, title and interest of the Obligor in certain described property (including rights under contracts in existence or to be entered into), and containing other provisions relating to representations and responsibilities of the Obligor to the Secretary as security for the issuance of Guarantees.

*Shipyard Project* means Advanced Shipbuilding Technology and Modern Shipbuilding Technology or both unless otherwise specified.

*Vessel* means all types of vessels, whether in existence or under construction, including passenger, cargo and combination passenger-cargo carrying vessels, tankers, towboats, barges and dredges which are or will be documented under the laws of the United States, floating drydocks which have a capacity of at least thirty-five thousand or more lifting tons and a beam of one hundred and twenty-five feet or more between the wing walls and oceanographic research or instruction or pollution treatment, abatement or control vessels, which are owned by citizens of the United States; except that an Eligible Export Vessel will not be documented under the laws of the United States.

### § 298.3 Applications

(a) *Process and certification.* When you apply for a commitment to execute Guarantees, you must:

(1) Complete Form MA 163 and send it to the Secretary, Maritime Administration, U.S. Department of Transportation, 400 Seventh Street, SW., Washington, DC 20590.

(2) Certify the application in the manner that Form MA 163 prescribes.

(b) *Required information.* You must include all required information on Form MA 163 or in attached exhibits and schedules submitted with the application. You must also include the following regarding the Vessel or Vessels, if applicable:

- (1) Any demise charters,
- (2) Time charters in excess of six months,
- (3) Contracts of affreightment,
- (4) Drilling contracts, and/or
- (5) Other contractual arrangements.

(c) *Declaration of Lobbying form.* You must also file the Declaration of Lobbying form as required by 31 U.S.C. 1352 with the initial application as part of the formal submission.

(d) *Attachments.* Each exhibit, schedule, and attachment must contain a statement, on the first page clearly identifying the document as an attachment to the application. You must state on each attachment the:

- (1) Name of the applicant; and
- (2) Date of the application.

(e) *Amendment.* You must mark "Amendment," on any amendment of data contained in the application. Each first page must contain a statement clearly identifying the document as an amendment to your application and must include the:

- (1) Name of the applicant;
- (2) Date of application; and
- (3) Certification required on Form MA 163.

(f) *Application time schedule.* You must submit each application to us at least four (4) months prior to the anticipated date by which you require a Letter Commitment.

(1) We may consider applications with less than four (4) months notice, prior to the anticipated date by which you require a Letter Commitment, if you submit written documentation to us that extenuating circumstances exist.

(2) During the first fifteen (15) calendar days after you submit your application, we will preliminarily review your application for adequacy and completeness.

(i) If we find that your application is incomplete, or if we require additional data, we will notify you promptly in writing, and you will have fifteen (15) calendar days, from the date of each

request for additional information, to correct deficiencies.

(ii) If you have not corrected the deficiencies or have not made substantial progress toward correcting them, within the 15 calendar days, then we may terminate the processing of your application without prejudice.

(3) Once we consider your Title XI application complete, we will act on the application within a period of 60 calendar days, unless for good cause, we find it necessary to extend the 60 day period.

(4) If you do not complete your application and we do not act upon your application within four (4) months from the submission date, unless we extend the time period, we will notify you in writing that processing of the application is terminated and that you may reapply at a later date.

(i) If we terminate your application without prejudice, we will not require you to pay a new filing fee for a later application for a similar project that you file within one year of the termination date.

(ii) If you submit an application for a substantially different project, you must pay a new filing fee. We will determine whether the application is substantially different on a case-by-case basis.

(5) If we issue you a Letter Commitment, you must submit two (2) sets of the Closing documentation to us for review at least six (6) weeks prior to the anticipated Closing. The six weeks time period will give us time to complete an adequate review of the documentation. You must use our standard form of documentation.

(g) *Degrees of risk.* When processing applications, we will consider the different degrees of risk involved with different applications.

(h) *Additional assurances.* Before we approve your application, we may require additional assurances if you are not a well established firm with strong financial qualifications and strong market shares seeking financing guarantees for replacement vessels in an established market in which projected demand exceeds supply. The additional assurances may include:

- (1) Firm charter commitments;
- (2) Parent company guarantees;
- (3) Greater equity participation;
- (4) Private financing participation;
- (5) Security interest on other property; and
- (6) Similar arrangements to any of these additional assurances.

(i) *Filing Fee.* When you submit your application, you must include a \$5,000 filing fee, which will be non-refundable, irrespective of whether we issue a Letter Commitment. However, the \$5,000

filing fee is credited toward the investigation fee described in § 298.15(b).

(j) *Confidential Information.* (1) If we receive a request for release of your information, we will notify you. If you believe that your application, including attachments, contains information you consider to be trade secrets or commercial or financial information and privileged or confidential, or otherwise exempt from disclosure under the Freedom of Information Act (FOIA) (5 U.S.C. 552), you may assert a claim of confidentiality. When submitting your application, you should mark "Confidential" on the pages that you consider confidential. The same requirement applies to any amendment to the application.

(2) *FOIA requests.* We will apply the procedures contained in the Department of Transportation's regulations at 49 CFR 7.17 regarding FOIA requests for information that the submitter has designated as confidential. We will consider your claim of confidentiality at the time someone requests the information under FOIA.

(3) *Statement of objections.* If we receive a request for release of your information, we will notify you. We will give you a reasonable period of time to give us a written, detailed statement explaining your objections to our release of the information. We will not give you notice if:

- (i) We determine that we should not disclose the information;
- (ii) The information has been lawfully published or made available to the public; or
- (iii) Law (other than 5 U.S.C. 552) requires us to disclose the information.

(4) *Our notification of intent to disclose.* If your objections to release of the information do not persuade us, we will notify you of our intent to disclose in a reasonable number of days before we intend to disclose the information. The written notice will include:

- (i) A statement explaining our reasons for not accepting the submitter's disclosure objections;
  - (ii) A description of the business information that we will disclose; and
  - (iii) A specific disclosure date.
- (k) *Priority.* We will give priority for processing applications to:

- (1) Vessels capable of serving as a United States naval and military auxiliary in time of war or national emergency,
- (2) Requests for financing construction of equipment or vessels less than one year old as opposed to the refinancing of existing equipment or vessels that are one year old or older,

(3) Any applications involving the purchase of vessels currently financed under Title XI if the purpose is to process the assumption of the obligations,

(4) Applications from those willing to take guarantees for less than the normal term for that class of vessel.

(5) *Eligible Export Vessels.* We may issue a commitment to guarantee Obligations for an Eligible Export Vessel if we determine, in our sole discretion, that the issuance of a commitment to guarantee Obligations for an Eligible Export Vessel will not cause us to deny an economically sound application to issue a commitment to guarantee Obligations for vessels documented under the laws of the United States operating in the domestic or foreign commerce of the United States, after considering:

- (i) The status of pending applications for commitments to guarantee obligations for vessels documented under the laws of the United States and operating or to be operated in the domestic or foreign commerce of the United States;
- (ii) The economic soundness of the applications referred to in paragraph (k)(5)(i) of this section; and
- (iii) The amount of guarantee authority available.

(Unless indicated otherwise in this part 298, information collection requirements have been approved by the Office of Management and Budget under control number 2133-0018.)

## Subpart B—Eligibility

### § 298.10 Citizenship.

(a) *Applicability.* Before you receive a legal or beneficial interest in a Vessel financed under Title XI of the Act which is operating in or will be operated in the U.S. coastwise trade, you and any other Person, (including the shipowner and any bareboat charterer), must establish your United States citizenship, within the definition of "Citizen of the United States" in § 298.2.

(b) *Prior to Letter Commitment.* Before we issue the Letter Commitment, you and any Person identified in paragraph (a) of this section, who is required to establish United States citizenship must establish United States citizenship in the form and manner stated in 46 CFR part 355.

(c) *Commitment Closing.* (1) Within 10 days before every Commitment Closing, unless we waive this requirement for good cause, you and all Persons identified with the project who have previously established United States citizenship in accordance with

paragraphs (a) and (b) of this section, must submit pro forma Supplemental Affidavits of Citizenship which we have approved for Closing as to form and substance, and

(2) On the date of the Closing, three (3) executed copies of Supplemental Affidavits of Citizenship that:

- (i) Show evidence of the continuing United States citizenship of the Persons in paragraph (a) of this section; and
- (ii) Bear the date of the Closing.

(d) *Additional information.* If we request additional material essential to clarify or support evidence of U.S. citizenship, you, the Obligor, or any Person identified in paragraph (a) of this section must submit the additional information.

(Approved by the Office of Management and Budget under control number 2133-0012.)

### § 298.11 Vessel requirements.

When you apply for a Guarantee, the Vessel for which you intend to receive financing for construction, reconstruction, or reconditioning must meet the following criteria:

(a) *United States Construction.* A Vessel, including an Eligible Export Vessel, financed by an Obligation Guarantee must be constructed in the United States. United States construction means that the Vessel is assembled in a shipyard geographically located within the United States.

(1) A U.S.-flag Vessel must meet the applicable United States Coast Guard requirements.

(2) An Eligible Export Vessel must be constructed in accordance with the requirements of the International Maritime Organization and must meet the applicable:

- (i) Laws, rules, and regulations of its country of documentation,
- (ii) Treaties, conventions on international agreements to which that country is a signatory, and
- (iii) Laws of the ports it serves.

(b) *Actual Cost.* We must approve your estimated Actual Cost for the construction, reconstruction, or reconditioning of a Vessel as a condition for issuance of the Letter Commitment. The estimated cost of the Vessel may include escalation for the anticipated construction period of the Vessel. We may contact the shipyard directly and may require you to have the shipyard that has contracted to build the Vessel to submit additional technical data, backup cost details, and other evidence if we have insufficient data.

(c) *Class, condition, and operation.* The Vessel must be constructed, maintained, and operated so as to meet the highest classification, certification,

rating, and inspection standards for vessels of the same age and type imposed by:

(1) The American Bureau of Shipping (ABS), or

(2) Another classification society that also meets the inspection standards of the United States Coast Guard with respect to the documentation of U.S.-flag vessels, or

(3) In the case of an Eligible Export Vessel, such standards as may be imposed by a member of the International Association of Classification Societies (IACS), classification societies to be ISO 9000 series registered or Quality Systems Certificate Scheme qualified IACS members who have been recognized by the United States Coast Guard as meeting acceptable standards with such recognition including, at a minimum, that the society meets the requirements of IMO Resolution A.739(18) with appropriate certificates required at delivery, so long as the home country of the IACS member accords equal reciprocity, as determined by us, to United States classification societies.

(4) Except in the case of an Eligible Export Vessel, the Vessel must be in compliance with all applicable laws, rules, and regulations as to condition and operation, including, but not limited to, those administered by the:

- (i) United States Coast Guard,
- (ii) Environmental Protection Agency,
- (iii) Federal Communications Commission,
- (iv) Public Health Service, or
- (v) Their respective successor agencies, and

(vi) All applicable treaties and conventions to which the United States is a signatory, including, but not limited to, the International Convention for Safety of Life at Sea.

(d) *Documentation.* (1) An Eligible Export Vessel must be documented in a country that is party to the International Convention for Safety of Life at Sea, or other treaty, convention, or international agreement governing vessel inspection to which the United States is a signatory, and must comply with the applicable laws, rules, and regulations of its country of documentation, all applicable treaties, conventions on international agreements to which that country is a signatory, and the laws of the ports it serves.

(2) All other Eligible Vessels must be documented under U.S. registry.

(e) *Reconstruction or reconditioning.* Repairs necessary for the Vessel to meet the classification standards approved by us, or any regulatory body, or for previous inadequate maintenance and

repair, will not constitute reconstruction or reconditioning within the meaning of this paragraph.

(f) *Condition survey.* If your application involves a reconstructed or reconditioned Vessel, you must make the Vessel available at a time and place acceptable to us so that we may conduct a condition survey. You must:

(1) Pay the cost of the condition survey.

(2) Ensure that the scope and extent of the condition survey will not be less effective than that required by the last ABS special survey completed (if the Vessel is classified), next due or overdue, whichever date is nearest in accordance with the Vessel's age.

(3) Ensure that the Vessel meets the standard of the survey necessary for retention of class (if the Vessel is classified), and

(4) Ensure that the operating records of the Vessel reflect normal operation of the Vessel's main propulsion and other machinery and equipment, consistent with accepted commercial experience and practice.

(g) *Metric Usage.* Our preferred system of measurement and weights for Vessels and Shipyard Projects is the metric system.

#### **§ 298.12 Applicant and operator's qualifications.**

(a) *Operator's qualifications.* We will not issue a Letter Commitment without a prior determination that you, the bareboat charterer, or other Person identified in the application as the operator of the Vessel(s) or Shipyard Project, possesses the necessary experience, ability and other qualifications to properly operate and maintain the Vessel(s) or Shipyard Project which serve as security for the Guarantees. You must also comply with all requirements of this part.

(b) *Identity and ownership of applicant.* In order for us to assess the likelihood that the project will be successful, we need information about you and the proposed project. To permit this assessment, you must provide the following information in your application for Title XI guarantees:

(1) *Incorporated companies.* If you or any bareboat charterer is an incorporated company, you must submit the following identifying information:

(i) Name of company, place and date of incorporation, and tax identification number, or if appropriate, international identification number of the company;

(ii) Address of principal place of business; and

(iii) Certified copy of certificate of incorporation and bylaws.

(2) *Partnerships, limited partnerships, limited liability companies, joint*

*ventures, associations, unincorporated companies.* If you or any bareboat charterer is a partnership, limited partnership, limited liability company, joint venture, association, or unincorporated company, you must submit the following identifying information:

(i) Name of entity, place and date of formation, and tax identification number, or if appropriate, international identification number of entity;

(ii) Address of principal place of business; and

(iii) Certified copy of certificate of formation, partnership agreement or other documentation forming the entity.

(3) *Other entities.* For any entity that does not fit the descriptions in paragraphs (b)(1) and (b)(2) of this section, we will specify the information that the entity must submit regarding its identity and ownership.

(4) You and any bareboat charterer must provide a brief statement of the general effect of each voting agreement, voting trust or other arrangement whereby the voting rights of any interest in you or the bareboat charterer are controlled or exercised by any person who is not the holder of legal title to such interest.

(5) You and any bareboat charterer must provide the following information regarding the entity's officers, directors, partners or members:

(i) Name and address;

(ii) Office or position; and

(iii) Nationality and interest owned (for example, shares owned and whether voting or non-voting).

(c) *Business and affiliations of applicants.* You must include:

(1) A brief description of your principal business activities during the past five years.

(2) A list of all business entities that directly or indirectly, through one or more intermediaries, control, are controlled by, or are under common control with you.

(3) The nature of the business transacted by each listed entity and the relationship between these entities. This information may be presented in the form of a chart.

(4) Whether any of the affiliated entities have previously applied for or received Title XI assistance.

(5) A statement indicating whether the applicant, any predecessor or affiliated entity has been in bankruptcy or reorganization under any insolvency or reorganization proceeding and if so, give details.

(6) A statement indicating whether the applicant or any predecessor or affiliated entity is now, or during the past five years has been, in default

under any agreement or undertaking with others or with the United States of America, or is currently delinquent on any Federal debt, and if so, provide explanatory information.

(7) A list of your banking references:

- (i) Principal bank(s) or lending institutions(s)—name and address;
- (ii) Nature of relationship; and
- (iii) Individual references—name(s), telephone and fax number of banking officer(s).

(d) *Management of applicant.* You must include:

(1) A brief description of the principal business activities during the past five years of each officer, director, partner or member you listed in paragraph (b)(5) of this section and if these persons (have) act(ed) as executive officers in other entities, indicate the names of these entities and whether such entities have defaulted on any U.S. Government debt, and

(2) The name and address of each organization engaged in business activities which have a direct financial relationship to those carried on or to be carried on by you with which any person listed in paragraph (d)(1) of this section has any present business connection, the name of each such person and, briefly, the nature of such connection.

(e) *Applicant's property and activity.* You must provide:

(1) A brief description of the general character and location of the principal assets employed in your business and those of your affiliate, other than vessels. Describe financial encumbrances, if any;

(2) A general description of the vessels currently owned and/or operated by you or your affiliates and a description of the areas of operation; and,

(3) In the case of an Eligible Shipyard which is an applicant for a guarantee for a Shipyard Project, a brief description of the general character (that is, the number of building ways, launch method, drydocks and size) and location (that is, water depth, length of riverfront) of the principal properties of the applicant employed in its business. You must also describe any financial encumbrances.

(f) *Operating ability.* (1) You must submit a detailed statement showing your ability to successfully operate the financed Vessel(s).

(2) If a company other than you will operate the Vessel(s), then the information in paragraph (f)(1) of this section must be provided for the operating company together with a copy of the operating agreement.

(3) You must submit a copy of any management agreement(s) between you and any related or unrelated organization(s) which will affect the management of the Title XI Vessel or shipyard.

(4) In the case of an Eligible Shipyard, which is an applicant for a guarantee for a Shipyard Project, a detailed statement must be submitted showing your ability to successfully operate the Shipyard Project and construct/reconstruct Vessels, including name, education, background of, and licenses held by, all senior supervisory personnel concerned with the physical operation of the Shipyard Project.

(5) Where an operator has an historical performance record, we will consider this record in evaluating your operating ability. For newly formed entities, we will evaluate the performance of affiliates and/or companies associated with the principals (where the principals have a significant degree of control) in determining your operating ability. However, unless the affiliates or principals have an obligation with respect to the debt, we will not consider historical performance in evaluating your creditworthiness.

#### **§ 298.13 Financial requirements.**

(a) *In general.* To be eligible for guarantees, you and/or your parent organization (when applicable), and any other participants in the project having a significant financial or contractual relationship with you must submit information, respectively, on their financial condition. You must submit this information at the time of the application. You must supplement this information if we require it in subsequent requests. You must submit information satisfactory to us to show that financial resources are available to support the Title XI project.

(b) *Cost of the project.* You must submit the following cost information with respect to the project:

(1) *Vessel financing Guarantees.* A detailed statement of the estimated Actual Cost of construction, reconstruction, or reconditioning of the Vessel(s) including those items which would normally be capitalized as Vessel construction costs. Net interest during construction is the total estimated construction period interest on non-equity funds less estimated earnings from the escrow fund, if such fund is to be established prior to Vessel(s) delivery.

(2) *Foreign components.* (i) You must exclude each item of foreign components and services from Actual Cost, unless we specifically grant a

waiver for the item. We will not grant a waiver for major foreign components of the hull and superstructure.

(ii) In deciding whether to grant a waiver for foreign components and services, we will consider your certification, to be reviewed by us, stating that:

(A) A foreign item or service is not available in the United States on a timely or price-competitive basis, or

(B) The domestic item or service is not of sufficient quality.

(iii) Although excluded from Actual Cost, foreign components of the hull and superstructure can be regarded as owner-furnished equipment that may be used in satisfying your equity requirements imposed by paragraph (f) of this section.

(3) *Costs incurred by written contracts.* If any of the costs have been incurred by written contracts such as shipyard contract, management or operating agreement, you should forward signed copies with the application. We may require you to have the contracting shipyard submit back-up cost details and technical data. You must submit this information in the format given in the Title XI application procedures.

(4) *Shipyard Project.* In the case of Shipyard Project, a detailed statement of the actual cost of such technology, including those items which would normally be capitalizable. If you incurred any of the costs through written contracts, you should forward signed copies of the contract with the application. We may require you to have manufacturers submit back-up cost details and technical data. You must submit this information in the format given in the Title XI application procedures.

(5) *Shore facilities, cargo containers, etc.* A detailed statement showing the actual cost of any shore facilities, cargo containers, etc., required to be purchased in conjunction with the project.

(6) *Additional project costs.* A detailed statement showing any other costs associated with the project which were not included in paragraphs (b)(1) through (5) of this section, such as:

- (i) Legal and accounting fees;
- (ii) Printing costs;
- (iii) Vessel insurance;
- (iv) Underwriting fees;
- (v) Fee to a Related Party; and
- (vi) Other fees.

(7) *Request for Actual Cost Approval and Reimbursement.* If the project involves refinancing, you must also submit the exhibit entitled Request for Actual Cost Approval and Reimbursement, its summary sheet and

supplemental schedules at the time of filing the application.

(c) *Financing.* (1) You must:

(i) Describe, in detail, how the costs of the project (sums referred to in paragraph (b) of this section) will be funded and the timing of such funding.

(ii) Include any vessel trade-ins, related or third party financings, etc.

(iii) Provide the proposed terms and conditions of all private funding, from both equity and debt sources and clearly identify all parties involved.

(iv) Obtain our approval of the terms and conditions for co-financing (involving a blend of Title XI and private financing for the debt portion), including the ability of the co-financiers to exercise their rights against collateral shared with us for any transaction.

(v) Demonstrate with financial statements that at least 12½ percent, or 25 percent as applicable, of the construction or reconstruction costs of the Vessel(s) or the cost of the Shipyard Project will be in the form of equity and not additional debt, except to the extent allowed by paragraph (h) of this section.

(vi) Disclose all of the Vessel(s), Shipyard Project financing in the format given in the Title XI application procedures.

(2) *Financial Information.* You must provide us with financial statements, prepared in accordance with U.S. generally accepted accounting principles (GAAP), and include notes that explain the basis for arriving at the figures except that for Eligible Export Vessels, your financial statements must be in accordance with GAAP if formed in the U.S., or reconciled to GAAP if formed in a foreign country unless a satisfactory justification is provided explaining the inability to reconcile. The financial statements must include the following:

(i) The most recent financial statements for you, your parent company and other significant participants, as applicable (year end or intermediate), and the three most recent audited statements with details of all existing debt. If you are a new entity and are to be funded from or guaranteed by external source(s), you must provide such statements for such source(s);

(ii) Your pro forma balance sheet and that of any guarantor (if applicable) as of the estimated date of execution of the Guarantees reflecting the assumption of the Title XI Obligations, including the current liability; and

(iii) Your pro forma balance sheets and that of the guarantor (if applicable) for five years after the Closing.

(Approved by the Office of Management and Budget under control number 2133-0005.)

(d) *Financial definitions.* For the purpose of this section and §§ 298.35 and 298.42 of this part:

(1) “Company” means any Person subject to financial requirements imposed under paragraph (f) of this section and in § 298.35, as well as the reporting requirements imposed by § 298.42.

(2) “Working Capital” means the excess, if any, of current assets over current liabilities, both determined in accordance with GAAP and adjusted as follows:

(i) In determining current assets you must exclude:

(A) Any securities, obligations or evidence of indebtedness of a Related Party or of any stockholder, director, officer or employee (or any member of his family) of the Company or of such Related Party, except advances to agents required for the normal current operation of the Company’s vessels and current receivables arising out of the ordinary course of business and not outstanding for more than 60 days; and

(B) An amount equal to any excess of untermiated voyage revenue over untermiated voyage expenses.

(ii) In determining current liabilities, you must deduct any excess of untermiated voyage expenses over untermiated voyage revenue and add one half of all annual charter hire and other lease obligations (having a term of more than six months) due and payable within the succeeding fiscal year, other than charter hire and such other lease obligations already included and reported as a current liability on the Company’s balance sheet.

(3) “Equity” or “net worth” means, as of any date, (the total of paid-in-capital stock, paid-in surplus, earned surplus and appropriated surplus,) and all other amounts that would be included in net worth in accordance with GAAP, but does not include:

(i) Any receivables from any stockholder, director, Officer or employee (or their family) of the Company or from any Related Party (other than current receivables arising out of the ordinary course of business and not outstanding for more than 60 days), and

(ii) Any increment resulting from the reappraisal of assets.

(4) “Long-Term Debt” means, as of any date, the total notes, bonds, debentures, equipment obligations and other evidence of indebtedness that would be included in long term debt in accordance with GAAP. You must include any guarantee or other liability for the debt of any other Person not otherwise included on the balance sheet.

(5) “Capitalizable Cost” means the aggregate of the Actual Cost of the Vessel or Shipyard Project and those other items which customarily would be capitalized as Vessel costs or Shipyard Project costs under GAAP.

(6) “Depreciated Capitalizable Cost” means the Capitalizable Cost of a Vessel or Shipyard Project, depreciated on a straightline basis over the same useful life as determined by us for Actual Cost, and depreciated as required by § 298.21(g).

(e) *Applicability.* The financial resources must be adequate to meet the Equity requirements in the project and Working Capital requirements, as set forth in paragraph (f) of this section.

(1) The various financial requirements shall be met by the owner of the Vessel or Vessels or Shipyard Project to be security to us for the Guarantees, except that if the owner is not the operator, the overall financial requirements will be allocated among the owner, the operator and other parties as determined by us.

(2) The Company must satisfy the applicable financial requirements, in addition to any other financial requirements already imposed or which may be imposed upon it in connection with other Vessels financed under the Title XI program or in connection with other Shipyard Project financed under the Title XI program.

(3) A determination as to whether the Company has satisfied all financial requirements shall be based on the assumption that the projected financing has been completed. Accordingly, you must submit:

(i) A pro forma balance sheet at the time of the application, reflecting any adjustment made pursuant to paragraph (f)(1)(i) of this section, and

(ii) A revised pro forma balance sheet, reflecting the completion of the projected financing, at least five business days before the first Closing at which the Obligations are issued.

(f) *Financial requirements at Closing.* Financial requirements can apply to one or more Companies, and are determined as follows:

(1) Owner as operator. Where the owner is to be the Vessel operator, minimum requirements at Closing usually are as follows:

(i) Working Capital. The Company’s Working Capital shall not be less than one dollar. This Working Capital requirement is based on the premise that the Company engages in a service-type activity with only normal vessel inventory. If Working Capital includes other inventory, in addition to such normal Vessel inventory, we may adjust the requirement as appropriate. Also, if we determine that the Company’s

Working Capital includes amounts receivable that it reasonably could not expect to collect within one year, we may make adjustments to the Working Capital requirements.

(ii) Long-Term Debt. The Company's Long-Term Debt must not be greater than twice its Equity.

(iii) Equity (net worth). The Company's Equity must be:

(A) The greater of:

(1) 50 percent of its Long-Term Debt; or

(2) 90 percent of its Equity as shown on the last audited balance sheet, dated not earlier than six months before the date of issuance of the Letter Commitment; or

(B) Such other amount as may be specified by us.

(2) Lessee or charterer as operator. Where a lessee or charterer is to be the Vessel operator, minimum requirements at Closing usually are as follows:

(i) Working Capital. The operator's Working Capital requirement will be the same as that which would have otherwise been imposed on the owner as operator under paragraph (f)(1)(i) of this section and based on the same premise stated in that paragraph.

(ii) Long-Term Debt. The operator's Long-Term Debt will be the same as that which would have otherwise been imposed on the owner as operator under paragraph (f)(1)(ii) of this section.

(iii) Equity (net worth). The operator's equity requirement will be the same as that which would have otherwise been imposed on the owner as operator under paragraph (f)(1)(iii) of this section.

(iv) The owner's Equity shall at least be equal to the difference between the Capitalizable Cost or Depreciated Capitalizable Cost of the Vessel (whichever is applicable) and the total amount of the Guarantees.

(3) Owner as General Shipyard Facility. Where the owner of Shipyard Project is a General Shipyard Facility, minimum requirements at Closing will be the same as those set forth in paragraph (f)(1) of this section for an owner as operator.

(g) *Adjustments to financial requirements at Closing.* If the owner, although not operating a Vessel, assumes any of the operating responsibilities, we may adjust the respective Working Capital and Equity requirements of the owner and operator, otherwise applicable under paragraph (f) of this section, by increasing the requirements of the owner and decreasing those of the operator by the same amount.

(h) *Subordinated debt considered to be Equity.* With our consent, part of the Equity requirements applicable under

paragraphs (c) and (f) of this section may be satisfied by debt, fully subordinated as to the payment of principal and interest on the Secretary's Note and any claims secured as provided for in the Security Agreement or the Mortgage. Repayment of subordinated debt may be made only from funds available for payment of dividends or for other distributions, in accordance with requirements of the Title XI Reserve Fund and Financial Agreement (described in § 298.35). Such subordinated debt shall not be secured by any interest in property that is security for Guarantees under Title XI, unless the Obligor and the lender enter into a written agreement, satisfactory to us, providing, among other things, that if any Title XI financing or advance by us to the Obligor shall occur in the future, such security interest of the lender shall become subordinated to any indebtedness to us incurred by the Obligor and to any security interest obtained by us in that property or other property, with respect to the subsequent indebtedness.

(i) *Modified requirements.* We may waive or modify the financial terms or requirements otherwise applicable under this section and §§ 298.35 and 298.42, upon determining that there is adequate security for the Guarantees. We may impose similar financial requirements on any Person providing other security for the Guarantees.

#### **§ 298.14 Economic soundness.**

(a) *Economic Evaluation.* We shall not issue a Letter Commitment for guarantees unless we find that the proposed project, regarding the Vessel(s) or Shipyard Project for which you seek Title XI financing or refinancing, will be economically sound. The economic soundness and your ability to repay the Obligations will be the primary basis for our approval of a Letter Commitment. We will consider the value of the collateral for which we will issue the Obligations as only a secondary consideration in determining your ability to repay the Obligations.

(b) *Basic feasibility factors.* In making the economic soundness findings, we shall consider all relevant factors, including, but not limited to:

(1) The need in the particular segment of the maritime industry for new or additional capacity, including any impact on existing equipment for which a guarantee under this title is in effect;

(2) The market potential for the employment of the Vessel or utilization of the Shipyard Project of a General Shipyard Facility over the life of the guarantee;

(3) Projected revenues and expenses associated with employment of the Vessel or utilization of the Shipyard Project of a General Shipyard Facility;

(4) Any charters, contracts of affreightment, transportation agreements, or similar agreements or undertakings relevant to the employment of the Vessel or utilization of the Shipyard Project of a General Shipyard Facility;

(5) For inland waterways, the need for technical improvements including but not limited to increased fuel efficiency, or improved safety; and

(6) Other relevant criteria.

(c) *Project Feasibility.* To demonstrate the economic feasibility of the project over the Guarantee period, you must submit the following information:

(1) *Purpose.* A detailed purpose for the obligations to be guaranteed.

(2) *Necessary exhibits.* Necessary exhibits to support your project feasibility as supplements to the application.

(3) *Relevant market information.* Information regarding the relevant market including a written narrative of the market (or potential market) for the project including full details on the following, as applicable:

(i) Nature and amount of cargo/passengers available for carriage and your projected share (provide also the number of units; that is containers, trailers, etc.);

(ii) Services or routes in which the Vessel(s) will be employed, including an itinerary of ports served, with the arrival and departure times, sea time, port time, hours working or idle in port, off hire days and reserve or contingency time, proposed number of annual sailings and number of annual working days for the Vessel(s) or, with respect to Shipyard Project, how the equipment will be employed;

(iii) Suitability of the Vessel(s) or Shipyard Project for their anticipated use;

(iv) Significant factors influencing your expectations for the future market for the Vessel(s) or Shipyard Project, for example, competition, government regulations, alternative uses, and charter rates; and

(v) Particulars of any charters, contracts of affreightment, transportation agreements, etc. You should supplement the narrative by providing copies of any marketing studies and/or supporting information (for instance, existing or proposed charters, contracts of affreightment, transportation agreements, and letters of intent from prospective customers).

(vi) The potential for purchasing existing equipment of a reasonable

condition and age from another source, including information regarding:

(A) Market assessment concerning the availability and cost of existing equipment that may be an alternative to new construction or the new Shipyard Project;

(B) The cost of modification, reconditioning, or reconstruction of existing equipment to make it suitable for intended use; and

(C) Descriptions of any bids or offers which you had made to purchase existing equipment, especially Vessels which currently are financed with Title XI Obligations including date of offer, Vessels, and amount of offer.

(4) *Revenues.* A detailed statement of the revenues expected to be earned from the project based upon the information in paragraph (c) of this section. Vessel revenue projections shall include shipping/hire rates for current market conditions or market conditions expected to exist at the time of Vessel delivery taking into account seasonal or temporary fluctuations. The revenues shall be based on a realistic estimate of the Vessel(s) or the new Shipyard Project utilization rate and at a breakeven rate for the project. A justification for the utilization rate shall be supplied and should indicate the number of days per year allowed for maintenance, drydocking, inspection, etc.

(5) *Expenses for Vessel financing.* For applications for Vessel financing, a detailed statement of estimated Vessel expenses including the following (where applicable):

(i) Estimated Vessel daily operating expenses, including wages, insurance, maintenance and repair, fuel, etc. and a detailed projection of anticipated costs associated with long term maintenance of the Vessel(s) such as drydocking and major mid-life overhauls, with a time frame for these events over the period of the Guarantee;

(ii) If applicable, a detailed breakdown of those expenses associated with the Vessel(s) voyage, such as port fees, agency fees and canal fees that are assessed as a result of the voyage; and

(iii) A detailed breakdown of annual capital costs and administrative expenses, segregated as to:

(A) Interest on debt;

(B) Principal amortization; and

(C) Salaries and other administrative expenses (indicate basis of allocation).

(6) *Expenses for a Shipyard Project.* For applications for a Shipyard Project, a statement of estimated expenses related to the Shipyard Project, including the following (where applicable):

(i) A detailed breakdown of estimated daily operating expenses for the shipyard, such as wages, including staffing, and segregated as to straight-time, overtime and fringe benefits; utility costs; costs of stores, supplies, and equipment; maintenance and repair cost; insurance costs; and, other expenses (indicate items included); and

(ii) A detailed breakdown of annual capital costs and administrative expenses, segregated as to:

(A) Interest on debt;

(B) Principal amortization; and

(C) Salaries and other administrative expenses (indicate basis of allocation).

(7) *Forecast of Operations.* Utilizing the revenues and expenses provided in paragraphs (c)(4),(5) and (6) of this section, you shall provide a forecast of operating cash flow, as defined in paragraph (d)(4) of this section, for the Title XI project for the first full year of operations and the next four years. The cash flow statements should be footnoted to explain the assumptions used.

(d) *Objective Criteria.* We must make a finding of economic soundness as to each project based on an assessment of the entire project. In order for the project to receive approval, we must determine that a project meets the following criteria:

(1) The projected long-term demand (equal to length of time that you request financing) for the particular Vessel(s) or new Shipyard Project to be financed must exceed the supply of similar vessels or new shipyard project in the applicable markets. We will determine the supply of similar vessels and similar shipyard projects based on:

(i) Existing equipment,

(ii) Similar vessels or new shipyard project under construction, and

(iii) The projected need for new equipment in that particular segment of the maritime industry.

(2) We will base our determination of the project's economic soundness on the following:

(i) Conformity of your projections with our supply and demand analyses;

(ii) Availability of charters, letters of intent, outstanding contractual commitments, contracts of affreightment, transportation agreements or similar agreements or undertakings; and

(iii) Your existing market share compared with the market share necessary to meet projected revenues.

(3) In cases where market conditions are temporarily inadequate for you to service the Obligation indebtedness at the time of Vessel delivery, or completion of the Shipyard Project, we may approve your application only if

you have sufficient outside sources of cash flow to service your indebtedness during this temporary period.

(4) With respect to the asset for which Obligations are to be issued, the operating cash flow to Obligation debt service ratio over the term of the Guarantee must be in excess of 1:1. Operating cash flow means revenues less operating and capital expenses including taxes paid but exclusive of interest, accrued taxes, depreciation and amortization for the Title XI asset. Debt service means interest plus principal.

#### **§ 298.15 Investigation fee.**

(a) *In general.* Before we issue a Letter Commitment, you shall pay us an investigation fee. The Letter Commitment will state the fee which is based on the formula in paragraph (b) of this section.

(1) The investigation fee covers the cost of the investigation of the project described in the application and the participants in the project, the appraisal of properties offered as security, Vessel inspection during construction, reconstruction, or reconditioning (where applicable) and other administrative expenses.

(2) If, for any reason, we disapprove the application, you shall pay one-half of the investigation fees.

(b) *Base Fee.* (1) The investigation fee shall be one-half ( $\frac{1}{2}$ ) of one percent on Obligations to be issued up to and including \$10,000,000, plus

(2) One-eighth ( $\frac{1}{8}$ ) of one percent on all Obligations to be issued in excess of \$10,000,000.

(c) *Credit for filing fee.* You will receive credit for the \$5,000 filing fee that you paid upon filing the original application (described in § 298.3) towards the investigation fee.

#### **§ 298.16 Substitution of participants.**

(a) You may request our permission to substitute participants to a Mortgage and/or Security Agreement in a financing that is receiving assistance authorized by Title XI of the Act.

(b) A non-refundable fee of \$3,000 is due, payable at the time of the request. The fee defrays all costs of processing and reviewing a joint application by a mortgagor and/or Obligor and a proposed transferee of a Vessel or Shipyard Project, which is security for Title XI debt, if the proposed transferee is to assume the Mortgage and/or the Security Agreement.

#### **§ 298.17 Evaluation of applications.**

(a) In evaluating project applications, we shall also consider whether the application provides for:



(1) The capability of the Vessel(s) serving as a naval and military auxiliary in time of war or national emergency.

(2) The financing of the Vessel(s) within one year after delivery.

(3) The acquisition of Vessel(s) currently financed under Title XI by assumption of the total obligation(s).

(4) The Guarantees extend for less than the normal term for that class of vessel.

(5) In the case of an Eligible Shipyard, the capability of the shipyard to engage in naval vessel construction in time of war or national emergency.

(6) In the case of Shipyard Project, the Guarantees extend for less than the technological life of the asset.

(b) In determining the amount of equity which you must provide, we will consider, among other things, the following:

- (1) Your financial strength;
- (2) Adequacy of collateral; and
- (3) The term of the Guarantees.

#### **§ 298.18 Financing Shipyard Projects.**

(a) *Initial criteria.* We may issue Guarantees to finance a Shipyard Project at a General Shipyard Facility. We may approve such Guarantees after we consider whether the Guarantees will result in shipyard modernization and support increased productivity.

(b) *Detailed statement.* You must provide a detailed statement, with the Guarantee application, which will provide the basis for our consideration.

(c) *Required conditions.* We shall approve your application for loan guarantees under this section if we determine the following:

(1) The term for such Guarantees will not exceed the reasonable economic useful life of the collective assets which comprise this Shipyard Project;

(2) There is sufficient collateral to secure the Guarantee; and

(3) Your application will not prevent us from guaranteeing debt for a Shipyard Project that, in our sole opinion, will serve a more desirable use of appropriated funds. In making this determination, we will consider:

- (i) The types of vessels which will be built by the shipyard,
- (ii) The productivity increases which will be achieved,
- (iii) The geographic location of the shipyard,
- (iv) The long-term viability of the shipyard,
- (v) The soundness of the financial transaction,
- (vi) Any financial impact on other Title XI transactions, and
- (vii) The furtherance of the goals of the Shipbuilding Act.

#### **§ 298.19 Financing Eligible Export Vessels.**

(a) *Notification to Secretary of Defense.* (1) We will provide prompt notice of our receipt of an application for a loan Guarantee for an Eligible Export Vessel to the Secretary of Defense.

(2) During the 30-day period, beginning on the date on which the Secretary of Defense receives such notice, the Secretary of Defense may disapprove the loan guarantee if the Secretary of Defense makes an assessment that the Vessel's potential use may cause harm to United States national security interests.

(3) The Secretary of Defense may not disapprove a loan Guarantee under this section solely on the basis of the type of vessel to be constructed with the loan Guarantee. The authority of the Secretary of Defense to disapprove a loan Guarantee under this section may not be delegated to any official other than a civilian officer of the Department of Defense appointed by the President, by and with the advice and consent of the Senate. We will not approve a loan guarantee disapproved by the Secretary of Defense.

(b) *Vessel eligibility.* We may not approve a Guarantee for an Eligible Export Vessel unless:

(1) We find that the construction, reconstruction, or reconditioning of the Vessel will aid in the transition of United States shipyards to commercial activities or will preserve shipbuilding assets that would be essential in time of war or national emergency;

(2) The owner of the Vessel agrees with us that the Vessel shall not be transferred to any country designated by the Secretary of Defense as a country whose interests are hostile to the interests of the United States; and

(3) We determine that the countries in which the shipowner, its charterers, guarantors, or other financial interests supporting the transaction, if any, have their chief executive offices or have located a substantial portion of their assets, present an acceptable financial or legal risk to our collateral interests. Our determination will be based on confidential risk assessments provided by the Inter-Agency Country Risk Assessment System and will take into account any other factors related to the loan guarantee transaction that we deem pertinent.

#### **Subpart C—Guarantees**

#### **§ 298.20 Term, redemptions, and interest rate.**

(a) *In general.* The maturity date of the Obligations must be satisfactory to us

and must not exceed the anticipated physical and economic life of the Vessel or Vessels or Shipyard Project, and may be less than but no more than:

(1) Twenty-five years from the date of delivery from the shipbuilder of a single new Vessel which is to be security for Guarantees;

(2) Twenty-five years from the date of delivery from the shipyard of the last of multiple Vessels which are to be security for the Guarantees but that the amount of the Guarantees will relate to the amount of the depreciated actual cost of the multiple Vessels as of the Closing;

(3) The later of twenty-five years from the date of original delivery of a reconstructed, or reconditioned Vessel which is to be security for the Guarantees, or at the expiration of the remaining useful life of the Vessel, as we determine; or

(4) The technological life of the Shipyard Project.

(b) *Required redemptions.* Where multiple Vessels or multiple Shipyard Project assets are to be used as security for the Guarantees, as set forth in paragraph (a) of this section, we may require payments of principal prior to maturity (redemptions) regarding all related Obligations, as we may deem necessary to maintain adequate security for the Guarantees.

(c) *Interest rate.* We will make a determination as to the reasonableness of the interest rate of each Obligation, taking into account the range of interest rates prevailing in the private market for similar loans and the risks that we assume.

#### **§ 298.21 Limits.**

(a) *Actual Cost basis.* We will issue a guarantee on an amount of the Obligation satisfactory to us based on the economic soundness of the transaction. The Obligation amount may be less than but not more than 75 percent or 87½ percent, whichever is applicable, under the provisions of section 1104A(b)(2) or section 1104B(b)(2) of the Act of the Actual Cost of the Vessel or Vessels or Shipyard Project asset(s).

(1) If minimum horsepower of the main engine is a requirement for Guarantees up to 87½ percent of the Actual Cost, the standard for the horsepower will be continuous rated horsepower.

(2) Where we refinance existing debt, the amount of new Obligations we issue for the existing debt may not exceed the lesser of:

(i) The amount of outstanding debt being refinanced (whether or not receiving assistance under Title XI); or

(ii) Seventy-five or 87½ percent, whichever is applicable, of the Depreciated Actual Cost of the Vessel or Shipyard Project with respect to which the new Obligations are being issued.

(b) *Actual Cost items.* Actual Cost is comprised essentially of those items which would customarily be capitalized as Vessel or Shipyard Project construction costs such as designing, engineering, constructing (including performance bond premiums that we approve), inspecting, outfitting and equipping.

(1) Cost items include those items usually specified in Vessel or Shipyard Project construction contracts, e.g., changes and extras, cost of owner furnished equipment, shoreside spare parts and commitment fees and interest on the Obligations or other borrowings incurred during the construction period (excluding interest paid on subordinated debt considered to be Equity), and less income realized from investment of Escrow Fund deposits during the construction period.

(2) Commissions (which represent a portion of the total shipyard contract price) may be included in the foreign equipment and services amount of the Actual Cost of an export project, provided:

(i) A majority of the work done by the parties receiving the commissions is in the form of design and engineering work, and

(ii) The commissions represent a small amount of the total contract price.

(3) You may include Guarantee Fees determined in accordance with the provisions of section 1104(e) of the Act as an item of Actual Cost.

(4) In approving an item of Actual Cost, we will consider all pertinent factors.

(c) *Items excludible from Actual Cost.* Actual Cost shall not include any other costs such as the following:

(1) Legal fees or expenses;

(2) Accounting fees or expenses;

(3) Commitment fees or interest other than those specifically allowed;

(4) Fees, commissions or charges for granting or arranging for financing;

(5) Fees or charges for preparing, printing and filing an application for Title XI Guarantees and supporting documents, for services rendered to obtain approval of the application and for preparing, printing and processing documents relating to the application for Guarantees;

(6) Underwriting or trustee's fees;

(7) Foreign, federal, state or local taxes, user fees, or other governmental charges;

(8) Investigation fee determined in accordance with section 1104(f) of the Act and § 298.15;

(9) Predelivery Vessel operating expenses, Vessel insurance premiums and other items which may not be properly capitalized by the owner as costs of the Vessel under GAAP;

(10) The cost of the condition survey required by § 298.11(f) and all work necessary to meet the standards set forth in that paragraph;

(11) The cost to the Shipowner of a Vessel which is to be reconstructed, or reconditioned, e.g., cost of acquisition or repair work;

(12) Generally, any amount payable to the shipyard for early delivery of the Vessel;

(13) Generally, any amount payable to the manufacturer of the Shipyard Project for early delivery of the equipment to the General Shipyard Facility;

(14) Predelivery Shipyard Project expenses which may not be properly capitalized by the General Shipyard Facility as costs of the Shipyard Project under GAAP; and

(15) The cost of major foreign components and other foreign components for which there is no waiver and their assembly when comprising any part of the hull and superstructure of a Vessel.

(d) *Substantiation of Actual Cost.* (1) Before we make distribution from the Escrow Fund or Construction Fund (described in §§ 298.33 and 298.34), and prior to our final Actual Cost determination for each Vessel or Shipyard Project, you must submit to us documents substantiating all claimed costs eligible under paragraph (b) of this section or, alternatively, appropriate certification of such costs by an agent who has received our approval.

(2) These documents may include, but need not be limited to, copies of invoices, change orders, subcontracts, and where we require, statements from independent certified or independent licensed public accountants that the costs for which you seek payment or reimbursement were actually paid or are payable for the construction of a Vessel or Shipyard Project.

(3) You must summarize, index and arrange these documents according to cost categories by following the directions contained in our forms.

(e) *Escalation as part of Actual Cost.* Escalation clauses in construction contracts shall be subject to our approval. After a review of the base contract price and the escalation clauses, we shall, in order to estimate the Actual Cost amount to be stated in the Letter Commitment, add to the approved base contract price the amount of estimated escalation as approved by us. We must subsequently

approve the amount of escalation cost you claimed as a component of Actual Cost.

(f) *Monies received in respect of construction.* (1) If you or any Person acting on your behalf, from time to time receives moneys due for construction of a Vessel or Shipyard Project (described in the Security Agreement) from the shipbuilder, guarantors, sureties or other Persons, you shall give us written notice of such fact.

(2) As long as we have not paid the Guarantees, you or other recipient shall promptly deposit these moneys in a Depository with a written notice that the Depository shall hold such moneys on deposit until it receives written instructions from us as to their disposition.

(3) We will determine the extent to which Actual Cost is to be reduced by these moneys.

(4) In no event shall Actual Cost be reduced with respect to payments by the shipyard to a Vessel or Shipyard Project owner of liquidated damages for late delivery of the Vessel or Shipyard Project.

(5) If we have paid the Guarantees, you or other recipient must promptly pay these moneys, including any liquidated damages, to us for deposit into the Maritime Guaranteed Loans account.

(g) *Depreciated Actual Cost.* After a Vessel or Shipyard Project has been delivered or redelivered (in the case of reconstruction or reconditioning), the limitation on the amount of Guarantees will be 75 or 87½ percent, whichever is applicable, of the Depreciated Actual Cost of the Vessel or Shipyard Project.

#### **§ 298.22 Amortization of Obligations.**

(a) Generally, after delivery or completion of Shipyard Project, and until maturity of the Obligations, provisions of the Trust Indenture or other part of the Documentation require you to make periodic payment of principal and interest on the Obligations.

(b) Usually, the payment of principal (amortization) shall be made semi-annually, but in no event, less frequently than on an annual basis, and in either case the amortization shall be in equal payments of principal (level principal), unless we consent to the periodic payment of a constant aggregate amount, comprised of both interest and principal components which are variable in amount (level payment). No other proposed method of amortization will be allowed which would reduce the amount of periodic amortization below that determined under the level principal or level

payment basis at any time prior to maturity of the Obligations, except where:

(1) You can demonstrate to our satisfaction that there will be adequate funds to discharge the Obligations at maturity;

(2) You establish a fund acceptable to us in which you deposit an equal annual amount necessary to redeem the outstanding Obligations at maturity; or

(3) With regard to Eligible Export Vessels, in accordance with such other terms as we determine to be more favorable and to be compatible with export credit terms offered by foreign governments for the sale of vessels built in foreign shipyards.

#### **§ 298.23 Refinancing.**

(a) We may approve guarantees of Obligations to be secured by one or more Vessels or a Shipyard Project issued to refinance existing Title XI debt for either Vessels or for Shipyard Project and existing non-Title XI debt, so long as the existing debt has been previously issued for one of the purposes set forth in sections 1104(a)(1) through (4) of the Act. Section 1104 (a) (1) of the Act requires that, if the existing indebtedness was incurred more than one year after the delivery or redelivery of the related Vessel or Shipyard Project, the proceeds of such Obligations will be applied to the construction, reconstruction or reconditioning of other Vessels or Shipyard Project or as provided in § 298.24.

(b) We shall require any security lien on the Vessel(s) or Shipyard Project to be discharged immediately before we place a Mortgage or other security interest on any of the above assets. You must satisfy all necessary eligibility requirements as set forth in subpart B of this part, including economic soundness.

#### **§ 298.24 Financing a Vessel more than a year after delivery.**

(a) We may approve Guarantees for a Vessel which has been delivered (or redelivered in the case of reconstruction or reconditioning of a Vessel) more than one year prior to the issuance of the Guarantees only if:

(1) The issuance of the Guarantees would otherwise satisfy the requirements of the Act and the regulations in this part, and

(2) The proceeds of the Obligation financing such existing Vessel are used to finance:

(i) The construction, reconstruction, or reconditioning of a different Vessel within one year of that Vessel's delivery or redelivery, as the case may be, or

(ii) Facilities or equipment pertaining to marine operations. Such facilities or equipment must be of a specialized nature, used principally for servicing vessels and in handling waterborne cargo in the close proximity of the berthing area, excluding over-the-road equipment (other than chassis and containers), permanent or semipermanent structures and real estate, as well as new or less than one year old.

(b) At the Closing of Guarantees covered by this section, you must deposit the proceeds of the Obligation into an Escrow Fund established to pay for the cost unless you demonstrate to our satisfaction that all such costs have been paid.

#### **§ 298.25 Excess interest or other consideration.**

We shall not execute Guarantees if any agreement in the Documentation directly or indirectly provides for:

(a) The payment to an Obligor of interest, or other compensation for services which have not been performed, in a manner that such compensation or payment is being provided as interest in excess of the rate approved by us; or

(b) Grants of security to an Obligor in addition to the Guarantees.

#### **§ 298.26 Lease payments.**

You must obtain our approval of the amount and conditions of lease or charter hire payments if the payment of principal and interest on Obligations would be dependent, in any way, upon the lease or charter hire payments for a Vessel or Shipyard Project.

#### **§ 298.27 Advances.**

(a) *In general.* (1) In accordance with section 207 and Title XI of the Act, we have the discretion to make or commit to make an advance or payment of funds to, or on behalf of the owner, or operator or directly to any other person or entity for items, including, but not limited to:

- (i) Principal,
- (ii) Interest,
- (iii) Insurance, and
- (iv) Other vessel-related expenses or fees.

(2) We will make advances or payments only to protect, preserve or improve the collateral held as our security for Title XI debt.

(3) When requesting an advance, you must demonstrate that:

(i) Your problems are short term (less than two years) by using market and cash flow analysis and other projections.

(ii) An advance(s), would assist you over temporary difficulties; and

(iii) There is adequate collateral for the advance.

(b) *Filing requirements.* (1) You shall apply for an advance or other payment as early as is reasonably possible.

(2) *Principal and interest payments.* We must receive a request for an advance for principal and interest payments at least 30 days before the initial payment date.

(3) *Insurance payments.* We must receive a request for an advance of insurance payments at least 30 days before a renewal or termination date.

(4) *Extenuating circumstances.* We may consider requests for assistance with less notice, upon written documentation of extenuating circumstances.

(5) *Supporting data.* Any requests for assistance must be accompanied by supporting data regarding:

- (i) Need for the advance,
- (ii) Financial assistance you sought from other sources,
- (iii) The measures that you are taking and have taken to alleviate the situation,
- (iv) Financial projections,
- (v) Proposed term of the repayment,
- (vi) Current and projected market conditions,
- (vii) Information on other available collateral,
- (viii) Liens and other creditor information, and
- (ix) Any other information which we may request.

### **Subpart D—Documentation**

#### **§ 298.30 Nature and content of Obligations.**

(a) *Single page.* An Obligation, in the form of a note, bond of any type, or other debt instrument, when engraved, printed or lithographed on a single sheet of paper must include on its face the:

- (1) Name of the Obligor,
- (2) Principal sum,
- (3) Rate of interest,
- (4) Date of maturity, and
- (5) Guarantee of the United States, authenticated by the Indenture Trustee, if any.

(b) *Several pages.* If the Obligation is typewritten, printed or reproduced by other means on several pages of paper, the Guarantee of the United States and the authentication certificate of the Indenture Trustee, if any, may appear at the end of the typewritten Obligation.

(c) *Rights and responsibilities.* The instrument which is evidence of indebtedness shall also contain all information necessary to apprise the Obligees of their rights and responsibilities including, but not limited to:

- (1) Time and manner for payment of principal and interest,

(2) Redemptions,  
 (3) Default procedure, and  
 (4) Notification (in case of registered Obligations) of sale or other transfer of the instruments.

#### **§ 298.31 Mortgage.**

(a) *In general.* Under normal circumstances, a Guarantee shall not be endorsed on any Obligation until we receive satisfactory evidence that we hold a Mortgage in one or more Vessels or a Mortgage or other security interest in the Shipyard Project. During construction of a new Vessel or any Shipyard Project, a security interest may be perfected by a filing under the Uniform Commercial Code.

(b) *Ensuring validity of security interest.* In order to ensure that our Mortgages or other security interests are valid and enforceable, we shall require that the Obligor obtain legal opinions, in form and substance satisfactory to us, from independent, outside legal counsel satisfactory to us, including foreign independent outside legal Counsel for Eligible Export Vessels, which opinions shall state, among other things, that the Mortgage or other security interest(s) are valid and enforceable:

(1) In the country in which the Vessel is documented (or, in the case of a security interest, in jurisdictions acceptable to us);

(2) In the United States; and

(3) For vessels operating on specified trade routes, in the country or countries involved in this service, unless we determine that those destinations are too numerous, in which case, we will instead require an opinion of foreign validity and enforceability in the Vessel's primary port of operation.

(c) *Alternative forms of security.* In the case where a Mortgage or security interest on the financed assets may not be available or enforceable, we will require alternative forms of security.

(d) *Mortgage in our favor.* The Security Agreement shall provide that upon delivery of a new Vessel or upon final completion of the Shipyard Project, or at the time Guarantees are issued with respect to an existing Vessel or the Shipyard Project, a Mortgage on the Vessel and a Mortgage or other security interest on the Shipyard Project will be executed in our favor, unless we determine that a Mortgage or a security interest is not available or enforceable in accordance with paragraph (c) of this section.

(e) *Filing.* You must file the Mortgage with the United States Coast Guard's National Vessel Documentation Center. You must file the Mortgage for an Eligible Export Vessel with the proper foreign authorities. For assets of a

General Shipyard Facility, you must file a Mortgage and security interest with the proper authorities within the appropriate state for recording. After you have recorded the Mortgage, you must deliver to us the Mortgage and evidence of the filing of the security interest.

(f) *Mortgage secured by multiple Vessels.* (1) When two or more Vessels are to be security for Guarantees, the Security Agreement may provide that one Mortgage relating to all the Vessels (Fleet Mortgage) shall be executed, perfected and delivered to us by the Obligor.

(2) If the Fleet Mortgage relates to undelivered Vessels, the Fleet Mortgage will be executed upon delivery of the first vessel. At the time of each subsequent Vessel delivery, the Obligor shall execute a supplement to the Fleet Mortgage which makes that Vessel subject to our Mortgage lien.

(3) The Fleet Mortgage shall provide that payment by the Obligor of the entire amount of Obligations covered or to be covered by Guarantees shall be required to discharge the Fleet Mortgage, regardless of the amount of the Secretary's Note or Notes issued and outstanding at the time of execution and delivery of the Fleet Mortgage or the number of Vessels covered by the Fleet Mortgage.

(4) The discharge date of the Fleet Mortgage shall be the maturity date of the Secretary's Note. We may require, as authorized by section 1104(c)(2) of the Act, such payments of principal prior to maturity (redemptions), regarding all related Obligations, as deemed necessary to maintain adequate security for the Guarantees.

(5) Each Fleet Mortgage shall provide that in the event of constructive total loss, requisition of title or sale of any Vessel covered by the Fleet Mortgage, indebtedness represented by the Obligations shall be paid, unless we otherwise determine that there remains adequate security for the Guarantees, and the Vessel shall be discharged from the Mortgage lien.

(g) *Adequacy of collateral.* (1) Under normal circumstances, a First Preferred Mortgage on the Vessel(s) or Shipyard Project will be adequate security for the Guarantees.

(2) If, however, we determine that the Mortgage on the Vessel(s) or Shipyard Project is not sufficient to provide adequate security, as a condition to approving the Letter Commitment or processing the application, we may require additional collateral, such as a mortgage(s) on other vessel(s) or Shipyard Project or on other assets, special escrow funds, pledges of stock,

charters, contracts, notes, letters of credit, accounts receivable assignments, and guarantees.

#### **§ 298.32 Required provisions in documentation.**

(a) Performance under shipyard and related contracts. Generally, shipyard and related contracts must contain provisions for:

(1) Furnishing by the shipyard or contractor of the Shipyard Project of satisfactory insurance and a satisfactory performance bond where Obligations are issued during the construction period, except that if the shipyard or contractor of the Shipyard Project demonstrates to our satisfaction that it has sufficient financial resources and operational capacity to complete the project, posting of a bond will not be required;

(2) Allowing access to the Vessel or Shipyard Project, as well as all related work projects being performed by the contractor and subcontractors, to our representative, at all reasonable times, to inspect performance of the work and to observe trials and other tests for the purpose of determining that the Vessel or Shipyard Project is being constructed, reconstructed, or reconditioned in accordance with contract plans and specifications approved by us;

(3) Submitting to us, upon request, one set of shipyard plans, in form and substance satisfactory to us, for the Vessel or Shipyard Project as built;

(4) Making periodic payments for the work in accordance with an agreed schedule, submitted by the shipyard or contractor, as appropriate, in a form acceptable to us, based on percentage of completion, after such percentage and satisfactory performance are certified by the Obligor, shipyard or contractor, as appropriate, and our representative as to each payment;

(5) Prohibiting the use of proceeds from the sale of Obligations for the payment of work performed outside the shipyard, unless we consent in writing to such use; and

(6) Requiring that all components of the hull and superstructure of a U.S.-documented Vessel and an Eligible Export Vessel shall be assembled in the United States.

(7) If Obligation will not be issued during the construction period of the Vessel and Shipyard Project, requiring that shipyard-related contracts shall generally include the provisions specified in paragraphs (a)(2), (a)(3) and (a)(6) of this section.

(b) *Assignments and general covenants from Obligor to us.* The Obligor shall assign rights and shall covenant with us, as we require,

including, but not limited to, the following:

(1) Assignment of all or part of the right, title and interest under the construction contract and related contracts, except those rights expressly reserved therein by the Obligor relating to such things as patent infringement and liquidated damages;

(2) Assignment of rights to receive all moneys which from time to time become due regarding Vessel or Shipyard Project construction;

(3) Assignment, where applicable, of all or a part of the bareboat charter, time charter, contracts of affreightment or other agreements relating to the use of the Vessel or Shipyard Project and all hire payable to the Obligor, and delivery to us of required consents by appropriate parties to any such assignments;

(4) Covenants relating to the filing of satisfactory evidence of continuing United States citizenship, in accordance with 46 CFR part 355, with the exception of Eligible Export Vessels and shipyards with Shipyard Projects; warranty of Vessel or Shipyard Project title free from all liens other than those specifically excepted; maintaining United States documentation of the Vessel or documentation under the laws of a country other than the United States with regard to an Eligible Export Vessel; compliance with the provisions of 46 U.S.C. 31301–31343, except that Eligible Export Vessels shall comply with the definition of a “preferred mortgage” in 46 U.S.C. 31301(6)(B), requiring, among other things, that the Mortgage shall comply with the mortgage laws of the foreign country where the Vessel is documented and shall have been registered under those laws in a public register; Notice of Mortgage, payment of all taxes (except if being contested in good faith); annual financial statements audited by independent certified or independent licensed public accountant.

(5) Covenants to keep records of construction costs paid by or for the Obligor’s account and to furnish us with a detailed statement of those costs, distinguishing between:

(i) Items paid or obligated to be paid, attested to by independent certified public accountants unless otherwise verified by us; and

(ii) Costs of American and foreign materials (including services) in the hull and superstructure.

(6) Covenants to maintain Marine and War Risk Hull and Machinery insurance on the Vessel or Eligible Export Vessel in an amount equal to 110% of the outstanding Obligations or up to the full commercial value of the Vessel or

Eligible Export Vessel, whichever is greater; Marine and War Risk Protection and Indemnity insurance; Interim War Risk Binders for Hull and Machinery, and Protection and Indemnity coverages underwritten by us as authorized by Title XII of the Act; and such additional insurance as may be required by us. All insurance required to be maintained shall be placed with the United States Government and American and/or British (and/or other foreign, if permitted by us by prior written notice) insurance companies, underwriters’ associations or underwriting funds approved by us through marine insurance brokers and/or underwriting agents approved by us. All insurance required to be maintained shall be placed under the latest (at the time of issue) forms of American Institute of Marine Underwriters policies approved by us and/or under such other forms of policies which we may approve in writing and/or policies issued by or for us insuring the Vessel or Eligible Export Vessel against the usual risks provided for under such forms, including such amounts of increase value or other forms of “that total loss only” insurance permitted by the Hull and Machinery insurance policies;

(7) Collateralize other debt due to us under other Title XI financings;

(8) Covenants to maintain shipyard insurance on the Shipyard Project in an amount equal to 110% of the outstanding Obligations or up to the full commercial value of the Shipyard Project, whichever is greater, and such additional insurance as may be required by us; and

(9) Covenants to maintain additional types of insurance as may be required by us with respect to Eligible Export Vessels, *i.e.* political risk insurance, to cover such items as the political, financial, and/or economic risk in a foreign country.

#### **§ 298.33 Escrow fund.**

(a) *Escrow Fund Deposits.* At the time of the sale of the Obligations, the Obligor shall deposit with us in an escrow fund (the “Escrow Fund”) all of the proceeds of that sale unless the Obligor is entitled to withdraw funds under paragraph (b) of this section. The Obligor must also deposit into the Escrow Fund on the Closing date an amount equal to six months interest at the rate borne by the Obligations, unless we find the existence of adequate consideration or accept other consideration in lieu of the interest deposit.

(b) *Escrow Fund Withdrawals.* You, as Obligor, may make a written request for us to disburse funds from the Escrow

Fund. Within a reasonable time thereafter, we shall disburse directly to the Indenture Trustee, any Paying Agent for such Obligations, or any other Person entitled to payment any amount which you are obligated to pay or have paid, on account of the items and amounts or any other item approved by us, provided that we are satisfied with the accuracy and completeness of the information contained in the following submissions:

(1) A responsible officer of the Obligor shall deliver an officer’s certificate, in form and substance satisfactory to us, stating that:

(i) There is no default under the construction contract or the Security Agreement;

(ii) There have been no occurrences which have or would adversely and materially affect the condition of the Vessel, its hull or any of its component parts, or the Shipyard Project;

(iii) The amounts of the request are in accordance with the construction contract including the approved disbursement schedule and each item in these amounts is properly included in our approved estimate of Actual Cost;

(iv) With respect to the request, once the contractor is paid there will be no liens or encumbrances on the applicable Vessel, its hull or component parts, or the Shipyard Project for which the withdrawal is being requested except for those already approved by us; and

(v) If the Vessel or Shipyard Project has already been delivered or completed, it is in class, if required, and is being maintained in the highest and best condition. The Obligor must also attach an officer’s certificate of the shipyard and other general contractors, in form and substance satisfactory to us, stating that there are no liens or encumbrances as provided in paragraph (b)(1)(iv) of this section and attaching the invoices and receipts supporting each proposed withdrawal to our satisfaction.

(2) No payment or reimbursement under this section shall be made:

(i) To any Person until the Construction Fund, if any, has been exhausted,

(ii) To any Person until the total amount paid by or for the account of the Obligor from sources other than the proceeds of such Obligations equals at least 12½ percent or 25 percent as applicable, of the Actual Cost of the Vessel or Shipyard Project is made;

(iii) To the Obligor which would have the effect of reducing the total amounts paid by the Obligor pursuant to paragraph (b)(2)(ii) of this section; or

(iv) To any Person on account of items, amounts or increases

representing changes and extras or owner furnished equipment, if any, unless such items, amounts and increases shall have been previously approved by us; provided, however, that when the amount guaranteed by us equals 75 percent or less of the Actual Cost and the Obligor demonstrates to our satisfaction the ability to pay in the remaining 25 percent, or more, then after the initial 12½ percent of Actual Cost has been paid by or on behalf of the Obligor for such Vessel or completed Shipyard Project and up to 37½ percent of Actual Cost has been withdrawn from the Escrow Fund for such Vessel or Shipyard Project, the Obligor must pay the remaining Obligor's equity of at least 12½ percent (as determined by us) before additional monies can be withdrawn from the Escrow Fund relating to such Vessel or Shipyard Project.

(3) We will not be required to make any disbursement except out of the cash available in the Escrow Fund. If any sale or payment on maturity results in a loss in the principal amount of the Escrow Fund invested in securities so sold or matured, the requested disbursement from the Escrow Fund shall be reduced by an amount equal to such loss, and the Obligor must pay to any Person entitled thereto, the balance of the requested disbursement from the Obligor's funds other than the proceeds of such Obligations.

(4) If we assume the Obligor's rights and duties under the Obligations or we pay the Guarantees, all amounts in the Escrow Fund (including realized income which has not yet been paid to the Obligor), shall be paid to us and be credited against any amounts due or to become due to us under the Security Agreement and the Secretary's Note.

(5) Other rights and duties with respect to withdrawals from the Escrow Fund shall be set out in the closing documentation in form and substance satisfactory to us.

(c) *Investment and liquidation of the Escrow Fund.* We may invest the Escrow Fund in obligations of the United States. We will deposit amounts in the Escrow Fund into an account with the U.S. Treasury Department and upon agreement with the Obligor, shall deliver to the U.S. Treasury Department instructions for the investment, reinvestment and liquidation of the Escrow Fund. We will have no liability to the Obligor for acting in accordance with such instructions.

(d) *Income on the Escrow Fund.* Unless there is an existing default, any income realized on the Escrow Fund shall be paid to the Obligor upon our receipt of such income.

(e) *Termination date of the Escrow Fund.* The Escrow Fund shall terminate 90 days after the delivery date of the last Vessel or Shipyard Project covered by the Security Agreement (the "Termination Date"). In the event that on such date the payment of the full amount of the aggregate Actual Cost of all of the Vessels or Shipyard Project has not been made or the amounts with respect to such Actual Cost are not then due and payable, then we and the Obligor by written agreement shall extend the Termination Date for such period as we and the Obligor shall determine is sufficient to allow for such contingencies. Any amounts remaining in the Escrow Fund on the Termination Date which are in excess of 87½ percent or 75 percent of Actual Cost, as the case may be, shall be applied to retire a pro rata portion of the Obligations.

#### **§ 298.34 Construction fund.**

(a) *Circumstances requiring deposits.* (1) When the Security Agreement provides for the establishment of an Escrow Fund, the Obligor shall also make Construction Fund deposits when the Obligor:

(i) Submits a claim to the agency that it has previously paid for items of Actual Cost and

(ii) Is seeking reimbursement at the Closing.

(2) The Obligor shall make the Construction Fund deposits as follows:

(i) At the time of the sale of the Obligations, the Obligor shall deposit with the Depository cash equal to the principal amount of the Obligations issued at such time less the sum of the aggregate principal amount then required to be in the Escrow Fund, and

(ii) The amount in excess of 12½ or 25 percent of Actual Cost or Depreciated Actual Cost, as applicable (whichever is payable under § 298.33(b) which we determine has been paid by or for the account of the Obligor.

(b) *Security interest and control.* We must have a security interest in and control over the Construction Fund and its proceeds.

(c) *Balance of the proceeds.* The Obligor will retain the balance of the proceeds, if any, from the sale of the Obligations, after depositing the amounts required to be deposited in the Escrow Fund and/or the Construction Fund.

(d) *Withdrawals and redeposits.* We shall, subject to the satisfaction of any applicable conditions contained in the Security Agreement, periodically approve disbursements from the Construction Fund under the same procedures and conditions as from the Escrow Fund in § 298.33(b), except the

request for withdrawal will not be subject to § 298.33(b)(2)(i) and (e). The administration of the Construction Fund shall also be subject to the terms and conditions of § 298.33.

#### **§ 298.35 Title XI Reserve Fund and Financial Agreement.**

(a) *Purpose.* In order to provide us with further security and to ensure payment of the interest and principal due on the Obligations, we will require the Company to enter into a Title XI Reserve Fund and Financial Agreement (Agreement) at the first Closing at which the Company issues Obligations. We may waive or modify provisions of the Agreement based on our evaluation of the aggregate security for the Guarantees.

(b) *Financial covenants.* There will be two sets of covenants. One set of covenants will be imposed regardless of the Company's financial condition (primary covenants). The other set of covenants will be imposed only if the Company does not meet specific financial conditions (supplemental covenants). The primary and supplemental covenants are to be set forth in the Agreement. Covenants shall be imposed on the Company as follows:

(1) *Primary covenants.* So long as Guarantees are in effect the Company shall not, without our prior written consent:

(i) Make any distribution of earnings, except as may be permitted as follows:

(A) From retained earnings in an amount specified in paragraph (b)(1)(i)(C) of this section, provided that, in the fiscal year in which the distribution of earnings is made there is no operating loss to the date of such payment of such distribution of earnings, and there was no operating loss in the immediately preceding three fiscal years, or there was a one-year operating loss during the immediately preceding three fiscal years, but such loss was not in the immediately preceding fiscal year, and there was positive net income for the three year period;

(B) If distributions of earnings may not be made under paragraph (b)(1)(i)(A) of this section, a distribution can be made in an amount equal to the total operating net income for the immediately preceding three fiscal year period, provided that:

(1) There were no two successive years of operating losses;

(2) There is no operating loss to the date of such distribution in the fiscal year in which such distribution is made; and

(3) The distribution of earnings made would not exceed an amount specified in paragraph (b)(1)(i)(C) of this section;

(C) Distributions of earnings may be made from earnings of prior years in an aggregate amount equal to 40 percent of the Company's total net income after tax for each of the prior years, less any distributions that were made in such years; or the aggregate of the Company's total net income after tax for such prior years, provided that, after making such distribution, the Company's Long-Term Debt does not exceed its Net Worth. In computing net income for purposes of this paragraph (b)(1)(i)(C), extraordinary gains, such as gains from the sale of assets, will be excluded;

(ii) Enter into any service, management or operating agreement for the operation of the Vessel or the Shipyard Project (excluding husbanding type agreements), or appoint or designate a managing or operating agent for the operation of the Vessel or the Shipyard Project (excluding husbanding agents) unless approved by us;

(iii) Sell, mortgage, transfer, or demise charter the Vessel or the Shipyard Project or any assets to any non-Related Party except as permitted in paragraph (b)(1)(vii) of this section or sell, mortgage, transfer, or demise charter the Vessel or any assets to a Related Party, unless such transaction is at a fair market value as determined by an independent appraiser acceptable to us, and is a total cash transaction;

(iv) Enter into any agreement for both sale and leaseback of the same assets so sold unless the proceeds from such sale are at least equal to the fair market value of the property sold;

(v) Guarantee, or otherwise become liable for the obligations of any other Person, except with respect to any undertakings as to the fees and expenses of the Indenture Trustee, except endorsement for deposit of checks and other negotiable instruments acquired in the ordinary course of business and except as otherwise permitted in this section;

(vi) Directly or indirectly embark on any new enterprise or business activity not directly connected with the business of shipping or other activity in which the Company is actively engaged;

(vii) Enter into any merger or consolidation or convey, sell, demise charter, or otherwise transfer, or dispose of any portion of its properties or assets (any and all of which acts are encompassed within the words "sale" or "sold" as used in this section), provided that, the Company will not be deemed to have sold such properties or assets if the net book value of the aggregate of all the assets sold by the

Company during any period of 12 consecutive calendar months does not exceed ten percent of the total net book value of all of the Company's assets; the Company retains the proceeds of the sale of assets for use in accordance with the Company's regular business activities; and the sale is not otherwise prohibited by paragraph (b)(1)(iii) of this section. The Company may not consummate such sale without our prior written consent if the Company has not, prior to the time of such sale, submitted to us, as required, its most recently audited financial statements referred to in § 298.42(a) and any attempt to consummate a sale absent such approval will be null and void *ab initio*.

(2) *Supplemental Covenants which may become applicable.* Unless, after giving effect to such transaction or transactions, during any fiscal year of the Company, the Company's Working Capital is equal to at least one dollar, the Company's Long-Term Debt does not exceed two times the Company's Net Worth and the Company's Net Worth is at least the amount specified by us, the Company shall not, without our prior written consent:

(i) Withdraw any capital;

(ii) Redeem any share capital or convert any of the same into debt;

(iii) Pay any dividend (except dividends payable in capital stock of the Company);

(iv) Make any loan or advance (except advances to cover current expenses of the Company), either directly or indirectly, to any stockholder, director, officer, or employee of the Company, or to any other Related Party;

(v) Make any investments in the securities of any Related Party;

(vi) Prepay in whole or in part any indebtedness to any stockholder, director, officer, or employee of the Company, or to any Related Party, which has a stated maturity of more than one year from such date;

(vii) Increase any direct employee compensation (as defined in this paragraph) paid to any employee in excess of \$100,000 per annum; nor increase any direct employee compensation which is already in excess of \$100,000 per annum; nor initially employ or re-employ any person at a direct employee compensation rate in excess of \$100,000 per annum; provided, however, that beginning with January 1, 2000 the \$100,000 limit may be increased annually based on the previous years' closing Consumer Price Index for All Urban Consumers published by the Bureau of Labor Statistics. For the purpose of this paragraph, the term "direct employee compensation" is the

total amount of any wage, salary, bonus commission, or other form of direct payment to any employee from all companies with guarantees under the Act as reported to the Internal Revenue Service for any fiscal year.

(viii) Acquire any fixed assets other than those required for the maintenance of the Company's existing assets, including normal maintenance and operation of any vessel or vessels owned or chartered by the Company;

(ix) Either enter into or become liable (directly or indirectly) under charters and leases (having a term of six months or more) for the payment of charter hire and rent on all such charters and leases which have annual payments aggregating in excess of an amount specified by us;

(x) Pay any indebtedness subordinated to the Obligations or to any other Title XI obligations;

(xi) Create, assume, incur, or in any manner become liable for any indebtedness, except current liabilities, or short term loans, incurred or assumed in the ordinary course of business as such business presently exists;

(xii) Make any investment whether by acquisition of stock or indebtedness, or by loan, advance, transfer of property, capital contribution, guarantee of indebtedness or otherwise, in any Person, other than obligations of the United States, bank deposits or investments in securities of the character permitted for monies in the Title XI Reserve Fund; and,

(xiii) Create, assume, permit or suffer to exist or continue any mortgage, lien, charge or encumbrance upon, or pledge of, or subject to the prior payment of any indebtedness, any of its property or assets, real or personal, tangible or intangible, whether now owned or thereafter acquired, or own or acquire, or agree to acquire, title to any property of any kind subject to or upon a chattel mortgage or conditional sales agreement or other title retention agreement, except loans, mortgages and indebtedness guaranteed by us under Title XI of the Act or related to the construction of a vessel approved for Title XI by us, and liens incurred in the ordinary course of business as such business presently exists.

(c) *Title XI Reserve Fund Net Income.* The Agreement shall provide that within 105 days after the end of its accounting year, the Company will compute its net income attributable to the operation of the Vessel(s) that were constructed, reconstructed, reconditioned or refinanced with Title XI financing assistance (Title XI Reserve Fund Net Income). The computation utilizes a ratio expressed as a



percentage, and applies this percentage to the Company's total net income after taxes. The numerator of the ratio is be the total original capitalized cost of all Company Vessels (whether leased or owned) which were constructed, reconstructed, reconditioned or refinanced with the assistance of Guarantees. The denominator shall be the total original capitalized cost of all the Company's fixed assets. In the case of Shipyard Project, the Agreement shall provide that within 105 days after the end of its accounting year, the Company shall submit its audited financial statements showing its net cash flow in a manner acceptable to us, in lieu of any other computation of Reserve Fund Net Income specified in this section for Vessels. The net income after taxes, computed in accordance with GAAP, will be adjusted as follows:

(1) The depreciation expense applicable to the accounting year shall be added back.

(2) There shall be subtracted:

(i) An amount equal to the principal amount of debt required to be paid or redeemed, and actually paid or redeemed by the Company (other than from the Title XI Reserve Fund) during the year; and

(ii) The principal amount of Obligations retired or paid (as defined in the Security Agreement), prepaid or redeemed, in excess of the required redemptions or payments which may be used by the Company as a credit against future required redemptions or other required payments with respect to the Obligations.

(d) *Deposits.* Unless the Company, as of the close of its accounting year, was subject to and in compliance with the financial requirements set forth in paragraph (b)(2) of this section, the Company shall make one or more deposits to a special joint depository account with us (the Title XI Reserve Fund) to be established pursuant to an agreement in writing (Depository Agreement) at the time the first deposit is required to be made. The amount of deposit as to any year, or period less than a full year, where applicable, will be determined as follows:

(1) Fifty percent of the Title XI Reserve Fund Net Income, less an amount equal to 10% of the Company's total original equity investment in the Vessel or Vessels, (if the Company is the owner of the assets), will be deposited into the Title XI Reserve Fund.

(2) In the case of Shipyard Project, the shipyard shall make a deposit at two percent of its net cash flow, as defined by GAAP, and as shown on its audited financial statements.

(3) Any additional amounts that may be required pursuant to the Security Agreement or any other agreement in the documentation to which the Company is a party.

(4) Any additional amounts that may be required, pursuant to provisions of the Security Agreement or any other agreement in the documentation to which the Company is a party.

(5) Irrespective of the Company's deposit requirement, as stated in paragraphs (d) (1) through (4) of this section, the Company will not be required to make any deposits into the Title XI Reserve Fund if any of the following events will have occurred:

(i) The Company will have discharged the Obligations and related Secretary's Note and will have paid other sums secured under the Security Agreement and Preferred Mortgage;

(ii) All Guarantees with respect to outstanding Obligations will have terminated pursuant to the provisions of the Security Agreements, other than by reason of payment of the Guarantees; or

(iii) The amount in the Title XI Reserve Fund, (including any securities at market value), is equal to, or in excess of 50 percent of the principal amount of outstanding Obligations.

(e) *Fund in lieu of Title XI Reserve Fund.* If the Company has established a Capital Construction Fund (CCF), pursuant to section 607 of the Act, whether interim or permanent, at any time when a deposit would otherwise be required to be made into the Title XI Reserve Fund, and the Company elects to make such deposits to the CCF, the Company must enter into an agreement, satisfactory to us, providing that all such deposits of assets therein will be security (CCF Security Amount) to the United States in lieu of the Title XI Reserve Fund. The deposit requirements of the Title XI Reserve Fund and Financial Agreement will be deemed satisfied by deposits of equal amounts in the CCF, and withdrawal of the CCF Security Amount will be subject to our prior written consent. If, for any reason, the CCF terminates prior to the payment of the Obligations, the Secretary's Note and all other amounts due under or secured by the Security Agreement or Mortgage, the CCF Security Amount will be deposited or redeposited in the Title XI Reserve Fund.

#### § 298.36 Guarantee Fee.

(a) *Rates in general.* (1) For annual periods, beginning with the date of the Security Agreement and prior to the delivery date of a Vessel or Shipyard Project, we shall charge a Guarantee Fee set at a rate of not less than ¼ of 1 percent and not more than ½ of 1

percent of the excess of the average principal amount of the Obligations estimated to be outstanding during the annual periods covered by said Guarantee Fee over the average principal amount, if any, on deposit in the Escrow Fund during said annual period (Average Principal Amount of Obligations Outstanding).

(2) For annual periods beginning with the delivery date of a Vessel or Shipyard Project, the Guarantee Fee shall be set at an annual rate of not less than ½ of 1 percent and not more than 1 percent of the Average Principal Amount of Obligations Outstanding during the annual periods covered by the Guarantee Fee. You will be responsible for payment of the Guarantee Fee.

(b) *Rate calculation.* (1) The Guarantee Fee rate generally shall vary inversely with the ratio of Equity to Long-Term Debt (Variable Rate) of the Person who we consider to be the primary source of credit in the transaction (Credit Source), for example,

(i) The long term time charterer (where the charter hire represents the source of payment of interest and principal with respect to the Obligations),

(ii) The guarantor of the Obligations,

(iii) The Obligor, or

(iv) The bareboat charterer.

(2) Where the Variable Rate is used, we may make such adjustments to the computation of Equity and Long-Term Debt considered necessary to reflect more accurately the financial condition of the Credit Source.

(3) We shall base our determination of Equity and Long-Term Debt on information contained in forms or statements on file with us prior to the date on which the Guarantee Fee is to be paid.

(4) With our consent, you may include in Equity and exclude from Long-Term Debt, any subordinated indebtedness representing loans from any credit source.

(5) We may establish a fixed rate or other method of calculation of the Guarantee Fee, upon an evaluation of the aggregate security for the Guarantees.

(c) *Variable Rate prior to Vessel or Shipyard Project.* For annual periods beginning prior to the delivery date of a Vessel or Shipyard Project being constructed, reconstructed, or reconditioned, the Guarantee Fee shall be determined as follows:

(1) If the Equity is less than 15 percent of the Long-Term Debt, the Guarantee Fee rate shall be ½ of 1 percent of the Average Principal Amount of Obligations Outstanding during the

annual period covered by the Guarantee Fee.

(2) If the Equity is at least 15 percent of the Long-Term Debt, but less than the Long-Term Debt, the Guarantee Fee rate shall be  $\frac{3}{8}$  of 1 percent of the Average Principal Amount of Obligations Outstanding during the annual period covered by the Guarantee Fee.

(3) If the Equity is equal to or exceeds the Long-Term Debt, the Guarantee Fee rate shall be  $\frac{1}{4}$  of 1 percent of the Average Principal Amount of Obligations Outstanding during the annual period covered by the Guarantee Fee.

(d) *Variable Rate after Vessel or Shipyard Project delivery or completion.* For annual periods beginning on or after the Vessel or Shipyard Project delivery date, the Guarantee Fee shall be determined as follows:

(1) If the Equity is less than 15 percent of the Long-Term Debt, the Guarantee Fee rate shall be 1 percent of the Average Principal Amount of Obligations Outstanding during the annual period covered by the Guarantee Fee.

(2) If the Equity is at least 15 percent of the Long-Term Debt but less than 60 percent of the Long-Term Debt, the Guarantee Fee rate shall be  $\frac{3}{4}$  of 1 percent of the Average Principal Amount of Obligations Outstanding during the annual period covered by the Guarantee Fee.

(3) If the Equity is at least 60 percent of the Long-Term Debt, but less than the Long-Term Debt, the Guarantee Fee rate shall be  $\frac{5}{8}$  of 1 percent of the Average Principal Amount of Obligations Outstanding during the annual period covered by the Guarantee Fee.

(4) If the Equity is equal to or exceeds the Long-Term Debt, the Guarantee Fee rate shall be  $\frac{1}{2}$  of 1 percent of the Average Principal Amount of Obligations Outstanding during the annual period covered by the Guarantee Fee.

(e) *Payment of Guarantee Fee.* (1) The Guarantee Fee covering the full period of the stated maturity of the Obligations commencing with the date of the Security Agreement shall be paid to us concurrently with the execution and delivery of said Agreement. The project's entire Guarantee Fee payment shall be made by you to us in an amount equal to the sum of the present value of the separate products obtained by applying the pertinent pre or post delivery Guarantee Fee rate or rates to the projected amount of the Average Principal Amount of Obligations Outstanding for each year of the stated maturity of the Obligations. In calculating the present value used in

determining the amount of the Guarantee Fee to be paid, we shall use a discount rate based on information contained in the President's most recently submitted budget.

(2) The Guarantee Fee may be included in Actual Cost, is eligible to be financed, and is non-refundable.

(f) *Proration of Guarantee Fee.* The Guarantee Fee shall be prorated where a Vessel delivery is scheduled to occur during the annual period with respect to which payment of said Guarantee Fee is being made, as follows:

(1) Undelivered Vessel. If the Guarantee Fee relates to an undelivered Vessel, the predelivery rate is applicable to the Average Principal Amount of Obligations Outstanding for the period from the date of the Security Agreement to the delivery date, and the delivered Vessel rate is applicable for the balance of the annual period in which the delivery occurs.

(2) Multiple Vessels. If the Guarantee Fee relates to more than one Vessel, the amount of outstanding Obligations will be allocated to each Vessel in the manner prescribed in § 298.33(d), and an amount shall be determined for each Vessel by using the rate that is applicable under paragraph (c) or (d) of this section. The Guarantee Fee shall be the aggregate of the amounts calculated for each Vessel.

#### § 298.37 Examination and audit.

(a)(1) We shall have the right to examine and audit the books, records (including original logs, cargo manifests and similar records) and books of account, which pertain directly to the project, of the Obligor, bareboat charterer, time charterer or any other Person who has an agreement with respect to control of, or a financial interest in, a Vessel or Shipyard Project, as well as records of a Related Party and domestic agents connected with such Persons, and shall have full, free and complete access to these items at all reasonable times.

(2) We shall have the right to full, free and complete access, at all reasonable times, to each Vessel or Shipyard Project for which Guarantees are in force.

(3) When a Vessel is in port or undergoing repairs, we may make photostatic or other copies of any books, records and other relevant documents or papers being examined or audited.

(b) The Person in control of the premises where we conduct the examination or audit must furnish, without charge, adequate office space and other facilities that we reasonably require in performing the examination, audit or inspection.

#### § 298.38 Partnership agreements and limited liability company agreements.

Partnership and limited liability company agreements must be in form and substance satisfactory to us prior to any Guarantee Closing, especially relating, but not limited to:

- (a) Duration of the entity;
- (b) Adequate partnership or limited liability company funding requirements and mechanisms;
- (c) Dissolution of the entity and withdrawal of a general partner or member;
- (d) The termination, amendment, or other modification of the entity without our prior written consent; and
- (e) Distribution of funds or ownership interest.

#### § 298.39 Exemptions.

We may exempt an applicant from any requirement of this part, unless required by statute or other regulations, in exceptional cases, on written findings that:

- (a) The case materially involves factors not considered in the promulgation of this part;
- (b)(1) A national emergency makes it necessary to approve the exemption, or
- (2) The exemption will substantially relieve the financial liability of the United States;
- (c) The exemption will not substantially impact effective regulation of the Title XI program, consistent with the objectives of this part;
- (d) The exemption will not be unjustly discriminatory; and
- (e) For Eligible Export Vessels, such exemption would assist in creating financing terms that would be compatible with export credit terms for the sale of vessels built in shipyards other than those in the United States.

#### Subpart E—Defaults and Remedies, Reporting Requirements, Applicability of Regulations

##### § 298.40 Defaults.

(a) *In General.* Provisions concerning the existence and declaration of a default and demand for payment of the Obligations (described in paragraphs (b) and (c) of this section) shall be included in the Security Agreement and in other parts of the Documentation.

(b) *Principal and interest Payment Default.* Unless we have assumed the Obligor's rights and duties under the Obligation and agreements and have made any payments in default under terms in the Obligation or related agreements, the following procedures regarding principal and interest payment default shall apply:

- (1) No demand shall be made for payment under the Guarantees unless

the default shall have continued for 30 days (Payment Default).

(2) After the expiration of said 30-day period, demand for payment of all amounts due under the Guarantees must be made no later than 60 days afterward.

(3) After demand for payment is made by or on behalf of the Obligees, we shall make payment under the Guarantees, except if we determine that a Payment Default has not occurred or that such Payment Default has been remedied prior to demand being made.

(c) *Security Default.* If a default occurs under the Security Agreement which is other than a Payment Default (Security Default), section 1105(b) of the Act allows us, in our sole discretion, to declare such default a Security Default, and we may notify the Obligor or agent of the Obligor of such Security Default, stating that demand for payment under the Guarantees must be made no later than 60 days after the date of such notification.

(d) *Payment of Guarantees.* If we receive notice of demand for payment of the Guarantees, we shall, no later than 30 days after the date of such demand (provided that we shall not have, upon such terms as may be provided in the Obligations or related agreements, prior to that demand, assumed the Obligor's rights and duties under the Obligation and agreements and shall have made any payments in default), make payment to the Obligees, Indenture Trustee or any other agent of the unpaid principal amount of Obligations and unpaid interest accrued and accruing thereon up to, but not including, the date of payment.

#### **§ 298.41 Remedies after default.**

(a) *In general.* The Security Agreement or other parts of the Documentation shall include provisions governing remedies after a default, which relate to our rights and duties, the rights and duties of the Obligor, and other appropriate Persons.

(b) *Action by the Secretary.* (1) We may take the Vessel or Shipyard Project and hold, lease, charter, operate or use the Vessel or Shipyard Project, accounting only for the net profits to the Obligor after a default has occurred and is continuing and before making payment required under the Guarantees. (2) After making payment required under the Guarantees, we may initiate or otherwise participate in legal proceedings of every type, or take any other action considered appropriate, to protect rights and interests granted to us under:

- (i) Sections 1105(c), 1105(e) and 1108(b) of the Act,
- (ii) The Security Agreement,

(iii) Other applicable provisions of law, and

(iv) The Documentation.

(c) *Security proceeds to Secretary.* Our interest in proceeds realized from the disposition of or collection regarding the security granted to us in consideration for the Guarantees (except all proceeds from the sale, requisition, charter or other disposition of property purchased by us at a foreclosure or other public sale, which proceeds shall belong to and vest exclusively in us ), shall be an amount equal to, but not in excess of, the sum of (in order of priority of application of the proceeds):

(1) All moneys due and unpaid and secured by the Mortgage or Security Agreement;

(2) All advances, including interest thereon, by us, under the Security Agreement and all our reasonable charges and expenses;

(3) The accrued and unpaid interest on the Secretary's Note;

(4) The accrued and unpaid balance of the principal of the Secretary's Note; and

(5) To the extent of any collateralization by the Obligor of other debt due to us from the Obligor under other Title XI financings, such other Title XI debt.

(d) *Security proceeds to Obligor.* You shall be entitled to the proceeds from the sale or other disposition of security, described in paragraph (c) of this section, if and to the extent that the proceeds realized are in excess of the amounts described in paragraphs (c)(1) through (5) of this section.

#### **§ 298.42 Reporting requirements—financial statements.**

(a) *In general.* The financial statements of the Company shall be audited at least annually, in accordance with generally accepted auditing standards, by independent certified public accountants licensed to practice by the regulatory authority of a State or other political subdivision of the United States or, licensed public accountants licensed to practice by the regulatory authority or other political subdivision of the United States on or before December 31, 1970.

(b) *Eligible Export Vessels.* In the case of Eligible Export Vessels, the accounts of the Company shall be audited at least annually, and unless otherwise agreed to by us, we shall require that the financial statements be in accordance with generally accepted accounting principles, by accountants as described in paragraph (a) of this section or by independent public accountants licensed to practice by the regulatory authority or other political subdivision of a foreign country, provided such

accountants are satisfactory to us. The accountants performing such audits may be the regular auditors of the Company.

(c) *Reports of Company and other Persons.* Except as we require otherwise, the Company must file a semiannual financial report and an annual financial report, prepared in accordance with generally accepted accounting principles, with us as specified in the Documentation. You must include:

(1) The balance sheet and a statement of paid-in-capital and retained earnings at the close of the required reporting period,

(2) A statement of income for the period, and

(3) Any other statement that we consider necessary to accurately reflect the Company's financial condition and the results of its operations.

(d) *Required form.* We will specify in a letter to the Company the form required for reporting and the number of copies that you must submit

(e) *Other Persons.* We may after providing the Company notice, also require the Company to submit financial statements of any other Person, directly or indirectly participating in the project, if the financial condition of that Person affects our security for the Guarantees.

(f) *Timeliness.* The required financial report for the annual period will be due within 105 days after the close of each fiscal year of the Company, commencing with the first fiscal year ending after the date of the Security Agreement. The required semiannual report will be due within 105 days after each semiannual period, commencing with the first semiannual period ending after the date of the Security Agreement.

(g) *Public accountant's report.* The annual report will be accompanied by the public accountant's report based on an audit of the company's financial statements. We may require an audit by the public accountants of the financial statements contained in the company's semiannual report. We also may require certification of the semiannual report by the accountants. Where independent certification is not required, a responsible corporate officer will attach a certification that such report is based on the accounting records and, to the best of that officer's knowledge and belief, is accurate and complete.

(h) *Leveraged lease financing.* If the method of financing involved is a leveraged lease financing, or a trust is the owner of the Vessels, we may modify the requirements for annual and semiannual accounting reports of the Obligor accordingly.

(i) *Letter of confirmation.* The Company must furnish, along with its financial report, a letter of confirmation

issued by its insurance underwriter(s) or broker(s) that the Company has paid premiums on insurance applicable to the preservation, protection and operation of the asset, which information must state the term for which the insurance is in force.

**§ 298.43 Applicability of the regulations.**

(a) The regulations in this part are effective August 21, 2000, and apply to all applications made, Letter Commitments, Commitments to Guarantee Obligations or Guarantees

issued or entered into on or after August 21, 2000, under section 1104(a) of the Merchant Marine Act, 1936, as amended.

(b) The regulations in this part do not apply to any applications made, Letter Commitments, Commitments to Guarantee Obligations, or Guarantees issued under those regulations in effect before August 21, 2000. See 46 CFR, parts 200 to 499, edition revised as of October 1, 1996 and 46 CFR, parts 200 to 499, edition revised as of October 1, 1999 for regulations that apply to

applications made, Letter Commitments, Commitments to Guarantee Obligations, or Guarantees issued before August 21, 2000.

**Subpart F—Administration [Reserved]**

Dated: July 6, 2000.

By order of the Maritime Administrator.

**Joel C. Richard,**

*Secretary, Maritime Administration.*

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