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MARAD’s Capital Construction Fund

AD HOC COMMITTEE ON SHORT SEA SHIPPING

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MARAD's CAPITAL CONSTRUCTION FUND "CCF" PROGRAM

The Merchant Marine Act of 1970 authorized a "Capital Construction Fund" tax deferral program that allows participating vessel owners and operators to purchase vessels and retire vessel debt with pre-tax dollars.

1970 ACT PREDICTION

"It is believed that these provisions will do more than anything else in the bill to help the ship operating, and therefore the shipbuilding industry to build ships in United Ships yards which are so urgently needed to modernize our United States merchant marine."

S. Rep. No. 91-1080, at 43 (1970)

MARAD's CAPITAL CONSTRUCTION FUND "CCF" PROGRAM

While this "CCF" Program does not have significant name recognition, the names of CCF Program participants do.

BP Shipping, Crowley Maritime, Exxon, General Dynamics Matson Navigation and the Overseas Shipholding Group, GATX Corporation and General Electric Credit & Leasing – are all CCF Program participants.

MARAD's CAPITAL CONSTRUCTION FUND "CCF" PROGRAM

The 1970 Act limited the CCF Program to the U.S. foreign trades and domestic Great Lakes and non-contiguous (Alaska, Hawaii and Puerto Rico) trades.

The CCF Program has now been extended to Container and Roll-on/Roll-off services in all domestic trades.

MARAD's CAPITAL CONSTRUCTION FUND "CCF" PROGRAM

The CCF Program allows a taxpayer (which enters into a contract with MARAD) to shelter income from current taxation in exchange for the taxpayer's commitment to purchase or construct a new vessel or reconstruct an existing vessel.

MARAD's CAPITAL CONSTRUCTION FUND "CCF" PROGRAM

The CCF Program shelter is temporary, because when the sheltered income is used to purchase, construct or reconstruct a vessel, or to pay down vessel debt, the taxpayer's cost basis in that vessel is correspondingly reduced for the purpose of computing future depreciation.

MARAD's CAPITAL CONSTRUCTION FUND "CCF" PROGRAM

It may be useful to think of the CCF Program as providing the taxpayer with a "super accelerated depreciation" --

with the "depreciation deductions" taken in the years prior to the vessel's construction or reconstruction, rather than after the vessel has been placed in or returned to service.

SEVEN POINTS TO REMEMBER

- The CCF Program is a contractual program which allows a taxpayer to shelter income from current taxation in exchange for the taxpayer's commitment to purchase, construct or reconstruct a vessel built in a U.S. shipyard.
- The CCF Program shelter is temporary, because when the sheltered income is used, the taxpayer's cost basis in the vessel is reduced in computing the taxpayer's future depreciation.

SEVEN POINTS TO REMEMBER

- To make use of the CCF Program the taxpayer must have taxable income (or scheduled depreciation) from the ownership, operation or sale of at least one “agreement vessel,” or must have investment income from deposits already made under the CCF Program.

- An “eligible” vessel is any U.S. built, U.S. flag vessel operating in any U.S. domestic or foreign trade. A “qualified vessel” is any U.S. built, U.S. flag vessel operating, or to be operated, in a U.S. foreign or domestic Great Lakes, non-contiguous (Alaska, Hawaii or Puerto Rico) or Short Sea Transportation trade.

SEVEN POINTS TO REMEMBER

- A CCF Program participant may make deposits equal to the total of its taxable income, depreciation and proceeds of sale for that year from “agreement vessels”, and its CCF Program investment income.

- “Qualified” withdrawals may be made for the purchase, or construction or reconstruction of a “qualified vessel”, or for the payment of “qualified vessel” associated debt.

- All other withdrawals are “non-qualified” withdrawals which are taxed at the participant’s highest marginal rate and attract an interest charge intended to pay back the tax deferral benefit.

ALPHA CORP

The CCF tax provisions occupy only one section in each of U.S. Code Titles 26 and 46 -- but that section fills seven printed pages.

ALPHA CORP

Let’s examine Program use by Alpha Corp an established vessel owner-operator – in accumulating equity funds for new vessel purchases.

ALPHA CORP: SHELTERING CURRENT EARNINGS

Alpha Corp currently operates an integrated tug and barge ("ITB") container service between New Orleans, Louisiana, and Tampa, Florida.

Alpha is investigating the acquisition of three small Roll-on/Roll-off ("Ro/Ro") vessels to carry 53 foot trailer units in a new trans-Gulf domestic service between Brownsville, Texas, and Tampa.

ALPHA CORP: SHELTERING CURRENT EARNINGS

Alpha Corp wishes to contract for 2012 deliveries. Alpha believes that shipyard prices will be approximately $30 million for each Ro/Ro, for a total cost of $90 million for three vessels.

Alpha expects MARAD Title XI debt financing for 80 per cent of the Ro/Ro costs. But Alpha will still need to provide $18 million for vessel equity.

ALPHA CORP: SHELTERING CURRENT EARNINGS

Alpha can only afford to put aside about $3 million per year from its current ITB service after tax earnings to fund the equity for this plan.

If Alpha accumulates its needed equity with only these $3 million set asides, Alpha will accumulate only $10.76 million over the next 5 years – enough equity for the purchase of only one new Ro/Ro.

ALPHA CORP: SHELTERING CURRENT EARNINGS

Year	***Taxable Income[a]***	***Tax Payable[b]***	***Non-CCF Account Deposits (Jan 1)[c]***	***Income on Non-CCF Account Balance (Dec 31) [c][d]***	***Tax Payable on Non-CCF Account Income[b]***	***Non-CCF Account Balance (Dec 31)***
1	$3,000,000	$1,200,000	$1,800,000	$180,000	$72,000	$1,908,000
2	$3,000,000	$1,200,000	$1,800,000	$370,800	$148,320	$3,930,480
3	$3,000,000	$1,200,000	$1,800,000	$573,048	$229,219	$6,074,309
4	$3,000,000	$1,200,000	$1,800,000	$787,431	$314,972	$8,346,767
5	$3,000,000	$1,200,000	$1,800,000	$1,014,677	$405,871	$10,755,573

Equity funds available for fleet expansion: $10,755,573 – One Ro/Ro

a) Taxable income from prior tax year.
b) Assuming a federal tax at Alpha’s highest marginal rate, and a combined federal and state tax rate of 40 percent.
c) Taxable income remains taxable in the absence of CCF account deposits.
d) Assuming a 10.0 percent rate of return on deposited funds.

ALPHA CORP: SHELTERING CURRENT EARNINGS

Alpha enters a CCF Program contract and deposits $3 million of ITB vessel earnings in each of the next five years for use as Ro/Ro vessel equity.

At the end of the five years, this $15 million, together with $5.15 million of investment income, will provide Alpha with $20.15 million for Ro/Ro vessel equity; sufficient for the purchase of the three Ro/Ros needed.

ALPHA CORP: SHELTERING CURRENT EARNINGS

Year	*Taxable Income[a]*	*CCF Account Deposits (Jan 1)*	*Tax Payable*	*Income on CCF Account Balance (Dec 31)[b]*	*Tax Payable on CCF Account Income*	*CCF Account Balance (Dec 31)*
1	$3,000,000	$3,000,000	-0-	$300,000	-0-	$3,300,000
2	$3,000,000	$3,000,000	-0-	$630,000	-0-	$6,930,000
3	$3,000,000	$3,000,000	-0-	$993,000	-0-	$10,923,000
4	$3,000,000	$3,000,000	-0-	$1,392,300	-0-	$15,315,300
5	$3,000,000	$3,000,000	-0-	$1,831,530	-0-	$20,146,830

Equity funds available for fleet expansion: $20,146,830 – Three Ro/Ros

a) Taxable income from prior tax year.
b) Assuming a 10.0 percent rate of return on deposited funds.

ALPHA CORP: SHELTERING CURRENT EARNINGS

Equity funds without CCF: $10,755,573 – One Ro/Ro

Equity funds with CCF: $20,146,830 – Three Ro/Ros

1970 ACT PREDICTION

“It is believed that these provisions will do more than anything else in the bill to help the ship operating, and therefore the shipbuilding industry to build ships in United Ships yards which are so urgently needed to modernize our United States merchant marine.”

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PREDICTION FULFILLED

Since 1970 there have been 73 Container and Ro/Ro vessels built for U.S. blue water trades in United States shipyards. MARAD CCF financing was a part of the financing for 72 of these 73 vessels.

THANK YOU

ADDITIONAL INFORMATION: For background and follow-on reading you may wish to refer to my "Financing with the Maritime Administration's Capital Construction Fund," Benedict's Maritime Bulletin, Third/Fourth Quarter 2007, or my Marine Money International articles "Financing the US Market via MARAD's "CCF" Program," Marine Money International, October 2007, and "Financing the US Market via MARAD's "CCF" Program," Marine Money International, June 2002.

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