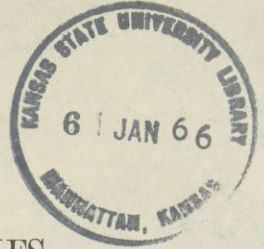


SHIP MORTGAGE BONDS

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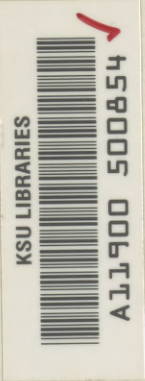
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HEARINGS
BEFORE THE
SUBCOMMITTEE ON
MERCHANT MARINE AND FISHERIES

OF THE
COMMITTEE ON COMMERCE
UNITED STATES SENATE
EIGHTY-NINTH CONGRESS



FIRST SESSION

ON

S. 2118

TO CLARIFY SECTIONS 9 AND 37 OF THE SHIPPING ACT,
1916, AND SUBSECTION O(d) OF THE SHIP MORTGAGE ACT,
1920, AND FOR OTHER PURPOSES

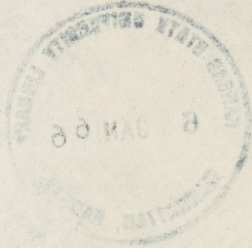
JUNE 23, JULY 9 AND 15, 1965

Serial No. 89-36

Printed for the use of the Committee on Commerce



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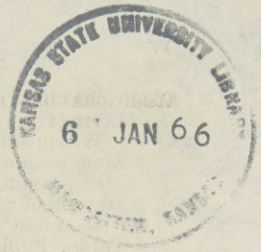
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Alvin James, vice president, Irving Trust Co., One Wall Street, New York, N. Y.

Barnett, John, counsel for the Chemical Bank, New York Trust Co., 60 Wall Street, New York, N. Y.

Clayton, Edwin S. Moore, One Chase Manhattan Plaza, New York, N. Y.

Irvin, Carl C., General Counsel, Maritime Administration, Bureau of Commerce, Washington, D. C.; represented by John B. Paskard, Assistant General Counsel, Division of Morgans, and State Insurance

Hugh Robert F. Leathers, Jr., Counsel, Federal Reserve Bank, D. C. on behalf of the Comptroller General, Washington, D. C.

James Solomon, attorney for Seatrade, Washington, D. C. and Virginia

Johnson & Johnson, 1000 Pennsylvania Avenue, N. W., Washington, D. C.

Keenan, Robert, Attorney at Law, 1000 Pennsylvania Avenue, N. W., Washington, D. C.

Letter from New York, N. Y. and General Counsel, State Insurance Commission, Washington, D. C.

Letter, Thomas A. Washington, President, State Insurance Commission, 400 First Street, N. W., Washington, D. C.

Letterhead, William B. Lee, Attorney, Rarick & Co., Two Wall Street, New York, N. Y.

Letter, Paul A. Webster, Attorney, 110 Broadway, New York, N. Y.

Letter, One Rockefeller Plaza, New York, N. Y., on behalf of the trustees, Teachers W. Fund and Raymond I. Scott, Central Corp.

Additional information received—

Communication from State Department dated July 20, 1965, and August 21, 1965, re Alvin James, dated July 6, 1965, and July 7, 1965, dated August 17, 1965, from the Embassy of the Federal Republic of Germany.

Letter by F. S. Gault of Agents, Fourth Street, Chemical Bank, New York Trust Co., trustee, Washington v. American Petroleum Corp.

Letter from Bank of America and Finance Co. with dated July 2, 1965, letter from Irving Trust & Co., 60 Wall Street, New York, N. Y., dated August 11, 1965.

Letter from First National City Bank, 600 First Avenue, New York, N. Y., dated June 18, 1965.

Letter from the Insurance Association of America, 1701 R Street, N. W., Washington, D. C., dated August 11, 1965.

Letter from Washington Insurance Co. of Arlington Avenue, New York, N. Y., dated June 21, 1965.

Letter from New York, N. Y. on the Insurance Co. of Manhattan Avenue, New York, N. Y., dated June 22, 1965.

SHIP MORTGAGE BONDS

WEDNESDAY, JUNE 23, 1965

U.S. SENATE,
 COMMITTEE ON COMMERCE,
 SUBCOMMITTEE ON MERCHANT MARINE AND FISHERIES,
 Washington, D.C.

The subcommittee met at 10:10 a.m. in room 1202, New Senate Office Building, Hon. E. L. Bartlett presiding.

Senator BARTLETT. The subcommittee will be in order.

The purpose of the hearing this morning is to take testimony on S. 2118, a bill intended to clarify sections 9 and 27 of the Shipping Act of 1916 and subsection O(d) of the Ship Mortgage Act of 1920, and for other purposes.

This legislation was introduced by request for the purpose of directing attention and initiating hearings on a proposal directed toward meeting any problem that arises out of the decision of the U.S. Court of Appeals for the Fourth Circuit, handed down April 5, 1965, in the case entitled "*Chemical Bank New York Trust Company v. S.S. Westhampton*."

Since this is an extremely complex matter, there will be no attempt to complete the hearings this morning, but I do hope that substantial progress can be made so that the record can be completed with further hearings early next month.

(The bill follows:)

[S. 2118, 89th Cong., 1st sess.]

A BILL To clarify sections 9 and 37 of the Shipping Act, 1916, and subsection O(d) of the Ship Mortgage Act, 1920, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 9 of the Shipping Act, 1916 (46 U.S.C. 808), is amended by adding at the end of the third paragraph thereof the following: "Provided, however, That any bond, note, or other evidence of indebtedness heretofore or hereafter made or issued under a trust indenture in connection with a mortgage on a vessel shall not be deemed to be such an interest in the vessel, the sale, mortgage, delivery, or transfer in any manner of which without the approval of the Secretary of Commerce is prohibited by this section, if the trustee designated in such trust indenture is a citizen of the United States within the meaning of section 2 of the Shipping Act, 1916 (46 U.S.C. 802)."

SEC. 2. Section 37 of the Shipping Act, 1916 (46 U.S.C. 835) is amended by adding at the end of section (b) thereof the following: "Provided, however, That any bond, note, or other evidence of indebtedness heretofore or hereafter made or issued under a trust indenture in connection with a mortgage on a vessel shall not be deemed to be such an interest in the vessel the sale, mortgage, delivery, or transfer in any manner of which without first obtaining the approval of the Secretary of Commerce is prohibited by this section, if the trustee designated in

Staff counsel assigned to this hearing: William C. Foster.

such trust indenture is a citizen of the United States within the meaning of section 2 of the Shipping Act, 1916 (46 U.S.C. 802)."

SEC. 3. Subsection O(d) of the Ship Mortgage Act, 1920 (46 U.S.C. 961(d)) is amended by adding at the end of the first sentence thereof the following: "*Provided, however,* Any bond, note, or other evidence of indebtedness heretofore or hereafter made or issued and secured by a mortgage on a vessel of the United States shall not be deemed to constitute a right under such mortgage within the meaning of this subsection if such mortgage is held by a trustee who is a citizen of the United States within the meaning of section 2 of the Shipping Act, 1916 (46 U.S.C. 802)."

SEC. 4. If any provision or portion of this Act, or the application thereof in any particular circumstance, is held invalid, the remainder of the Act and the application of such provision or portion to other circumstances shall not be affected thereby.

(The agency comments follow:)

COMPTROLLER GENERAL OF THE UNITED STATES,
Washington, D.C., June 22, 1965.

B-97285.

HON. WARREN G. MAGNUSON,
*Chairman, Committee on Commerce,
U.S. Senate.*

DEAR MR. CHAIRMAN: Your letter of June 11, 1965, invites our comments on S. 2118, a bill to clarify sections 9 and 37 of the Shipping Act, 1916, and subsection O(d) of the Ship Mortgage Act, 1920, and for other purposes.

We have no special information or knowledge that would assist in the consideration of S. 2118, and therefore have no comments to offer.

Sincerely yours,

FRANK H. WEITZEL,
Assistant Comptroller General of the United States.

FEDERAL MARITIME COMMISSION,
OFFICE OF THE CHAIRMAN,
June 16, 1965.

HON. WARREN G. MAGNUSON,
*Chairman, Committee on Commerce,
U.S. Senate,
Washington, D.C.*

DEAR MR. CHAIRMAN: This is in reply to your request of June 11, 1965, for the views of the Federal Maritime Commission with respect to S. 2118, a bill to clarify sections 9 and 37 of the Shipping Act, 1916, and subsection O(d) of the Ship Mortgage Act, 1920, and for other purposes.

Inasmuch as the bill does not affect the responsibilities or jurisdiction of the Commission, we express no views as to its enactment.

The Bureau of the Budget has advised that there would be no objection to the submission of this letter from the standpoint of the administration's program.

Sincerely yours,

JOHN HARLEE,
Rear Admiral, U.S. Navy (Retired), Chairman.

THE GENERAL COUNSEL OF THE TREASURY,
Washington, D.C., July 29, 1965.

HON. WARREN G. MAGNUSON,
Chairman, Committee on Commerce, U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: Reference is made to your request for the views of this Department on S. 2118, to clarify sections 9 and 37 of the Shipping Act, 1916, and subsection O(d) of the Ship Mortgage Act, 1920, and for other purposes.

The proposed legislation would amend the Shipping Act, 1916, and the Ship Mortgage Act, 1920, to make it clear that the approval of the Maritime Administration of the Department of Commerce is not necessary for the issuance or transfer to persons not citizens of the United States of ship mortgage bonds on a vessel of the United States if the mortgage is held by a trustee who is a citizen.

While the Bureau of Customs of this Department has certain responsibilities in administering the laws which would be amended by the bill, the policy considerations here involved are beyond the scope of the Department. The Secretary of Commerce is primarily charged with consideration of policy matters with respect to the transfer of interests in vessels owned in the United States and will no doubt comment on the advisability of the proposal from the standpoint. Should the proposed legislation be enacted, this Department anticipates no unusual administrative difficulties in carrying out its responsibilities thereunder.

The Department has been advised by the Bureau of the Budget that there is no objection from the standpoint of the administration's program to the submission of this report to your committee.

Sincerely yours,

FRED B. SMITH,
Acting General Counsel.

Senator BARTLETT. The first witness is Carl C. Davis, General Counsel of the Maritime Administration. Mr. Davis, we are pleased to have you here.

STATEMENT OF CARL C. DAVIS, GENERAL COUNSEL, MARITIME ADMINISTRATION, DEPARTMENT OF COMMERCE, WASHINGTON, D.C.; ACCOMPANIED BY JOHN R. TANKARD, ASSISTANT GENERAL COUNSEL, DIVISION OF MORTGAGE AND MARINE INSURANCE, MARITIME ADMINISTRATION, DEPARTMENT OF COMMERCE, WASHINGTON, D.C.

Mr. DAVIS. Thank you.

Mr. Chairman, I have with me Mr. John Tankard, Assistant General Counsel in charge of the Division of Mortgage and Marine Insurance.

Senator BARTLETT. We are delighted to have you.

Mr. DAVIS. Mr. Chairman, thank you for the opportunity of appearing before your committee to present the views of the Maritime Administration of the Department of Commerce, and of the Department, on S. 2118.

The purpose of S. 2118 is to cure the difficulties with respect to ship financing which were created by the decision of the Court of Appeals, Fourth Circuit, in *Chemical Bank New York Trust Company, Trustee, Mortgagee v. Steamship Westhampton*, decided April 5, 1965. This case involved a mortgage on an American-flag ship which was held in trust by a U.S. citizen trustee to secure a bond held by an alien.

Before stating the holding in this case, I will state the various statutes which govern the financing of American-flag ships with foreign funds and those which govern the transfer of American-flag ships to foreign ownership or registry.

Section 4132 of the Revised Statutes (46 U.S.C. 11) provides that a ship, wherever built, may be documented under U.S. laws for operation in foreign trade if it is owned by citizens of the United States or by a corporation organized under the laws of the United States, or of any State thereof, whose chief executive officer and chairman of the board of directors are citizens of the United States and all but a minority of the number of directors necessary to constitute a quorum are citizens of the United States. This section has no prohibition on alien ownership of stock in the corporation. The Bureau of Customs, which administers the documentation laws, will document such a vessel even

if all of the stock in the corporation is owned by aliens. Such a vessel, however, cannot engage in the coastwise trade.

Section 4312 of the Revised Statutes (46 U.S.C. 252) together with section 27 of the Merchant Marine Act, 1920, provides that a vessel may be documented for operation in the coastwise trade if the vessel was built in the United States and is owned by citizens of the United States as defined in section 2 of the Shipping Act, 1916. Section 2 of the Shipping Act, 1916, states that a corporation is not a citizen of the United States for purposes of operation in the coastwise trade unless it meets the same requirements as for documentation for operation in foreign trade and, in addition, the controlling interest in the corporation is owned by citizens of the United States. This section further provides that the controlling interest will not be deemed to be held by citizens of the United States unless such citizens hold 75 percent of the stock. Under these provisions, therefore, an alien is permitted to hold 25 percent of the stock so long as this does not constitute a controlling interest.

Section 9 of the Shipping Act, 1916, provides that it is unlawful, without the approval of the Secretary of Commerce, to sell, mortgage, lease, charter, deliver, or in any manner transfer to any person not a citizen of the United States—as defined in section 2 thereof—or to place under foreign registry, any vessel, or any interest therein, owned in whole or in part by a citizen of the United States and documented under the laws of the United States. The section further provides that any vessel, or any interest therein, chartered, sold, transferred, or mortgaged to a person not a citizen of the United States, or placed under foreign registry, in violation of the section shall be forfeited to the United States.

The definition of citizen of the United States in section 2 is the same for foreign trade as for domestic trade except that for foreign trade the controlling interest will not be deemed to be in citizens of the United States unless at least 50 percent of the stock in the corporation is owned by citizens of the United States. Section 9 is in force both in peacetime and in times of emergency. The prohibition of this section applies only to U.S. documented vessels which are owned by citizens of the United States. If the controlling interest is not in citizens of the United States, this section does not prohibit transfer of the vessel to foreign ownership or registry without the consent of the Secretary of Commerce.

Section 37 of the Shipping Act, 1916, which is in effect during war or national emergencies is broader than section 9. We have been in a national emergency within the meaning of section 37 since 1950. Section 37 provides with regard to ships that during war or national emergency declared by the President it is unlawful, without the prior approval of the Secretary of Commerce, to transfer to foreign registry any vessel owned by a citizen of the United States or by any corporation organized under the laws of the United States or any State thereof. This prohibition applies to all American-flag vessels. The section also provides that it is unlawful to sell, mortgage, lease, charter, deliver, or in any manner transfer to any person not a citizen of the United States, any such vessel or any interest therein. The section further provides that any vessel or any interest therein which is sold, mortgaged, leased, chartered, delivered, transferred, or docu-

mented in violation of the section shall be forfeited to the United States, and that any such sale, mortgage, lease, charter, delivery, transfer, or documentation shall be void.

The Ship Mortgage Act, 1920, provides for the creation of preferred mortgages on vessels documented under the laws of the United States if the mortgage is recorded in the office of the Collector of Customs of the port of documentation of the vessel. The mortgagee under such a mortgage must be a citizen of the United States as defined in section 2 of the Shipping Act, 1916. This act specifically provides that the term mortgagee in the case of a mortgage involving a trust deed and a bond issue thereunder means the trustee designated in the deed. The act states no requirements with respect to the citizenship of the bondholders, and we believe this indicates that the bondholders may be aliens.

The purpose of reciting the foregoing provisions of law is to indicate that there are circumstances under which the financing of ships with foreign funds is permitted and welcomed under U.S. laws. There are circumstances under which an American-flag ship can be subjected to sale in a foreign port. If the vessel is furnished necessaries in a foreign port, such as repairs, supplies, towage or, use of drydock or marine railway, the supplier obtains a maritime lien under the general maritime law, and he can subject the vessel to sale if he is not paid.

The facts in *Chemical Bank New York Trust Company, Trustee, Mortgagee v. Steamship Westhampton* decided by the Court of Appeals, Fourth Circuit, were that a mortgage on an American-flag ship was given to a U.S. citizen trustee to secure a bond held by an alien. The court held that the mortgage was not entitled to preferred status under the Ship Mortgage Act, 1920, because the bond which was secured by the mortgage was an interest in a ship under section 37 of the Shipping Act, 1916, and the issuance of the bond to an alien had not been approved by the Secretary of Commerce.

We believe the decision in this case is wrong. We believe that section 37 of the Shipping Act, 1916, contains within itself a definition of "interest" in a ship which excludes a bondholder. The section provides that it is unlawful to sell, mortgage, lease, charter, deliver, or in any manner transfer, without the approval of the Secretary of Commerce, to any person not a citizen of the United States, any interest in a ship documented under the laws of the United States; that any such interest which without such consent is sold, mortgaged, leased, chartered, delivered, or transferred in violation of the section is forfeited to the United States; and that any such sale, mortgage, lease, charter, or delivery is void.

We believe that under this section an interest in a ship is an ownership interest such as a partner or joint adventurer would have and that it does not include the interest of a bondholder. It is reasonable to talk of mortgaging, leasing, or chartering a ship, or if the ship is owned by partners, of the mortgaging, leasing, or chartering an interest in the ship. But it is not reasonable to talk of mortgaging, leasing, or chartering the interest of a bondholder. In ordinary legal language the term "mortgage" includes the bond secured by the mortgage, but the plain language of the Ship Mortgage Act, 1920, is that in case of a bond issue the term mortgagee means the trustee. And that act states no requirements with regard to the citizenship of the bondholders.

As we have stated, we believe that the decision in the *Westhampton* case is wrong. A petition for reargument was filed on May 5, 1965, and on the same date the Committee of American Steamship Lines filed a petition to appear in the case. The Court of Appeals, Fourth Circuit, on May 24, 1965, issued an order granting the petition of the Committee of American Steamship Lines and on May 25, 1965, invited replies to the petition for reargument. The Department of Commerce is preparing a request to the Department of Justice that if rehearing is granted, the Department of Justice appear to represent the position of the Department of Commerce or permit the Department of Commerce to appear on its own behalf to present its position.

If rehearing is granted and if, regardless of its outcome, a petition for certiorari is made to the U.S. Supreme Court, it may be well over a year from now before this litigation is finally settled.

In the meantime the private financing of ships must go on unless the Government is willing to do direct financing which it is not. We can take administrative action by way of giving advance blanket approval under sections 9 and 37 to the acquisition of bonds by foreigners which, in our opinion, would obviate the difficulties created by the *Westhampton* decision, and we have such action under consideration. We believe that all of the approvals we have given under our title XI financing would constitute approval under sections 9 and 37 to the foreign holding of the bonds involved in that financing. The bond market, nevertheless, is sensitive, and we believe legislation should be enacted so as to give further assurance of the validity of future and past financing.

The bill, S. 2118, would amend sections 9 and 37 of the Shipping Act, 1916, by including provisos which state that any bond, note, or other evidences of indebtedness heretofore or hereafter made under a trust indenture in connection with a mortgage on a ship is not an interest in a ship within the meaning of those sections if the trustee is a citizen of the United States. We believe these amendments would take care of the difficulties created by the *Westhampton decision* with respect to bonds secured by a mortgage in the hands of a trustee. The mortgage, however, goes on the ship only after the ship is completed. The construction of a ship is frequently financed by a loan which is secured by an assignment of the owners' rights in the ship to a trustee. This situation is not clearly within the language of the proposed amendment. We recommend therefore that the bill be amended by inserting in line 8, page 1, after the word "vessel," and in line 10, page 2, after the word "vessel" a comma and the words "or in connection with an assignment of the owner's right, title or interest in respect of a vessel under construction" and a comma.

Where the provisions in sections 1 and 2 of the bill speak of the citizen ship of the trustee, they use the language "the trustee designated in such trust indenture." Since such trustee may have a successor, we recommend that the bill be amended by inserting in line 2, page 2, and in line 14, page 2, after the word "indenture" a comma and the words "including any successor or assign" and a comma.

Subsection O(d) of the Ship Mortgage Act, provides that no rights under a mortgage of a vessel of the United States shall be assigned to a person not a citizen of the United States without the approval of the Secretary of Commerce and that any such assignment shall be

void. Section 3 of the bill would amend this section to provide that any bond, note, or other evidence of indebtedness heretofore or hereafter made and secured by a mortgage on a vessel of the United States shall not be deemed to constitute a right under a mortgage within the meaning of that section if the mortgage is held by a trustee who is a citizen of the United States. We think this is a necessary amendment.

The provisions of the bill would be retroactive. It is not clear under the decision what would be forfeited to the United States. We believe the ship is forfeited on the basis that the court is in substance holding that the ship was mortgaged to an alien without our consent. The Maritime Bar, which includes some of the best lawyers in the United States, have been in agreement that our approval under sections 9 and 37 of the Shipping Act, 1916, of the issuance or transfer of a bond to an alien is not necessary. Any contracting that has been done, therefore, with respect to a ship that has a preferred mortgage on it with a bond held by an alien was done in the belief that the preferred mortgage was valid. We do not believe that the people who did this contracting should obtain a windfall gain as a result of this decision or that the United States should benefit by the forfeiture. We agree, therefore, that the bill should be retroactive.

With the amendments proposed, we recommend favorable consideration of the bill.

While the Bureau of the Budget advises there is no objection to the submission of this testimony, it has been unable to secure the views of the Department of Justice in the time available and believes that the committee will want to have that department's views in its consideration of the bill.

Senator BARTLETT. Thank you, Mr. Davis. Mr. Foster, do you have any questions?

Mr. FOSTER. Yes, sir.

Mr. DAVIS, what effect would this bill have on pending litigation?

Mr. DAVIS. Mr. Foster, I do not believe that this bill would affect the pending litigation in the *Westhampton* case.

Mr. FOSTER. Why?

Mr. DAVIS. Because you have to deal with the question of vested rights, and if that decision is not reversed, I think we may have the problem of vested rights involved there.

Mr. FOSTER. In any event, the position of the Maritime Administration would be that the legislation should not affect the pending litigation; is that correct?

Mr. DAVIS. That is my view; yes, sir.

Mr. FOSTER. And if this bill might be interpreted in such a way as to affect it, the Administration would not be opposed to amending the bill, accordingly?

Mr. DAVIS. Mr. Foster, I think I would oppose the amendment of the bill, accordingly, because the factors which now cause me to say that this bill should not affect pending litigation in the *Westhampton* case would have maybe been overcome by subsequent court decisions.

Mr. FOSTER. I wonder if you could develop that a bit more because I am not sure I understand what you said.

Mr. DAVIS. I think if we amend this bill accordingly, there would be a holding by the court of appeals, or the Supreme Court, that the

secondary creditors involving the *Westhampton* decision did not have vested rights.

Mr. FOSTER. Let me try my question again. Congress, of course, within the framework of the Constitution, can make legislation retroactive.

Mr. DAVIS. That is true.

Mr. FOSTER. It is possible to draft a retroactive provision which is applicable to certain transactions, events, or occurrences, and not to others.

Mr. DAVIS. That is right. You have it provided for in this legislation.

Mr. FOSTER. It would be possible to express that Congress is not interested in having this amendment to the extent that it does change the law as determined by the court subsequently, is not interested in having the amendment affect the determination of pending cases, but is interested in having the legislation affect all of the transactions that had occurred prior to the effective date of the act.

By transactions, I mean the negotiations and the sale of bonds that occurred prior to the effective date. It could apply to those sales, but not apply to any actions pending in court.

Mr. DAVIS. Congress could do that, that is true, and, of course, it has been done. I remember, for example, the Home Port Act. However, I think it is an unnecessary act on the part of Congress if you think that it might involve a constitutional question without such provision being in the statute, and I would say that those interests that might be constitutionally protected would be protected, anyway.

You have a severability clause in there that if any portion is held invalid, this will not affect the validity of the other portions. The court is not going to take anyone's vested right by reason of this bill.

So I would think that an amendment reserving the rights in litigation would not be necessary in the bill.

Mr. FOSTER. Let me just make the comment that it is not too clear, of course, what a vested right is. Any time Congress acts, rights are changed, and sometimes changed retroactively.

Mr. DAVIS. And particularly in this area of the law of maritime liens, what constitutes a vested right is a very difficult question.

For example, as you know, this is an area of secret liens. The one and only nonsecret lien that we know of is the preferred ship mortgage. Otherwise, you are in an area of secret liens. You are also in an area that within categories, for example, on one side you have the tort liens, and on the other side, you have your contract liens.

Normally, in the land law, you can walk up and find out what your situation is when you extend credit. Here, subsequent events always affect your priority status as a creditor within either category, contract or court tort lien. The last in time and first in priority in respect of payment is the governing rule. Some people's priority status, their so-called vested rights status, is being affected constantly as the ship operates.

The law is designed this way to encourage people to continue to promote credit to the vessel, to keep it in operation for navigation in commerce, affording an opportunity to make money. But, your creditor's rights are constantly changing.

Mr. FOSTER. I wonder if you would say a bit more about the point you made on page 8 of your statement, in which you said:

We can take administrative action by way of giving advance blanket approval under sections 9 and 37 to the acquisition of bonds by foreigners which, in our opinion, would obviate the difficulties created by the *Westhampton* decision, and we have such action under consideration.

What can you do to meet this problem without legislation?

Mr. DAVIS. Well, in respect to the past financing transactions, I am not prepared to say whether or not we could issue retroactive blanket approvals. Insofar as future transactions are concerned, I do think we could issue blanket approvals, but all of this may not fully achieve what the Congress has tried to accomplish by ship-financing legislation.

This is a sensitive area in which Congress has constantly urged us to do everything we can to get the interest rate down, to have a wide market for these bonds, to get them accepted on the market, and this legislation, if the objectives of Congress are to be carried out, is highly essential to that mission.

Mr. FOSTER. If the Maritime Administration has the authority to solve a problem for the future and you are not sure of whether or not you have authority to solve the problem for the past, one thought might be that Congress might wait to see whether you couldn't decide whether or not you could solve it for the past.

Mr. DAVIS. Well, Mr. Foster, in our title XI financing, we think that our actions have been such as to have given approval. With respect to other financing—and, of course, you know there is a lot of outside financing—we have refused to exercise our discretion predicated upon our decisions that it was not necessary to grant such approvals. Once having made the decision not to exercise our discretion, I doubt our ability now to turn around and exercise our discretion after the event.

Mr. FOSTER. Mr. Davis, the Maritime Administration is an agile and effective instrument of Government, and it can change its position from time to time as circumstances arise.

I don't quite understand why that agility could not be practiced in this situation. You have to reconsider your position when court decisions are made and other occurrences develop?

Mr. DAVIS. Oh, yes.

Mr. FOSTER. I don't understand why you wouldn't consider it, and as I understand it, from your statement, you say we have such action under consideration. Is it my understanding you don't have any active consideration of the possibility of issuing a retroactive blanket confirmation of this?

Mr. DAVIS. No; the one we have under consideration, Mr. Foster, is forfeiture.

Mr. FOSTER. Only?

Mr. DAVIS. Yes, sir.

Senator BARTLETT. Mr. Kenney?

Mr. KENNEY. If I may, on this point, if I understand your statement, then, and your discussion of the court case, section 37 of the Shipping Act of 1916 is one of the controlling sections?

Mr. DAVIS. Yes, sir.

Mr. KENNEY. That, of course, as I read it, requires the prior approval of the Secretary of Commerce to do these things.

Mr. DAVIS. It says we must weigh it against the national interest at the time, and not to go back and do it now, when we already—

Mr. KENNEY. You couldn't go back and do it now with language that calls for prior approval of the Secretary.

Mr. FOSTER. That is right. This order, to get the record straight, are you saying that you believe, under the law, you considered doing this, but you are not considering doing it; or is your position that under the law you have determined that you don't have any authority to do it?

Mr. DAVIS. Under the law, we have determined that we do not have the authority to do it retroactively. But, prospectively, we have that under consideration right now for future transactions.

Mr. FOSTER. So you have no authority to solve the problem retroactively, in your opinion.

Mr. DAVIS. Because it has to be done at the time of the incident.

Mr. FOSTER. It is not that the administration is not being its usual agile self, but you do not have the authority.

Mr. DAVIS. On page 4, I have inserted the word "prior." I did leave it out in the draft.

Mr. FOSTER. How serious is this in terms of financing the construction of new vessels for the U.S. merchant marine?

Mr. DAVIS. I think it has created quite a serious problem, and if I may say so, the man who has been dealing with the people involved, most closely, is Mr. Tankard. May I refer to him in response to that question?

Mr. TANKARD. The Congress has devoted a lot of its legislation to making ship financing acceptable in the marketplace. The history of the administration of title XI shows that there is about a half percent interest rate factor here—difference between a mortgage given directly to a citizen mortgagee investor and a mortgage given to a trustee with the bond sold to the public, or to investors who are not willing to undertake the role of the mortgagee.

Now, the one-half percent interest factor, alone, would amount to about a half million dollars, roughly, in additional interest charge in the financing of a ship over the 25-year life of the ship.

I think that if the objectives intended by the Congress and the administration of the statute are to be achieved, then it is necessary that the bonds have complete marketability as we thought they had before the *Westhampton* decision.

There are about 300 ships in the subsidized fleet. Now, these ships all have to be financed. It is now the policy of the Government and the Congress not to appropriate money directly to finance these ships. The reliance is completely on title XI. In relying on title XI and pledging the faith of the United States, and in making the contracts of insurance incontestable, it has been the objective to obtain the lowest possible interest rate, to have an interest rate reasonable in relation to the interest rate on direct obligations of the Government, and to have it commensurate with the pledge of the faith of the United States.

That has been our objective, and I think we have successfully achieved it with the underwriting groups that have been involved.

This decision could be a serious threat to the accomplishment of those objectives. The bondholders, naturally, would be concerned about investing in a mortgage which is invalid. It raises the question as to the basic validity of the Government's insurance.

If that validity turns on the citizenship of the bondholders, then this could occur: the citizenship might be involved in the holding of one or more bonds or it might be involved in the holding of the entire group of bonds.

The Congress intended, for example, that there be investments by States, State funds, pension funds, many of which are not characterized in the law as citizens or noncitizens. They are undefined or unclassified in the law.

Now, these groups could not invest in these bonds if there are questions of validity of the Government's insurance and the mortgage involved. I might add that in many instances, the bonds that are issued are bearer bonds. In the case of the Santa Paula financing, there was a \$9 million mortgage. Over \$8 million of those bonds, over 8,000 in number of bonds, were bearer bonds.

These bonds went into the marketplace. We do not know, and it would be very difficult to determine who all the owners have been. We do not know the citizenship of those owners. Under this decision, there could be real questions as to whether or not those bonds are valid bonds. However, in respect of the title XI bonds, we have given approval to the transactions.

We have approved the mortgagee; we have approved every document that goes into the transaction under which the bonds are sold, under which the rights of the bondholders are created, under which the trustee exercises all of its functions.

In every way, we have examined the transactions. For that reason, we do not think that approval under the Shipping Act is additionally required, or if it is required, we think that it has been given.

Mr. FOSTER. One other question, if I may, Mr. Chairman. I wonder if you could supply for the committee a half dozen specific examples of the types you just mentioned in which this problem arose?

Mr. TANKARD. Public bond issues?

Mr. FOSTER. Yes, sir; you know, reference—

Mr. DAVIS. You mean in which this bond problem is involved?

Mr. FOSTER. Yes, sir.

Mr. DAVIS. Yes, sir.

Mr. TANKARD. We can give the committee examples. We have a compilation, if you would like it, of all of the trustee and the non-trusted financings, if the committee would like that.

Mr. FOSTER. Yes, sir, please.

Mr. TANKARD. We will furnish that.

Mr. FOSTER. Thank you, Mr. Chairman.

(The information requested above follows:)

SHIP MORTGAGE BONDS

TITLE XI, MERCHANT MARINE ACT, 1936, AS AMENDED
Public bond issues outstanding—With trustees as of June 30, 1965
 [Bonds sold to public and traded through brokers] ¹

Mortgagor	Mortgagee/trustee	Vessel	Date of mortgage	Original principal amount
American Export Isbrandtsen Lines, Inc.	First National City Bank	Export Ambassador	June 20, 1961	\$4,500,000
		Export Adventurer	do	4,500,000
		Export Agent	do	4,500,000
American President Lines, Ltd.	Bank of America National Trust & Savings Association	Export Aide	do	4,500,000
		President Lincoln	May 23, 1961	7,200,000
		President Tyler	Aug. 3, 1961	7,200,000
		President Polk	Aug. 27, 1963	4,850,000
		President Monroe	do	4,850,000
Grace Line, Inc.	First National City Bank	President Harrison	do	4,850,000
	Chemical Bank New York Trust Co.	Santa Paula	Nov. 7, 1958	9,000,000
	The Chase Manhattan Bank	Santa Rosa	Oct. 15, 1958	7,000,000
	Morgan Guaranty Trust Co.	Santa Magdalena	Feb. 4, 1963	7,000,000
	Bankers Trust Co.	Santa Mariana	June 14, 1963	6,800,000
	Manufacturers Hanover Trust Co.	Santa Maria	Sept. 23, 1963	6,800,000
Moore-McCormack Lines, Inc.	The Chase Manhattan Bank	Santa Mercedes	Apr. 7, 1964	6,720,000
Nautilus Petroleum Carriers Corp.	Irving Trust Co.	Argentina	May 13, 1960	10,000,000
Pacific Far East Line, Inc.	do	Brasil	Feb. 14, 1963	9,000,000
States Steamship Co.	Crocker-Citizens National Bank	Sister Katingo	Dec. 23, 1958	9,606,000
		China Bear	July 3, 1962	5,850,000
		Philippine Bear	Mar. 14, 1962	6,000,000
		M. M. Dant	Nov. 26, 1962	4,750,000
		C. E. Dant	Feb. 6, 1963	4,750,000
		California	Jan. 18, 1962	5,050,000
		Oregon	Apr. 19, 1962	5,050,000
		Hawaii	Aug. 16, 1962	5,050,000
		Washington	June 26, 1962	5,050,000
Tankers & Tramps Corp.	Irving Trust Co.	Atlas	Aug. 27, 1958	9,583,900
Gulf & South American Steamship Co., Inc.	Chemical Bank New York Trust Co.	Gulf Farmer	May 1, 1964	3,000,000
		Gulf Banker	June 26, 1964	3,000,000
		Gulf Trader	Sept. 23, 1964	3,000,000
		Gulf Shipper	Nov. 10, 1964	3,000,000
United States Lines Co.	The Chase Manhattan Bank	American Challenger	Dec. 27, 1963	3,750,000
		American Charger	do	3,750,000
		American Champion	do	3,750,000
		American Chieftain	do	3,750,000

¹ Coupon bonds which may be registered as to principal in the denominations of \$1,000 and/or registered bonds without coupons in the denominations of \$1,000 and integral multiples thereof.

² Commitment to insure mortgage on undelivered vessels.

SHIP MORTGAGE BONDS

Private bond or note issues outstanding—With trustees as of June 30, 1965

[Bonds and/or notes placed privately and not generally traded through brokers]

Mortgagor	Mortgagee/trustee	Vessel	Date of mortgage	Original principal amount	Identity of original holders
American Export Isbrandtsen Lines, Inc.	First National City Bank	Atlantic	Feb. 5, 1960	\$5,313,000	New York Life Insurance Co. First National City Bank.
American Mail Line, Ltd.	The Pacific National Bank of Seattle.	Washington Mail Philippine Mail Japan Mail	Jan. 2, 1962 July 1, 1963 do	4,000,000 4,500,000 4,500,000	State of Washington. Washington State Finance Commission. Employees Retirement System of the State of Washington.
American President Lines, Ltd.	Bank of American National Trust & Savings Association.	President Roosevelt	Mar. 31, 1962	3,400,000	State of Washington.
Black Ball Transport, Inc.	The Chase Manhattan Bank.	Coho	Dec. 22, 1959	2,683,900	Teachers' Insurance & Annuity Association of America.
Colonial Tankers Corp.	First National City Bank.	Western Hunter	Dec. 21, 1961	16,250,000	Metropolitan Life Insurance Co.
Containerships, Inc.	Morgan Guaranty Trust Co.	Floridian	Aug. 12, 1960	3,402,350	Morgan Guaranty Trust Co. of New York as trustee of various trusts. The Philadelphia Savings Fund Society. Morgan Guaranty Trust Co. as agent for an institutional account.
Farrell Lines, Inc.	First National City Bank	African Comet African Mercury African Meteor African Neptune African Sun	Aug. 22, 1962 Dec. 21, 1962 Oct. 31, 1962 Feb. 20, 1963 May 1, 1963	4,000,000 4,000,000 4,000,000 4,000,000 4,000,000	Notes: First National City Bank. Continental Illinois Bank & Trust Co. of Chicago. Bonds: First National City Bank. First National City Trust Co. Aetna Life Insurance Co. Connecticut General Life Insurance Co.
Mayflower Steamship Corp.	Morgan Guaranty Trust Co.	Mayflower	Jan. 9, 1961	11,500,000	Morgan Guaranty Trust Co. of New York as trustee of various pension trusts; Connecticut General Life Insurance Co. Aetna Life Insurance Co. Brooklyn Savings Bank The Ocean Accident & Guarantee Corp., Ltd. Columbia Casualty Co.

SHIP MORTGAGE BONDS

Private bond or note issues outstanding—With trustees as of June 30, 1965—Continued

[Bonds and/or notes placed privately and not generally traded through brokers]

Mortgagor	Mortgagee/trustee	Vessel	Date of mortgage	Original principal amount	Identity of original holders
Mount Vernon Tanker Co.....	Morgan Guaranty Trust Co.....	Mount Vernon Victory.	Jan. 27, 1961	11,858,900	The Chase Manhattan Bank. Morgan Guaranty Trust Co. as trustee for various pension trusts. Continental Assurance Co. Teachers Insurance & Annuity Association of America. State Mutual Life Assurance Co. of America. Fidelity Mutual Life Insurance Co. 43 savings banks. Penn Mutual Life Insurance Co. State Mutual Life Assurance Co. of America. John Hancock Mutual Life Insurance Co. Morgan Guaranty Trust Co. of New York as trustee for 6 trusts. The Penn Mutual Life Insurance Co. The Philadelphia Savings Fund Society. National Life Insurance Co. Continental Assurance Co. The First National Bank of Chicago as trustee of various trusts. Connecticut General Life Insurance Co. Provident Mutual Life Insurance Co. of Philadelphia. State Mutual Life Assurance Co. of Worcester. Connecticut Mutual Life Insurance Co. Home Life Insurance Co. The Life States Life Insurance Co. in the city of New York. New York Trust Co. as agent for the Act Institute of Chicago. The United States Trust Co. of New York as agent for Williams College. The Penn Mutual Life Insurance Co. Metropolitan Life Insurance Co. Crocker-Citizens National Bank. American Trust Co. Security First National Bank of Los Angeles. New York State Teachers Retirement System. Pension Trust (Trust No. 295,234).
Newport Tankers Corp.....	Savings Banks Trust Co.....	Achilles	June 7, 1960	10,792,900	
Penn Tanker Co.....	First National City Bank.....	Penn Challenger	Jan. 8, 1960	9,117,000	
Rye Marine Corp.....	Morgan Guaranty Trust Co.....	Thetis	Sept. 15, 1959	10,511,000	
Sea Transport Corp.....	Manufacturers Hanover Trust Co.	Eagle Voyager Eagle Traveler	Apr. 30, 1959 Mar. 26, 1959	10,500,000 10,500,000	
The Oceanic Steamship Co., Inc.....	Crocker-Citizens National Bank	Mariposa Monterey (Fleet mortgage)	Dec. 28, 1956 do	12,000,000	
Prudential Lines, Inc.....	National Commercial Bank & Trust Co.	MA Hull 177	Apr. 24, 1964 ¹	4,028,470	
Washington Tug & Barge Co.....	First National City Bank.....	MA Hull 178 Griffo	do ¹ Aug. 31, 1961	4,028,470 428,350	

¹ Commitment to insure mortgage on undelivered vessels.

SHIP MORTGAGE BONDS

Private note issues outstanding—No trustees as of June 30, 1965

Mortgagor	Mortgagee	Vessel	Date of mortgage	Original principal amount
Albatross Tanker Corp.	Penn Mutual Life Insurance Co.	Erna Elizabeth	Dec. 10, 1959	\$8,903,600
American Eagle Tanker Corp.	The Bowery Savings Bank	American Eagle	Mar. 17, 1959	8,623,000
American Trading & Production Corp.	The Guardian Life Insurance Co. of America	Maryland Trader	Sept. 10, 1958	2,612,266
Eagle Terminal Tankers, Inc.	do	Eagle Courier	Oct. 10, 1958	7,875,000
Isbrandtsen Tankers, Inc.	Pension Holding Corp.	Hans Isbrandtsen	Oct. 30, 1958	9,487,000
Mamhatten Tankers Co.	The Prudential Insurance Co. of America	Mamhattan	Jan. 13, 1957	20,925,000
Matson Navigation Co.	Crocker-Citizens National Bank	Matson	May 10, 1951	13,690,600
Monticello Tanker Co.	The Bowery Savings Bank	Monticello Victory	Oct. 19, 1961	11,698,800
Mount Washington Tanker Co.	do	Mount Washington	Oct. 20, 1962	12,313,450
National Transport Corp.	The Prudential Insurance Co. of America	Mount Washington	Oct. 31, 1963	12,313,450
Norfolk, Baltimore & Carolina Line, Inc.	Seaboard Citizens National Bank of Norfolk	National Defender	Oct. 23, 1959	16,488,000
	do	Maryland Clipper	Nov. 3, 1961	132,000
Ocean Transportation Co., Inc.	The Bowery Savings Bank	Ocean Ulla	Feb. 25, 1960	10,400,000
Sea Bees B-10, Inc.	Lafayette National Bank of Brooklyn	Costantino	Nov. 2, 1955	10,195,000
Tanker Four Lakes, Inc.	Pension Holding Corp.	Four Lakes	Mar. 11, 1959	2,250,000
The Cabins Tanker, Inc.	do	The Cabins	Sept. 28, 1959	2,250,000
Transeastern Shipping Corp.	The Bowery Savings Bank	Transeastern	July 30, 1959	11,825,000
Eagle Terminal Tankers, Inc.	Pension Holding Corp.	Eagle Transporter	Nov. 14, 1958	7,875,000

Senator BARTLETT. To your knowledge, has any financing under title XI been contemplated in the next few months?

Mr. DAVIS. Yes, sir; there is, Senator. We have a fleet of four ships coming up within the next 2 months with the American President Lines. We have another group coming up approximately 2 or 3 months later for Delta, and also a group for Grace Lines for ships being built now. There are a number coming up.

Senator BARTLETT. In your opinion, the financing will be difficult under the existing situation?

Mr. DAVIS. In our opinion, it will, Mr. Chairman.

Senator BARTLETT. What is the prevailing interest rate?

Mr. DAVIS. I believe 4.4 percent.

Senator BARTLETT. What is the maximum life of the bonds, or is there any limit?

Mr. DAVIS. They are 20 and 25 years from the execution of the mortgages. There are more at 20 than at 25.

Senator BARTLETT. When did APL bonds go on the market?

Mr. DAVIS. They haven't decided firmly, Mr. Chairman. They hope to go on the market next month.

Senator BARTLETT. What would be the aggregate amount of dollars in the bonds for the four ships?

Mr. DAVIS. \$20 to \$25 million.

Senator BARTLETT. Customarily, under title XI, is financing readily available?

Mr. DAVIS. Yes, sir.

Senator BARTLETT. Going back to the point raised by Mr. Foster, looking not to the past about this but to the future, it is my understanding from what you said that even if you did give this blanket approval, you are not so sure that the market will respond as you desire it to?

Mr. DAVIS. In fact, we are quite concerned about it, plus the other important element of investors' counsels who have to furnish their clients with opinions. They have to be firm in their opinions. All required approvals must have been given.

Senator BARTLETT. If the Department decides to confer this blanket approval, it would be, of course, after determination that this is legally correct?

Mr. DAVIS. That is the problem we are currently studying.

Senator BARTLETT. Let's say that you decided affirmatively; that you decided that this approval can be given, you are still not sure that other lawyers would accept your judgment?

Mr. DAVIS. That is true.

Senator BARTLETT. Mr. Kenney?

Mr. KENNEY. Do I understand that the court case only affects the validity of the rights with respect to the bonds which are foreign held?

Mr. DAVIS. That is not clear, and I don't believe that inference could be drawn. I think it affects the validity with respect to priority of all bonds. Of course, there was only one involved in the *Westhampton* case.

Mr. KENNEY. I am talking about the full weight of this decision taken to its full purpose. In other words, it is not solely with respect to other interests in quotas, as they define it?

Mr. DAVIS. That is right.

Mr. KENNEY. Do these bonds now have a prior claim? Are these mortgages a first preferred? Do they have better standing than other claims against the vessel?

Mr. DAVIS. Let me explain it this way: At the time a preferred ship mortgage goes on a vessel, all—

Mr. KENNEY. When you say "preferred ship mortgage," you mean a mortgage under title XI?

Mr. DAVIS. I am talking about preferred ship mortgage under the Ship Mortgage Act, 1920. All liens that are against that vessel at that time have priority over the preferred ship mortgage. The Ship Mortgage Act, itself, has certain exceptions provided for in there with respect to later priorities. For example, tort claims, wages, salvage—those will continue to have priority over the mortgage.

Mr. KENNEY. And this bill would not affect those priorities?

Mr. DAVIS. It would not. Then going to the question of subsequently created contract liens, they would all be behind the preferred ship mortgage.

Senator BARTLETT. But wages would be ahead of that mortgage?

Mr. DAVIS. Wages as provided for in the Ship Mortgage Act, itself.

Mr. KENNEY. And other seamen claims?

Mr. DAVIS. Other seamen's claims, tort claims; yes, sir.

Senator BARTLETT. Thank you very much.

Mr. DAVIS. Thank you, Mr. Chairman.

Senator BARTLETT. Mr. Kominers, please.

We are glad to have you gentlemen.

Mr. KOMINERS. Thank you, Mr. Chairman.

STATEMENT OF ODELL KOMINERS, KOMINERS & FORT, WASHINGTON, D.C.; ACCOMPANIED BY ARTHUR SCHULTE, LEHMAN BROS., NEW YORK, N.Y.; AND GEORGE H. SCHREINER, VICE PRESIDENT, AMERICAN PRESIDENT LINES, LTD., SAN FRANCISCO, CALIF.

Mr. KOMINERS. Mr. Chairman, I am accompanied by Mr. Arthur Schulte, of Lehman Bros., and by Mr. George Schreiner, of American President Lines, Ltd.

My name is Odell Kominers. I am a partner in the law firm of Kominers & Fort, with offices in the Tower Building, Washington, D.C. I appear today as counsel for the Committee of American Steamship Lines in support of S. 2118.

CASL is an association of 14 American-flag steamship lines which maintain essential common carrier steamship services in foreign commerce under operating-differential subsidy agreements with the United States. These companies have issued, under trust indentures, title XI government-insured bonds aggregating \$241,989,940. Title XI of the Merchant Marine Act, 1936, was enacted, and amended from time to time, solely to encourage the private financing of the vessel replacement programs of American-flag shipowners.

Public issues of bonds secured by mortgages insured under title XI are the principal and least costly method of financing available to the shipowners to carry out their replacement obligations. Two of the CASL lines are now negotiating and must conclude in the very near future, additional title XI bond financing in the aggregate amount of about \$50 million.

This vessel replacement program has been seriously jeopardized, not only because questions have been raised regarding the validity of some title XI bonds already sold, but more importantly because the marketability of future title XI bond issues is impaired, as the result of a recent decision of the U.S. Court of Appeals for the Fourth Circuit in the case of *Chemical Bank New York Trust Company v. The Steamship Westhampton* (Nos. 9637 and 9638, decided April 5, 1965).

S. 2118 would overcome the implications of the *Westhampton* decision by amending sections 9 and 37 of the Shipping Act, 1916, and subsection O(d) of the Ship Mortgage Act, 1920. Enactment of this general legislation, will correct the situation for bonds issued in connection with the financing of American-flag vessels, whether or not insured under title XI. However, we have been assured that it is not intended by this bill to affect litigation now pending, whether involving the *Westhampton* or other ships, and CASL has no desire to seek to affect the outcome of pending litigation by legislation.

The mortgage and bond involved in the *Westhampton* case were not insured by the United States pursuant to the provisions of title XI. However, the *Westhampton* decision of the Court of Appeals for the Fourth Circuit has created uncertainty regarding title XI insured mortgage bonds due to the broad implications and immediate impact of the court's holding that a ship mortgage bond is considered "an interest" in the vessel, with the result that the issuance, sale, or transfer of such bonds to a person not a citizen of the United States as defined in section 2 of the Shipping Act, 1916, was held to render the mortgage invalid since it did not have the prior approval of the Maritime Administrator.

Hence, the mortgage lost its preferred status. This seriously affects the security of the bondholders. In addition, sections 9 and 37 of the Shipping Act, 1916, contain penal provisions for violations of the sale and transfer restrictions, and also provide for forfeiture under certain circumstances of the vessel involved. Obviously, if the court's decision is interpreted to require procedure under such penal or forfeiture provisions, serious and unnecessary injury would be inflicted upon persons who acted in complete good faith.

This *Westhampton* holding assumes greater importance because the financial community requires certainty as to the preferred status of the mortgage and the validity of bonds secured by such mortgages. A noncitizen within the meaning of section 2 of the Shipping Act, 1916, is quite different from a "foreigner" in the usual sense. Section 2 defines citizenship only in terms of "corporation, partnership, or association." There are no express statutory criteria for determining the citizenship of organizations such as pension funds, mutual insurance companies, certain savings banks, States of the United States, or agencies of such States. In the past such organizations have been major purchasers of title XI insured ship mortgage bonds. Indeed one CASL company has outstanding a title XI insured ship mortgage bond issued under a trust indenture to the largest American life insurance company which, at the time the bond was issued, was not technically a "citizen of the United States" because it had two Canadians on its board of directors. The statute at that time required that all directors be citizens. The statute was amended in 1959 to permit

noncitizens to be directors providing they did not aggregate more than a minority of the number of directors necessary to constitute a quorum.

The Court of Appeals for the Fourth Circuit has granted a motion of the Committee of American Steamship Lines to appear as *amicus curiae* in support of a petition for reconsideration of its decision filed by the Chemical Bank, and has ordered the other parties to the case to file briefs in response to the petition for reconsideration. It is possible that the court may revise or even restrict its decision so as plainly to be inapplicable to title XI insured mortgages and bonds.

The Maritime Administration may also grant some form of clarifying approval to future title XI insured bond issues. However, neither of these possibilities can completely resolve the problems raised because (1) two of our lines must make immediate decisions and arrange firm commitments for their vessel financing, (2) further delay of some 12 to 18 months may result if the original decision of the court of appeals or its decision on reconsideration is taken by certiorari to the Supreme Court, and (3) favorable action on reconsideration by the court of appeals, or some general approval given by the Maritime Administration, cannot guarantee that this issue will not arise again in some other circuit. This is particularly true with respect to bond issues heretofore insured and now outstanding.

S. 2118 is retroactive and will apply to bonds issued and outstanding prior to the decision. This is necessary to protect such bonds from possible attack, and is required in the interest of the Government, the bondholders, and the shipowners. I believe the statute, as amended by S. 2118, will conform with the clear intent of Congress in the enactment of title XI. A brief review of the legislative history of title XI will emphasize the congressional intent. The history of this legislation demonstrates clearly that Congress intended title XI bonds to be fully negotiable and that they reach the broadest market possible. The decision in the *Westhampton* case, if held applicable to title XI bonds, may destroy the negotiability of the bonds.

1. When the large-scale replacement program commenced in 1953, Congress enacted Public Law 288 (83d Cong., 1st sess.), making major changes in title XI. As stated in this committee's report to the Senate (S. Rept. 821), these changes were necessary because—

Title XI in its present form has not proved effective in attracting private capital. This bill is intended to remove some of the shortcomings of the existing mortgage insurance provisions of the act in an effort to accomplish its original purpose—to encourage the use of private funds. * * *

2. Public Law 781 (83d Cong., 2d sess.) was enacted in September 1954. As stated in the committee's report (S. Rept. 1804):

This bill is the result of the committee's effort to overcome the shortcomings revealed by experience in Public Law 288.

3. It developed that there were still shortcomings in the law insofar as the financial community was concerned. To overcome the problem, Public Law 613 (84th Cong., 2d sess.) was enacted in June 1956, to provide that "The faith of the United States is solemnly pledged to the payment of interest on" and 90 percent of the unpaid balance of mortgages generally and 100 percent of the unpaid balance of mortgages on special purpose vessels.

4. One of the most significant amendments was Public Law 1017 (84th Cong., 2d sess.), enacted in August 1956, extending the insurance from 90 percent to 100 percent on all vessels because of the reluctance of potential investors to assume the uninsured 10 percent risk.

5. In July 1958 it became apparent that receipts from mortgage insurance premiums were insufficient to build up the Federal ship mortgage fund to the point where the solemn pledge of the faith of the United States could be complied with in the event of default. This was impeding the program. Public Law 85-520 was thereupon enacted, granting authority to the Secretary of Commerce to borrow funds from the Treasury if sufficient funds were not otherwise available to honor insurance obligations.

6. Public Law 86-123, enacted in July 1959, further broadened the title XI program by permitting the insuring of mortgages on existing new vessels to finance the future construction of additional new vessels.

7. In July 1959 Public Law 86-127 was also passed. The amendment provided for the creation of escrow funds to be held by the Treasury Department. This permitted full title XI insurance for the financing of ships under construction. Prior to this amendment Government insurance under title XI as to ships under construction was limited to the amounts actually paid to the shipyards. Companies which desired to issue bonds while the ship was still under construction experienced difficulty in marketing the bonds at the most favorable interest rates because of incomplete insurance.

The foregoing amendments demonstrate the continuing desire and intent of Congress to improve the program for financing new ship construction by meeting the practical problems which arose in the administration of title XI. The principal purpose of the amendments was to broaden and strengthen the market for title XI insured bonds, and hence obtain the most flexible form of private financing at the lowest rate.

The Maritime Administration recognized this congressional purpose. It repeatedly approved bond issues under trust indentures without requiring sections 9 or 37 approval for each individual issuance, sale, or transfer of a bond, so long as the trustee was a citizen of the United States and the terms of the mortgage and trust indenture were approved by the Administration. The trustees were closely scrutinized, not only as to citizenship but also as to financial integrity and ability to service the mortgages and trust indentures, pursuant to which title XI insured bonds are issued, the Government retains the very highest degree of control over such vessels. In particular, a trustee-mortgagee cannot, in the first instance, foreclose the mortgage; instead, it must demand payment of the mortgage insurance from the Government and assign the mortgage directly to the United States. This procedure was reported to Congress from time to time. In my opinion neither Congress nor the Maritime Administration intended or foresaw the implications of the *Westhampton* case on title XI insured bonds.

During the time that Mr. Davis was testifying, I had an opportunity to review the amendments he suggested in the draft bill. After conferring with my colleagues, I am prepared to state that these

amendments are acceptable to the CASL companies. They are helpful in perfecting the language to the existing statute.

Thank you for the opportunity to appear before your committee today.

Mr. Schulte and Mr. Schreiner each have a short prepared statement. It is entirely up to you gentlemen whether you wish them now or if you wish to question, if you have any questions.

Senator BARTLETT. I think we will question you first.

Mr. FOSTER. I don't have any questions.

Senator BARTLETT. Mr. Kenney?

Mr. KENNEY. I don't believe I do, either, sir.

Senator BARTLETT. Without this legislation, do you believe these ships proposed to be built by the CASL members could be constructed. Would the financing be available?

Mr. KOMINERS. I do not believe the financing could be obtained and, and in any event, I do not believe that it could be obtained at as attractive a rate of interest as will be obtainable in the event the legislation is enacted.

Senator BARTLETT. That was going to be my next question. What do you think the spread might be? I know this is speculative, highly.

Mr. KOMINERS. I would speculate, but I think either Mr. Schulte or Mr. Schreiner could better answer that question because they are the gentlemen for American President Lines who will actually be on the firing line. My guess is it would cost at least a half a point, half a percentage point, and not half of what the mortgage bankers call a point.

Senator BARTLETT. Is there dissent from that conclusion?

Mr. SCHREINER. No.

Mr. SCHULTE. No.

Senator BARTLETT. Explain for my education, if you will, just what "preferred status" means in the sense you used it on page 2 when you said "Hence, the mortgage lost its preferred status."

Mr. KOMINERS. A preferred mortgage under the Ship Mortgage Act is preferred only as against certain types of later accruing liens. The statute, as Mr. Davis very properly stated, clearly specifies certain types of subsequently accruing claims, which come ahead of a valid preferred mortgage. The preferred mortgage, however, with those exceptions, is similar to a first mortgage on real estate in that it is a prior claim as against subsequently or recorded claims. The claims which are not defeated are those for wages, repairs, tort claims, and a few others which I do not have at the tip of my tongue.

Senator BARTLETT. Now, you mentioned the possibility that the Maritime Administration might grant the blanket approval to which Mr. Davis alluded. What if that blanket approval were granted tomorrow, would the CASL members, in your opinion, be able to proceed then?

Mr. KOMINERS. They could proceed, but I nevertheless believe it would cost them something in the interest rate, perhaps appreciable amounts.

The reason I say that, Senator, is this: My own experience in the early practice of the law was as a real estate lawyer, and I ran into the natural inclination of attorneys to turn titles down when there is any

possible doubt. That is the easiest thing to do. And the safest thing from the standpoint of a prospective purchaser. When in doubt, be safe and say it is not good. Demand something more to protect your claim.

Senator BARTLETT. Plenty of bonds on the market, in other words, concerning which there is no doubt whatsoever.

Mr. KOMINERS. I would say that for the future the attorneys representing the lenders might very well take the position that they question the authority of the Maritime Administration to give a blanket approval for 25 years. I personally agree with Mr. Davis, that the Administration has the authority to grant such approval. That does not mean that all other lawyers representing financing institutions would agree with either or both of us.

Senator BARTLETT. You wouldn't be putting up the \$50 million.

Mr. KOMINERS. That is right. I would be representing the company which would not particularly care, apart from the additional charge to it, whether the opposing counsel guessed right or wrong. But opposing counsel in an effort to be safe might insist upon something more than a blanket approval.

Additionally, unless you get a blanket approval for the life of the bonds or the trust indenture, you would be required to come back repeatedly for approvals, which in turn would impair the negotiability of the bonds.

Senator BARTLETT. Thank you very much.

Are you ready, sir?

Mr. SCHULTE. Mr. Chairman, my name is Arthur D. Schulte. I am a partner of Lehman Bros., New York investment bankers. Our firm has been a leading manager of title XI bond financing for the subsidized steamship industry since 1958, when public offerings of such bonds first became practicable.

On previous occasions, I have had the privilege of testifying before Senate and House committees regarding certain amendments to title XI which have since been incorporated into the Merchant Marine Act. The purpose of the prior amendments was to provide the Federal Government and the American-flag shipping industry with the most effective and least expensive means for financing this country's massive vessel-replacement program.

As I recall the legislative history of title XI, some of the amendments were enabling amendments, while others represented straight-forward clarification of congressional intent so that even the man-in-street investor could understand the Federal Government's full commitment to the title XI insurance program.

Prior to these amendments, merchant marine bonds insured under title XI could be sold only to a very limited group of sophisticated investors, consisting usually of savings banks and insurance companies, and the bonds had to carry a very high rate of interest. This interest rate, which was usually at least 5 percent, dropped to as low as 4.20 percent when it was possible to convince a broader segment of the investing public that the principal and interest of title XI bonds were unconditionally insured by the U.S. Government, and that there could be absolutely no question that accrued interest as well as the principal amount of the bonds would be paid when due.

We believe that if some new doubt arises as to the Federal Government's full commitment to such payments, the public market for title XI bonds will again become restricted. In that case, the low interest rates available in public financing may no longer be available thereby unduly burdening the issuers and imposing an unnecessarily high contingent liability upon the Federal Government.

In our opinion, S. 2118 represents the clarification type of amendment. We fully support the prompt passage of this bill so that there can be no possible confusion in the mind of any investor concerning the title XI program. We understand that a recent Federal court decision in the case of *Chemical Bank v. The Steamship Westhampton* is now creating confusion which, if allowed to persist, will, in our opinion, hinder the efficient marketing of title XI bonds at the relatively low interest rates that have been achieved to date. Such a condition would result in the sale of our Government's credit at unnecessarily high costs.

S. 2118 dispenses with all approvals of bondholders of the type required in the *Westhampton* case where the trustee is a citizen of the United States. In title XI cases with which we are familiar, the Secretary of Commerce not only approves the trustee and enters into an insurance contract with him, but he also effectively restricts the power of the trustee—and through him the bondholders—to foreclose upon the vessel or obtain any effective interest therein.

It appears to us that, when the trustee is a U.S. citizen there is no need to restrict any legalistic interest which a bondholder may have in a vessel—under the *Westhampton* case. Of course, the Shipping Act, even after this amendment, would still effectively prohibit any actual transfer of the vessel from the trustee to a noncitizen without the Secretary's further approval.

Even though my partners and I firmly believe that the confusion created by the *Westhampton* case is unwarranted as it relates to title XI financings, that confusion must be dissipated. To assure the successful continuation of the vessel replacement program and the most efficient financing thereof, I would commend to you the prompt passage of S. 2118.

Thank you.

Senator BARTLETT. Mr. Schulte, would you discuss a situation such as this with your partners? How many do you talk with?

Mr. SCHULTE. Possibly half a dozen.

Senator BARTLETT. How many partners are there?

Mr. SCHULTE. I have 28 partners, Senator.

Senator BARTLETT. That is kind of extraneous, but I was curious.

Why, in your judgment, were these bonds so unattractive before title XI came into being and was perfected, or relatively so?

Mr. SCHULTE. Because there was question in the minds of the investing public as to the Government's full faith and credit, whether or not the Maritime Administration would have the money to pay off in case of a default. That was remedied by having the bill passed which gave the Secretary of Commerce recourse to the Secretary of the Treasury. We felt that to make this bond a readily salable instrument, if I may use a simple homey expression, we had to make the investor, potential investor, realize that in case of a default of any sort, he would be paid off just like cash on the barrelhead basis. And

when we got that idea across, and it was difficult to get it across, then we were able to expand the market for these bonds, and instead of selling these bonds almost on a mortgage basis, with high interest rates that mortgages produce, just as savings banks and some of the major life insurance companies, we found we were able to bring in small State funds, pension funds, college funds, church funds. We haven't yet reached the point, and I hope one day we will, that we will be able to have individual investors buy \$1,000 or \$2,000 worth or of bonds, but we have broadened the market tremendously during the last 5 or 6 years as a result of the amendments which Mr. Kominers mentioned.

Senator BARTLETT. Why has it not yet been possible to go to the small bondholder?

Mr. SCHULTE. It is purely a matter of education, and I think that we are getting that.

Mr. KENNEY. You don't want to issue them at 25 face value?

Mr. SCHULTE. That might be difficult.

Mr. KENNEY. I am intrigued to learn that you can buy a 100 percent guaranteed bond at 4.20 interest rate, instead of a savings bond that only pays 3.75.

Mr. SCHULTE. That is right. I think, if I remember correctly, that the last issue that was placed prior to the amendments which have just been described were placed at a little over 5 percent. Then the first issue publicly in a matter which I have described came out at 4.20 percent.

The last one which my firm managed was one at $4\frac{3}{8}$ percent. Now, I don't know what the next one will be, but I do believe, if there is again a question in the minds of the investing public on these bonds, the interest rates will soar.

I would like to say also, if I may, to paraphrase what you said before, the trustees will feel—pension funds and State funds will feel—that there are too many bonds on the market, about which they can be sure to run any risk, and I think also that it is very important that this legislation be passed because of the very fact that it is being considered, if not passed, might lead people to believe that the Senate and the House support the position of the court of appeals in the *Westhampton* case. I think that must be dispelled.

Senator BARTLETT. What if Mr. Kenney were to write over to Lehman Bros., and say, "I understand Lehman Bros. is going to have something to do with issuance of some bonds for APL, and I would like \$10,000 worth of the bonds"? You don't deal with the \$10,000 man yet, but hopefully someday; is that it?

Mr. SCHULTE. Oh, yes, we would be very glad to sell them.

Senator BARTLETT. You will probably get the letter tonight. [Laughter.]

Mr. SCHULTE. I will even be glad to raise a smaller denomination.

Mr. KENNEY. I would need that.

Senator BARTLETT. He was talking about \$25.

In your opinion, Mr. Schulte, what if Government were to withdraw entirely from this field, there would be no Government guarantees and no Government insurance, no Government assistance of any kind, would these bonds be salable?

Mr. SCHULTE. No. Categorically, no.

Senator BARTLETT. Why?

Mr. SCHULTE. Because a vessel is a very special purpose object and if the bonds were in default, and the vessels had to be foreclosed, it would be very hard to find a market for them.

Senator BARTLETT. Mr. Foster?

Mr. FOSTER. No questions.

Senator BARTLETT. Mr. Kenney?

Mr. KENNEY. One other thing, Mr. Schulte: On page 2 of your statement you indicate that failure to enact the bill may restrict the market for title XI bonds and may impose an unnecessarily high contingent liability upon the Federal Government. I don't understand how this would affect the contingent liability of the Government, which is 100 percent.

Mr. SCHULTE. Because the Government guarantees the interest as well as the principal on these bonds, and if the bonds have to be sold at a 6-percent interest instead of 4——

Mr. KENNEY. I see. Thank you.

Senator BARTLETT. If this news ever gets out, I don't think there will be any trouble selling the bonds.

Thank you very much.

Mr. SCHULTE. Thank you.

Senator BARTLETT. Mr. Schreiner.

Mr. SCHREINER. Mr. Chairman and members of the committee, my name is George H. Schreiner. I am vice president and treasurer of American President Lines, Ltd., 601 California Street, San Francisco, Calif. I appear here on behalf of the Committee of American Steamship Lines which represents 14 American-flag steamship companies who have operating-differential subsidy agreements with the United States. I am here to recommend passage of S. 2118, and in particular, to urge prompt passage. Legislation seems the only timely and complete remedy available in the situation created by the decision of the Fourth Circuit Court of Appeals in the *Westhampton* case.

American President Lines, Ltd. finds itself first among CASL companies, since the *Westhampton* decision, who wish to enter the marketplace with a new issue of merchant marine bonds. On December 31, 1964, American President Lines, Ltd., contracted with Ingalls Shipbuilding Corp. at Pascagoula, Miss., and the Maritime Administration for the construction of four modern freighters. Construction is now in progress. We will require proceeds of the bond issue to meet commitments under the construction contract. Up to 75 percent of our cost for each vessel may be paid from bond proceeds, but we must provide the remaining 25 percent from other funds on hand. Half of the 25 percent payable from other funds on hand must first have been expended before any bond proceeds can be used. Based on shipyard estimates, I believe that bond proceeds can first be used in November 1965.

Under the contemplated financing arrangements, the merchant marine bonds will be offered to the public. When the bonds are issued, the proceeds will be deposited in escrow for disbursement by the Secretary of Commerce when authorized for progress payments to the shipyard. The bonds are secured by the unexpended amount in escrow and a Government insured chattel mortgage on the ship under construction. The chattel mortgage is supplanted by a Government insured first preferred ship mortgage on delivery of the completed ships.

Our investment bankers advise that the public offering should be made as soon as possible. When this recommendation was first made to us in March 1965, we immediately began to prepare the necessary documents for approval by the Maritime Administration. The *Westhampton* decision of April 5 caused us to delay a bit but the papers were delivered to the Maritime Administration in early May. American President Lines, Ltd., is anxious to proceed with an offering to the public, but of course it is unwise to seek commitments from lenders without the necessary approval of the Maritime Administration assuring title XI insurance coverage.

Amid uncertainty as to the broad legal implications of the *Westhampton* decision, time passes while the need to sell bonds becomes more urgent. Quite justifiably, in the unsettled circumstances resulting from the court decision, the Maritime Administration must deliberate before proceeding with the necessary approvals which will enable us to offer the bonds to the public.

Amid uncertainty, I am reluctant to approach the marketplace, yet my company soon will need funds. Prompt passage of S. 2118 seems the only timely way to dispel uncertainty. Other CASL companies desire to issue merchant marine bonds also, one before December 1965, to finance ship construction under their mandatory replacement programs. They have found merchant marine bonds the only means of raising private capital for such purposes at reasonable interest rates. The interest rates are acceptable to lenders principally because of the characteristics of the bonds and the security offered. In the opinion of the CASL companies, continuation of the present uncertainty will jeopardize the market acceptance of future issues at reasonable interest rates.

American President Lines, Ltd., is also confronted with another problem because of the *Westhampton* decision. Once again, it will be first among the CASL companies required, since the *Westhampton* decision, to deliver a first preferred ship mortgage as security for merchant marine bonds now outstanding. The bonds were issued on August 27, 1963, and at present they are secured by bond proceeds in escrow and chattel mortgages on three ships now under construction by National Steel & Shipbuilding Co. at San Diego, Calif. When each ship is delivered by the yard, we must deliver a first preferred ship mortgage to the trustee for the bondholders in substitution for the security of the chattel mortgage on the ship. It is currently estimated by the shipbuilder that the first of the ships will be delivered on October 11, 1965. On that date the validity of the first preferred ship mortgage which we propose to deliver may be questioned unless prior action is taken to dispel the uncertainty.

In summary, CASL companies who issue merchant marine bonds will encounter situations similar to those which confront American President Lines, Ltd. My company faces a need to issue new merchant marine bonds within a relatively short span of time and before November 1965. Also, on October 11, 1965, or whenever the first ship is delivered, my company must deliver a valid first preferred ship mortgage to the trustee for bondholders under an already outstanding issue of merchant marine bonds. The cloud raised by the *Westhampton* decision cannot be dissipated completely before those dates except by legislation such as S. 2118.

On behalf of the Committee of American Steamship Lines, I appreciate the opportunity to be heard on this urgently needed legislation.

Senator BARTLETT. Thank you. Mr. Foster?

Mr. FOSTER. No questions.

Senator BARTLETT. Mr. Kenney?

Mr. KENNEY. Can you give us a quick indication of what it really means to APL in terms of dollars, for instance, if we don't act on this bill? Is there a convenient measure of what you think it is going to cost you?

Mr. SCHREINER. Yes, sir. We expect, it is our program, to borrow about \$5 million per ship. There are four ships currently under the contract. As a matter of fact, we have an option to add a fifth ship to that contract, so it is between \$20 and \$25 million that we are talking about at this time.

Mr. KENNEY. It isn't that the failure of the passage of the bill won't cost you \$20 or \$25 million?

Mr. SCHREINER. It won't cost you that.

Mr. KENNEY. It affects your financing?

Mr. SCHREINER. It affects us as far as I understand it, from counsel I have had, it affects seriously our ability to obtain that kind of money in the market.

Mr. KENNEY. Thank you.

Senator BARTLETT. The yard might not deliver the ships?

Mr. SCHREINER. That gets into issues—

Senator BARTLETT. Question stricken.

Thank you. Thank you, gentlemen.

Mr. Davis, will you return for a minute?

I think the record ought to contain some information as to the experience of the Government, its financial experience under title XI. Has the Government lost money, has the Government made money, what are the facts?

If you don't have all the answers readily available, you may submit it in writing.

Mr. DAVIS. I think it would be best if we submitted a statement to that, Senator, and we will be happy to do so.

Senator BARTLETT. Fine. Thank you.

(The statement follows:)

STATEMENT OF MARITIME ADMINISTRATION'S EXPERIENCE UNDER TITLE II,
MERCHANT MARINE ACT, 1936, AS AMENDED

The history of the Maritime Administration's Federal ship mortgage insurance program (title XI) shows a sustained congressional intent to implement the provisions of title XI, first enacted in 1938, so as to provide Government insurance to a degree necessary to assure private financing of the construction, reconstruction, or reconditioning of U.S. flag merchant vessels. This congressional intent is evidenced by a succession of liberalizing amendments to title II, culminating in 100-percent insurance of the unpaid mortgage principal, and interest, payable in cash upon the occurrence of specified defaults in the shipowners' mortgage obligations and the assignment of the mortgage by the mortgagee to the United States. Until the 100-percent insurance provision was incorporated in title XI, the program failed to attract private capital to the ship mortgage field as only two insurance contracts, aggregating approximately \$2,400,000, were approved. Under the impetus of the 100-percent insurance in 1956 and the subsequent amendments to title XI which stimulated the sale of title XI insured bonds to the public, the program has grown to a total of 96 ships, representing ship con-

struction costs in excess of \$1 billion, and title XI insured obligations of almost \$600 million for the following:

	Total ships
Cargo ships -----	44
Tankers -----	31
Passenger ships -----	10
Miscellaneous -----	11
Total -----	96
Less:	
Mortgage defaults -----	16
Voluntary insurance terminations -----	11
Total -----	27
Total as of June 30, 1965 -----	79

¹ The 6 defaults referred to above are as follows:

The mortgage on the tanker *Gold Stream* of Red Hills Corp., was foreclosed and \$3,410,495.37 was paid to the mortgagee. This ship was sold to the Penntans Co. for \$2,112,000.

The mortgage on the *Carib Queen* of TMT Traller Ferry, Inc., was foreclosed and the Government paid \$4,087,292 to the mortgagee. This ship, renamed the USNS *Taurus*, is on loan to the Navy Department, without charge, and is being operated by the MSTs as a roll-on, roll-off ship for military vehicles, filling a vital role for defense purposes.

The mortgage on the freighter *Coast Progress* of Coastwise Line was foreclosed, involving total obligations to the title XI fund of approximately \$1,200,000. This ship was sold for \$751,500 to Matson Navigation Co.

The mortgage on the tanker *Titan* of Overseas Oil Transport Corp., was foreclosed and \$11,945,282 was paid the mortgagee. The ship was sold to Globe Seaways, Inc., for \$8,325,000.

Upon assignment of the mortgage on the roll-on, roll-off vessel MV *New Yorker* of Containerships, Inc., \$3,253,086.85 was paid to the mortgagee. Foreclosure has been averted by successive charters, extending until 1975, which provide revenues more than sufficient for mortgage debt service.

The mortgage on the passenger ship *Leitani* of Hawaiian-Textron, Inc., was foreclosed involving total obligations to the title XI fund of approximately \$5 million. This ship has been sold to American President Lines for \$3,200,000, renamed the SS *President Roosevelt*, and after undergoing extensive reconversion work, is now an addition to the American transpacific passenger service, financed once again under title XI.

Additional defaults were averted by temporary financial assistance in the form of advances and deferments of principal payments, shown on exhibits A and B, respectively.

The outstanding obligations for the 79 ships currently under title XI approximate \$425 million. In addition applications are pending for title XI insurance on 31 ships with an estimated total cost, excluding construction-differential subsidy, of \$132,283,900 with potential insured mortgages of \$99,213,500.

With the Government's prompt fulfillment of the pledge "of the faith of the United States to the payment of interest on and the unpaid balance of the principal amount" (sec. 1103(e) of the Merchant Marine Act, 1936, as amended) in the six mortgage defaults referred to above, title XI, insured obligations have attained a very high degree of acceptability in the financial community and with the investing public. As the program has grown in favor, the title XI insured obligations have come to be considered almost comparable in security to U.S. Government bonds and the interest rates are only slightly in excess of Government bonds of like maturities.

In addition, the title XI program has obviated the need for direct Government financing which would involve the appropriation of hundreds of millions of dollars; it has lent essential support to the large ship replacement program made necessary by the overage factor in the American merchant marine and the need for efficient ships to serve the commercial and national defense needs of the United States; it has created and encouraged a greater interest in the American merchant marine; and by producing lower interest rates for ship mortgage obligations it has lowered the cost of ownership and operation of vessels under U.S. flag, minimizing the Government's liability for title XI insurance and improving the general economy of the United States.

The Federal ship mortgage insurance revolving fund, from which title XI mortgage insurance obligations are paid, has an annual gross income of approximately \$3 million from investigation fees and insurance premiums. The fund has a retained income or net worth of approximately \$10 million (derived solely

from activities under the program, none from appropriated money), and is considered solvent for the foreseeable future, absent substantial defaults on tanker mortgages. The continuing depression in the tanker segment of the industry, aggravated by the completion of the colonial pipeline last winter, is the major source of concern in the title XI program.

EXHIBIT A

Advances of principal payments

Company	Date	Amount	Amount repaid
American Eagle Tanker Corp.....	{ June 24, 1960	\$107,787.50	(1)
	{ Sept. 24, 1960	107,787.50	
National Transport Corp.....	June 1, 1960	206,100.00	All
Nautilus Petroleum Carriers Corp.....	{ June 23, 1960	101,603.00	All
	{ Sept. 23, 1960	120,075.00	All
Red Hills Corp. ²	{ Dec. 24, 1959	65,165.00	-----
	{ June 24, 1960	65,165.00	-----
Transeastern Shipping Corp.....	{ Dec. 24, 1960	89,720.67	All
	{ Sept. 24, 1960	90,842.18	All
	{ Dec. 24, 1960	91,977.71	All
Containerships, Inc.....	Jan. 1, 1961	84,866.88	-----
Tankers & Tramps Corp.....	Aug. 9, 1963	266,000.00	-----
Total.....		1,397,090.44	-----
Outstanding June 25, 1965.....		696,771.88	-----

¹ An amount equal to the 2 advances is held in the restricted fund as collateral. Can be withdrawn on Maritime's request or with Maritime's approval.

² Termination due to default.

EXHIBIT B

Deferrals of principal payments

Company	Period of deferral	Total deferred	Payment resumption date
American Eagle Tanker Corp.....	Mar. 24, 1961, to Dec. 24, 1962.....	\$862,300.00	Mar. 24, 1963
National Transport Corp.....	Sept. 1, 1960, to June 1, 1962.....	1,648,800.00	Sept. 1, 1962
Nautilus Petroleum Carriers Corp.....	{ June 23, 1960, to Sept. 23, 1959.....	240,150.00	Apr. 1, 1963
	{ Dec. 23, 1960, to Mar. 23, 1963.....	1,200,750.00	Do
Overseas Oil Transport Corp. ¹	June 24, 1961, to Mar. 24, 1962.....	1,236,930.00	June 24, 1963
Petrol Shipping Corp. ²	June 24, 1960, to Mar. 24, 1962.....	843,815.04	July 1, 1962
	{ Mar. 24, 1959, to June 24, 1959.....	130,330.00	Mar. 24, 1963
Red Hills Corp. ¹	{ Mar. 24, 1960, to Dec. 24, 1961.....	521,320.00	-----
	{ Sept. 24, 1962, to Dec. 24, 1962.....	154,152.70	-----
Tankers & Tramps Corp.....	June 24, 1960, to Mar. 24, 1962.....	959,390.00	July 1, 1962
	{ Jan. 1, 1964 (1 semiannual).....	266,000.00	July 1, 1964
Transeastern Shipping Corp.....	Mar. 24, 1961, to Dec. 24, 1962.....	778,441.79	Mar. 24, 1963
Containerships, Inc.....	{ July 1, 1961, to Jan. 1, 1962.....	254,600.64	Apr. 1, 1962
	{ Oct. 1, 1962, to Apr. 1, 1963.....	254,600.64	(3)
Coastwise Line ¹	{ Sept. 19, 1963 (24 months).....	45,969.27	-----
	{ Dec. 26, 1959, to Dec. 26, 1960.....	170,000.00	Mar. 26, 1961
Penn Tanker Co.....	July 1, 1962, to June 1, 1964.....	635,446.80	July 1, 1964
Rye Marine Corp.....	Dec. 1, 1962, to Sept. 1, 1964.....	749,229.43	Dec. 1, 1964
Matson Navigation Co.....	Jan. 1, 1963, to May 9, 1969.....	⁴ 3,777,022.70	May 9, 1969
Newport Tankers Co.....	Sept. 1, 1963, to Dec. 1, 1963.....	185,223.70	Mar. 1, 1964
Manhattan Tankers Co.....	June 24, 1963, to Mar. 24, 1965.....	2,092,500.00	June 24, 1965
Total.....		⁵ 17,006,972.71	-----

¹ Terminations due to default.

² Voluntary termination.

³ Defaulted.

⁴ Includes \$684,210.53 previously deferred for period Jan. 1 to July 1, 1963. Reduced payments through remaining period of mortgage with balloon payment of \$3,777,022.70 due at maturity.

⁵ Deferrals are normally rescheduled over the remaining life of the mortgage resulting in periodic reductions in the amounts deferred. In addition, some companies have prepaid on the amounts deferred or have deposited earnings in a restricted fund which is collateral to the mortgage, thereby reducing the Government's potential liability.

Senator BARTLETT. Mr. Austin, please, vice president, Irving Trust Co.

STATEMENT OF JAMES A. AUSTIN, VICE PRESIDENT, IRVING TRUST CO., NEW YORK, N.Y.

Mr. AUSTIN. My name is James A. Austin. I am a member of the New York bar and for the past 16 years have been a vice president of Irving Trust Co., One Wall Street, New York, N.Y., and head of the bank's corporate trust division. I am appearing here today in support of Senate bill 2118.

Over the years Irving Trust Co. has acted as trustee for, and the corporate trust division has administered, various issues of bonds, both title XI and otherwise, secured by mortgages on U.S.-flag vessels. Until April of this year we have always understood and been advised that, our own American citizenship having been established, our acceptance of such a trusteeship, followed by delivery of and payment for the bonds, gave the bondholder an instrument of debt secured as to payment by a first preferred mortgage on the vessel concerned, and this regardless of (1) whether the bondholders were many, few, or one, and (2) the citizenship of the bondholder or bondholders.

We have never regarded holders of bonds issued under a trust indenture as acquiring a legal interest in the property is a vessel or any other property. The holder of a first mortgage bond receives from any issuer—whether it be an industrial, an electric power company, a railroad, or a shipping concern—evidence of his debt and the right to benefit from realization in accordance with the provisions of the indenture upon the security held by the trustee.

In substance, that is the ultimate right, in the event of default, to have the pledged property legally sold so that the proceeds of the sale may be applied to the satisfaction of the debt. The provisions for realization upon the security for the benefit of all bondholders is a principal reason for the interposition of a corporate trustee, thus cutting off the bondholder, as such, from any right of foreclosure or any direct dealing with the mortgaged property.

A further compelling reason is to preserve freedom on the part of bondholders to sell their bonds when and as they see fit without, until now, any concern that such a sale involved transfer of an interest in the underlying property, real or personal. Indeed, if any contrary concept were generally applied, it could be harmful not only to the market for bonds secured by ship mortgages but for bonds secured by mortgages on any personal or real property.

Such a result must follow if the rationale of the fourth circuit court in the *Steamship Westhampton* case is strictly applied. The court there stated, on page 21 of the opinion:

We are led to the conclusion therefore that, both as a general principle and in the contemplation of Congress, a ship mortgage bond is an interest in the ship mortgaged.

It would follow, if the court has correctly propounded the general principle, that an electric utility mortgage bond is an interest in the electric plant and real estate mortgaged, with the result that the sale of such a bond would be a sale of an interest in such plant and property. The ramifications of such a doctrine are novel, not to say alarming.

In the thought that this "general principle" is not only bad law but, as it stands, could accomplish considerable and widespread mischief, I urge the adoption of S. 2118 believing, as I do, that its enactment

would serve to remove present doubt cast by the fourth circuit on what in all probability was the original intention of Congress. Otherwise, the market for ship mortgage bonds will be severely prejudiced and the congressional intent with respect to the financing of merchant fleet replacements put in almost certain jeopardy.

For the peculiar vice of the court's doctrine in the case of ship mortgages, including those under title XI, is that if the mortgage is not rendered invalid at inception due to initial ownership by aliens of bonds it purports to secure, then it may be rendered invalid at a later time if, through a sale by an American national, any of the bonds come into the possession of holders who cannot, under the Shipping Act, qualify as American citizens. Sophisticated investors are not likely to accept the risks inherent in such uncertainties.

I thank you for this opportunity to put my views before you.

Senator BARTLETT. The committee appreciates your appearance, Mr. Austin.

I have no questions.

Mr. AUSTIN. Thank you.

Senator BARTLETT. Mr. Mulholland, we are glad to have you here.

STATEMENT OF WILLIAM D. MULHOLLAND, JR., MORGAN STANLEY & CO., NEW YORK, N.Y.

Mr. MULHOLLAND. My name is William D. Mulholland, Jr., and I am a general partner of Morgan Stanley & Co., investment bankers.

Senator BARTLETT. How many partners do you have?

Mr. MULHOLLAND. I have 21, sir.

Over the last 13 years I have been engaged in the business of the underwriting and private placement of corporate securities, including ship mortgage bonds, and in the furnishing of financial advice to corporations.

I have been informed that the recent decision of the fourth circuit in the case of *Chemical Bank New York Trust Company v. Steamship Westhampton* makes invalid a ship mortgage bond which has been transferred, without the prior written approval of the Maritime Administration, to a person not a citizen of the United States as defined in the shipping statutes. By use of the term "ship mortgage bond," I mean a bond issued under a trust indenture, secured by a preferred mortgage on the vessel and with a U.S. citizen as trustee-mortgagee.

The statutory definition of citizen in the Shipping Act is limited to corporations, partnerships, and associations. Under the definition, it is difficult to ascertain whether many of the organizations covered thereby are in fact U.S. citizens and it is unclear what principles are to be applied to determine citizenship of organizations not covered, such as pension trusts.

The problem of the definition of citizenship had not been considered crucial in the area of mortgage financing because it was generally thought that in the case of a trust deed and an issue of bonds thereunder the Ship Mortgage Act requires only that the trustee-mortgagee be a U.S. citizen and that the citizenship of the bondholders is irrelevant.

If the fourth circuit's ruling is a correct statement of the law—which is by no means conceded—the use of a trust indenture is of no significance and the citizenship of the bondholder determines the va-

lidity of the bond and the validity of the mortgage. Thus, I am informed, a bond may be invalid if, unbeknown to the holder, a prior holder was not a citizen. Further, in a case where there are a number of bonds, under the court's reasoning, the mortgage may be invalid if any one of many of the bonds is transferred to a noncitizen. That would leave the other bondholders without security for their investment.

This decision, I believe, creates some very serious problems in the field of ship financing. These problems fall generally into two areas: first, those related to financings already consummated and in respect of which securities are now outstanding and, second, those related to the future financing of U.S.-flag vessels.

As to previously consummated financings, there are outstanding today hundreds of millions of dollars in principal amount of bonds—including approximately \$413 million insured under title XI—secured by first preferred ship mortgages. These bonds have been purchased by investors in the belief that they were valid and binding obligations of the issuer entitled to the benefits of the indenture under which they were issued and secured by an effective mortgage upon a vessel. In this belief they were joined by the members of the bar who gave the purchasers their opinions to the foregoing effect, by those who in good faith sold the bonds, and by the Maritime Administration.

The *Westhampton* decision, it seems clear, casts substantial doubt upon the status of these bondholders as creditors in the event it should become necessary to enforce the security of the mortgage and materially impairs the ability of a present holder of such bonds to sell his holdings in the secondary market. I need not dwell, I am sure, upon the possibilities for losses by innocent investors inherent in such a situation.

Furthermore, I am mindful that in connection with the issuance and sale of bonds, the issuer frequently represents and warrants to the purchaser that the bonds have been validly issued; these representations and warranties customarily survive the delivery of the securities to which they refer.

This raises the possibility of suits for rescission, with potentially disastrous consequences for the unfortunate companies involved. It has been suggested that in those instances where bonds have been insured by the U.S. Government, under title XI, one consequence of the *Westhampton* decision would be to materially increase the likelihood of the Government having to meet heavy insurance claims.

It is difficult to see how this decision can fail to have an unsettling effect upon outstanding securities leading to losses by their holders. Under these circumstances it seems almost inevitable that confidence will be severely shaken and the merchant marine placed under a cloud, so far as financing is concerned, which may require many years to dispel. Aside from considerations of fairness to those affected, this is probably the most compelling reason for giving consideration to legislation designed to establish beyond question the validity of outstanding bonds secured by first preferred ship mortgages.

In the general area of future vessel financing, a number of problems seem to me to have been created by the *Westhampton* decision. If it is assumed that the specific approval of the Maritime Administra-

tion is necessary in the case of every transfer of a bond to a noncitizen, then one can envision formidable complications, especially where a public offering of bonds is contemplated. Merely to complete the original distribution of securities would require identification of the citizenship status of all the participating underwriters, every dealer taking down bonds for retail distribution as well as every retail purchaser of bonds on the initial offering; this would require considerable time and effort.

It would be necessary to assure that no transfer involving a noncitizen were overlooked since every such instance would require specific approval of the Maritime Administration. The failure through inadvertence or otherwise would, as I understand it, place in question the validity of the bonds and their security.

Mr. KENNEY. You indicated in cases some of the potential buyers and holders of these, that there is no criterion in the statute for determination of citizenship.

Is that correct?

Mr. MULHOLLAND. Usually an organization acting as a trustee, I suppose more often than not, is a bank or a trust company whose responsibility and duties depend on precise terms of the trust instrument; but generally speaking, their task is to receive, account for, and invest the funds entrusted to them for the benefit of the beneficiaries of the trust.

And such an organization isn't—

Mr. KENNEY. Its citizenship is not defined in the act.

Mr. MULHOLLAND. I don't believe it is really contemplated in the terms that one is to use in determining who is and who is not a citizen under the act.

Mr. KENNEY. That is what I wanted to be sure of.

Mr. MULHOLLAND. Naturally, the parties to the financing could be expected to require firm assurance as to such validity as a condition to the consummation of the financing.

Bearing in mind that time is of the essence in the marketing of a public offering of securities, I believe it is fair to say that these are very considerable obstacles to a successful financing. It is possible to envision, I suppose, a form of expedited procedure for securing the requisite approval but it would seem to me that any procedure suggestive of automatic or perfunctory approval of a list of names would be inconsistent with what is said to be the purpose of requiring Maritime Administration review and approval of such transfer in the first place.

Even assuming it were possible to cope successfully with the difficulties posed by this decision in an initial offering of securities, there would still exist a very questionable situation in connection with subsequent transfer of bonds. The failure to obtain a required approval of transfer at any point in a chain of transfers would cast doubt upon the validity of the security. A purchaser of bonds would not have any basis for determining whether the bond he was purchasing had at some time been held by a noncitizen who had not obtained Maritime Administration approval of his purchase. The practical effect would, I believe, be a substantial impairment in the marketability of bonds subject to this requirement.

While this in itself would be sufficient to raise serious questions as to the desirability of such an investment in the mind of a potential

investor, a further cause of concern would be the possibility that the failure on the part of another holder of bonds to secure a required approval of transfer would have the effect of invalidating the entire issue so that even by the exercise of the utmost care in this respect, a bondholder could not be certain that his security would not be impaired by the actions of others over whom he exercised no control or even had any knowledge.

It is worth noting that since the enactment of the Shipping Act of 1916 there has been a very significant change in the composition of the market for debt securities. Today one of the most important segments of this market is governmental and noninsured corporate pension funds. Over the last few decades, particularly since World War II, these institutions have experienced substantial growth in assets so that today they represent in the aggregate one of the largest sources of funds for investment in high grade corporate and U.S. Government obligations.

This was not the case 30 or 40 years ago. The requirements for determining U.S. citizenship do not lend themselves to application to such organizations, among others, so that today many investment institutions cannot be certain that they qualify as U.S. citizens within the strict limitations imposed by law. This means that in the light of the *Westhampton* decision, the purchase of a bond secured by a first preferred ship mortgage on a U.S.-flag vessel by such an institution would probably require the specific approval of the Maritime Administration.

A practical effect of the court's interpretation of the law is to impose an onerous restriction upon the ordinary commerce in a certain class of securities among well-established domestic financial institutions with such severe penalties for failure to comply as to throw serious doubt upon the ability of this class of securities to compete in the marketplace with other investment media.

The practical difficulties of compliance, the uncertainties created, and the severe penalties involved if the court's interpretation of the law is correct are, in my opinion, grave impediments to the financing of U.S.-flag vessels as now carried on.

Unless this situation is corrected, it will be a very stout-hearted investor indeed who will be willing to assume these risks and burdens when other attractive investment opportunities are available which do not involve similar disadvantages.

Thank you.

Senator BARTLETT. Thank you very much.

I have no questions.

Mr. KENNEY. I have none.

Senator BARTLETT. We appreciate your appearance.

Senator BARTLETT. Mr. Stokes is appearing for Kheel and Scully.

STATEMENT OF ISAAC N. P. STOKES, COUNSEL FOR KHEEL & SCULLY; WEBSTER, SHEFFIELD, FLEISCHMANN, HITCHCOCK, & CHRYSTIE, NEW YORK, N.Y.

Mr. STOKES. Mr. Chairman, my name is Isaac N. P. Stokes. I am a member of the law firm of Webster, Sheffield, Fleischmann, Hitchcock & Chrystie, counsel for the trustees in the reorganization proceedings

under chapter X of the Bankruptcy Act involving Seatrade Corp., which is the owner of the vessel *Westhampton*.

The trustees, Mr. Theodore W. Kheel and Mr. Raymond J. Scully, were very sorry that they were not able to get here today. They appreciated the willingness of the committee to hear them, and they have asked me, as their counsel, to present their statement in their behalf.

SENATOR BARTLETT. Entirely satisfactory.

MR. STOKES. AS I have just stated, Mr. Kheel and Mr. Scully are the trustees for the Seatrade Corp. Their concern with Senate bill 2118 is its retroactive effect on the rights of creditors in litigation now pending with regard to mortgages on this vessel and two other vessels, aggregating about \$3 million.

In August 1962, Seatrade Corp. issued a bond in the amount of \$960,000 payable in German currency to a German bank. The bond was issued under an indenture between Seatrade and a New York bank which purported to effect a preferred mortgage on the *Westhampton* to secure payment of the bond. Following default in interest and sinking fund payments on the bond, the mortgage trustee brought foreclosure proceedings in the U.S. District Court for the District of Baltimore. After the vessel had been sold by judicial sale but before the proceeds of the sale had been distributed, Seatrade went into reorganization proceedings under the Bankruptcy Act and the trustees were appointed to administer its affairs and to seek to work out a plan of reorganization.

In the proceedings in the Federal district court in Baltimore, various creditors who claimed maritime liens against the vessel argued that the mortgage was not entitled to preferred status under the Ship Mortgage Act, 1920, and that consequently the proceeds of sale should be applied first to the payment of their claims before any payment on the mortgage. The bankruptcy trustees took the position that the mortgage not only lacked preferred status because of failure to comply with the requirements of the Ship Mortgage Act, but was completely void because the mortgage financing was effected without the approval of the Maritime Administration required by the Shipping Act, 1916. The functions of the Secretary of Commerce specified in the act have been transferred to the Maritime Administration.

The bankruptcy trustees consequently contended that the proceeds of sale remaining after payment of valid maritime liens should be turned over to them for the benefit of the estate of Seatrade. Since efforts to work out a reorganization plan for the continuance of Seatrade's business have not been successful, funds turned over to the trustess will be applied to the expenses of administering the estate and the payment of the claims of creditors in accordance with the priorities required by law.

The district court held that the mortgage was not entitled to preferred status, since it did not meet the requirements of the Ship Mortgage Act with respect to the nationality of the mortgagee. It agreed with the creditors holding maritime liens that the provision of the act which states that an indenture trustee shall be deemed to be the mortgagee was inapplicable to a situation where, as in this case, there was only a single bond issued under the indenture. The court did not reach the question raised by the bankruptcy trustees as to the fundamental validity of the mortgage under the Shipping Act.

On appeal to the Court of Appeals for the Fourth Circuit, that court held that the mortgage did comply with the requirements of the Ship Mortgage Act as regards the nationality of the mortgagee. The court then went on to consider the question raised by the bankruptcy trustees as to the fundamental validity of the mortgage and held that the mortgage was invalid because the transaction was not approved by the Maritime Administration as required by the Shipping Act.

I might point out here that the definition of "mortgagee" to include an indenture trustee is in the Ship Mortgage Act of 1920, but it is not included in the Shipping Act of 1916. It was the validity of the mortgage under the act of 1916 with which the court of appeals was concerned and it pointed out in its opinion that the definition was not applicable.

I might also point out that the interpretation which the Maritime Administration had given as to the nationality or citizenship question when a mortgage trustee was involved was inconsistent with earlier interpretations by its predecessor agency, the Shipping Board. Those interpretations had never been, as far as we have been able to ascertain, expressly overruled, although they seemed to be inconsistent with the later ones. The court also pointed this out in its opinion.

The indenture trustee, together with the committee of American Steamship Lines as a friend of the courts, has petitioned the court of appeals for a reargument, and action on this petition is now pending. And as Mr. Kominers pointed out, it is entirely possible that the breadth of the court's opinion will be narrowed on rehearing.

Meanwhile, Senate bill 2118 has been introduced to amend the applicable statutory provisions so as to eliminate, in a case of this kind, the requirement of Maritime Administration approval.

Mortgages issued under very similar circumstances, each in the amount of about \$1 million, on another vessel of Seatrade and a vessel of one of its affiliates are involved in similar litigation now pending in Bombay and Port Said. It is expected that the Indian and Egyptian courts will apply the law of the United States, as the law of the flag of the vessels, and will not reach final decisions until they have the benefit of a final decision in the *Westhampton* case to serve as a precedent.

The bankruptcy trustees are not concerned with the merits of this bill insofar as it affects mortgages that may be executed hereafter or even mortgages already executed but not yet involved in foreclosure proceedings. The trustees believe, however, that once foreclosure proceedings have been commenced, the rights of the different classes of creditors in the proceeds of the sale of the properly claimed to be subject to the mortgage should be determined by the law as then in effect, and that to change this law retroactively is unfair and open to serious constitutional objections.

The mortgage trustee is trying to save the mortgage by parallel steps in two branches of the Government. In the judicial branch, it is proceeding by a petition for rehearing, of which the bankruptcy trustees have been given formal notice as required by the rules of the Court. In the legislative branch it is seeking passage of the pending bill to change the applicable law. I realize of course that it is not the only party concerned with this legislation.

But there is no legal requirement for notice to the bankruptcy trustees of such a move, and they did not in fact learn of the introduction

of the bill and the scheduling of this hearing until the afternoon of June 18. For this reason, it is requested that the record of these hearings be held open for a reasonable time to permit the bankruptcy trustees to file a memorandum of law with the committee regarding the very important question of the constitutionality of the bill as regards its retroactive effect in taking away the rights of creditors that have accrued in foreclosure proceedings already instituted.

I might point out that, although there are many decisions holding that the Congress can constitutionally legislate retroactively, there are other decisions, including decisions of the Supreme Court, which set certain limits on that power of the Congress, and the question as to which class of cases this particular bill would fall under is one that requires very careful scrutiny.

Meanwhile the trustees urge this committee to consider the questions of policy involved in making the bill apply retroactively to the *Westhampton* mortgage.

The memorandum in support of this bill which accompanied its introduction on June 10 was concerned primarily with the effect that the *Westhampton* decision might have on mortgages insured by the Government under title XI of the Merchant Marine Act, 1936. It should be noted that the *Westhampton* mortgage was not an insured mortgage, and neither were the mortgages on the two vessels involved in the related proceedings in India and Egypt. The bankruptcy trustees are not, therefore, concerned with the bill as it may change or clarify the law with respect to insured mortgages, although they are not aware of any reason for differentiating between insured and uninsured mortgages insofar as the bill would change the law retroactively to affect pending litigation.

If a borrower who has borrowed money on a mortgage seeks for his own benefit to have the mortgage set aside on the technical argument that the instrument which he intended to be a mortgage was not actually a mortgage, there may be nothing particularly unfair in remedial legislation that would give the lender the security that both parties to the transaction intended him to have. But that is not the situation with which we are concerned here.

The issue involved in the pending litigation is not whether the loss should be borne by the borrower or the lender, but how the loss should be distributed among the different classes of creditors who extended credit to the borrower, including those who furnished supplies to the vessel, the vacation plan of the crew, and a large group of unsecured creditors—which will presumably include the bondholder if the mortgage is finally held to be invalid.

I might add that the United States as a creditor, is also very much involved in these proceedings, having large claims arising out of freight transactions.

SENATOR BARTLETT. Out of which transactions?

MR. STOKES. Freight transactions for foreign aid shipments, and so it is also a creditor and is affected by this mortgage.

When the mortgage was foreclosed, all creditors were entitled to whatever share of the proceeds of sale the law then in effect gave to them. It is difficult to see any valid reason for retroactively changing the law to take away from the owners of maritime liens and the general creditors funds to which they were then entitled, in order to give these funds to the bondholder who was not then entitled to them.

This is all of course on the assumption that the *Westhampton* decision is correct. There is pending a petition for reargument to review it, and there is always the possibility of review by the Supreme Court, but the law, as it now stands, for the *Westhampton* litigation, is that the bond was invalid.

The bankruptcy trustees have no quarrel with the purpose of the bill, which they understand to be the elimination of uncertainties as to the validity of ship mortgages, so that the marketability of outstanding bonds will not be impaired and so that ship construction can be readily financed in the future. They submit, however, that in order to achieve this purpose it is both unnecessary and unfair to cut down rights that have accrued to innocent creditors under the existing law. To avoid this result, the bankruptcy trustees suggest that the bill be amended by the addition of a fifth section reading substantially as follows:

Nothing in this act shall be construed to alter retroactively the rights of any secured or unsecured creditor of the owner of a vessel in any litigation pending upon the effective date of this act.

Thank you very much, Mr. Chairman.

Senator BARTLETT. Mr. Foster?

Mr. FOSTER. Yes, sir. Thank you.

We have had called to the committee's attention one case that is pending, the *Westhampton* case. You mentioned two other cases now pending in foreign courts. I gather the reason that these have come to your attention is because of your position as counsel for the trustees and their interest in that litigation.

Mr. STOKES. That is correct, they are parties to both of those litigations.

Mr. FOSTER. How many other vessels are involved in the courts throughout the world?

Mr. STOKES. I do not know of any. I do not know of any other foreclosure proceedings where the validity of the mortgage is in issue as regards the interpretation of the applicable legislation.

Mr. FOSTER. Why would you have reason to know?

Mr. STOKES. I think that we probably would have heard of it. I certainly cannot say that there is none, but a great many members of the New York Bar are very interested in this litigation and I feel quite sure that we would have heard from counsel if there had been any other cases. I am quite sure counsel would have gotten in touch with us, they would have asked for copies of our brief, and so on.

Mr. FOSTER. Thank you. With this proposed amendment, the bill is acceptable to your interests?

Mr. STOKES. Yes, sir. The trustees are not experts on the shipping policy of the United States. Their concern is the rights of creditors and they see no objection and feel that it is not really their concern to express an opinion on the merits of this legislation, otherwise than as it may affect the litigation in which they are interested. They certainly have no objection.

Mr. FOSTER. The type of amendment that you propose here would obviate the constitutional question that you raised earlier?

Mr. STOKES. Yes, sir; it would, because we feel that there would be no serious constitutional question as to the validity of the act if this retroactive feature were eliminated.

Mr. FOSTER. What you are attempting to do by these words is to permit the legislation to be retroactive in terms of the types of financing arrangements that have been made in the past, except for those financing arrangements that have come into question in the litigation that is pending in court proceedings at the time the bill would become law.

Mr. STOKES. That is correct. It might, of course, be argued that this would be unconstitutional if it were retroactive in any respect, but we don't see that as a serious problem because until there are foreclosure proceedings, the rights of the creditors in the proceeds of any particular sale—the rights of the creditors in any particular fund—have not accrued and we feel that the real objection to this bill is that it steps into a pending court case and seeks to change the law which the court has already applied and to alter the rights of creditors which matured, accrued, became vested, or whatever you want to call it. I realize these are all words that different people attach different meanings to, and I am not using them in the technical sense, but that it is objectionable both as a matter of sound Government administration, and on constitutional grounds, for legislation to upset the outcome of pending litigation in this type of a situation where the rights of the parties have already been determined by the law as in effect when these foreclosure proceedings began.

Mr. FOSTER. Do you know whether any State, or whether there are very many States, that have what is usually referred to as general saving clauses as a part of their code or statutes which, as a general rule, save rights pending in litigation in all cases in which legislation is passed unless there is a specific provision otherwise?

Mr. STOKES. No, sir; I don't remember seeing such a provision, but it would not surprise me at all if there were such.

Mr. FOSTER. You are familiar with the fact that the United States Code includes provisions which, for example, saves any actions or rights for the securing of penalties or forfeitures unless the legislation specifically provides otherwise?

Mr. STOKES. I realize that there are such general provisions and in the limited time we have had to work on this matter, we have been concentrating on the questions of the policy involved and our study of the various legal and constitutional features has not been completed. I do remember seeing such provisions. I think it would be very difficult to determine exactly how they would apply in any particular case of this kind.

You mentioned penalty or forfeiture. We are not concerned here with a penalty in the sense of a criminal penalty. It was argued in a brief submitted to the court of appeals in the *Westhampton* case, that the trustees' position was meaningless because if the mortgage was void, the vessel would be forfeited to the United States and since it had been sold, the proceeds would be forfeited.

There is a provision for forfeiture of the vessel in the event that the mortgage is executed in violation of the law. However, we believe that the forfeiture provision is inapplicable to the proceeds of sale of the vessel and there is a decision of the Circuit Court of Appeals for the Second Circuit which holds expressly that a very similar forfeiture provision was inapplicable to the proceeds of the sale of the vessel as distinct from the vessel itself.

Mr. FOSTER. This legal brief or memorandum will be available very shortly?

Mr. STOKES. I will get it to you just as soon as we can. If you have any particular deadline by which you would like it, we will—

Senator BARTLETT. We will try to reach an estimate on that before we conclude today.

Mr. FOSTER. I have no further questions.

Senator BARTLETT. Do you have any?

Mr. KENNEY. No.

Mr. STOKES. Mr. Chairman, I don't know whether the decision in the *Westhampton* case is in the record of this hearing or whether you wanted it to be.

Senator BARTLETT. It ought to be.

Mr. STOKES. I will be glad to give counsel a copy.

Senator BARTLETT. All right. It will be placed in the record.

(The *Westhampton* case follows:)

UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Nos. 9637 & 9638.

Chemical Bank New York Trust Company, Trustee, Mortgagee, Appellant,
versus

Steamship WESTHAMPTON (formerly Steamship MONTAUK POINT), her
engines, boilers, etc., Appellee.

APPEALS FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF
MARYLAND, AT BALTIMORE. ROZEL C. THOMSEN, DISTRICT JUDGE.

(Argued November 12, 1964. Decided April 5, 1965.)

Before SOBELOFF, Chief Judge, and HAYNSWORTH and J. SPENCER BELL, Circuit
Judges.

William A. Grimes (Ober, Williams & Grimes; Thatcher, Proffitt, Prizer, Crawley & Wood; Edward C. Kalaidjian; Cravath, Swaine & Moore; John W. Barnum; Robert Rosenman; and John C. Hancock on brief) for Appellant; William R. Dorsey, III, (Foley & Grainger; John J. Foley; David R. Owen; Semmes, Bowen & Semmes; Beal, McQuade & Fitzpatrick, and Arthur M. Beal, Jr., on brief) for Appellee Caltex, etc.; Solomon Kaplan (Sol C. Berenholtz on brief) for Appellee Seafarers Vacation Plan; and Isaac N. P. Stokes for Trustees in Bankruptcy.

SOBELOFF, Chief Judge:

These appeals are from a decree that the first preferred mortgage and indenture dated August 6, 1962, from Seatrade Corporation to Chemical Bank New York Trust Company, is not a preferred mortgage under section 922 of the Ship Mortgage Act of 1920. 41 Stat. 1000 (1920), as amended, 46 U.S.C.A. § 922 (Supp. V, 1964).

Seatrade contracted with Struelcken Shipyard of Hamburg, Germany, during 1961, to convert an aged T-2 tanker into a modern bulk cargo carrier. The tanker involved was the SS. WESTHAMPTON, a vessel documented under the laws of the United States at all times relevant to this case. Seatrade paid the shipyard 30% of the conversion cost and sought to borrow the remainder from the Hamburgische Landesbank Girozentrale, a Hamburg bank. The loan was to be secured by a first preferred mortgage on the WESTHAMPTON. American counsel advised Landesbank that such a mortgage to an alien would be valid only if approved by the American Maritime Administration as required by the Shipping Act, 46 U.S.C.A. §§ 808, 835. Furthermore, the bank's counsel pointed out that, even if approved by the Commission, the mortgage would still not be preferred under the terms of the Ship Mortgage Act, 46 U.S.C.A. §§ 911-984, because the proposed mortgagee was an alien. An alternative course was therefore suggested—the debt be secured by a first mortgage in favor of

United States citizen trustee, with a bond for the amount of the loan to be issued to Landesbank. Pursuant to this advice Landesbank requested Chemical Bank New York Trust Company to act as mortgagee and trustee under the trust indenture.

Accordingly, the indenture was executed and the bond issued in New York City on August 6, 1962, the terms of the transaction having been agreed on between Landesbank and Seatrade. The mortgage and indenture were prepared by Landesbank, which does not appear as a party on the face of the papers. The proceeds of the loan, \$960,000 (DM 3,836,000), passed directly from the German bank to the German shipyard. It is conceded that Chemical, the American mortgagee-trustee, undertook no more than nominal duties.

A single bond in the full amount of the indenture was executed and delivered to Landesbank. The president of Seatrade, Manuel Kulukundis, gave Landesbank his personal written guarantee of payment of the bond, and Seatrade gave the bondholder ten promissory notes, each in the amount of an installment of principal and interest.

Landesbank has been at all times the owner of the bond. At the closing it gave Chemical a written warranty that the bond was being purchased as an investment with the intention of holding it until maturity. Landesbank then agreed not to dispose of the bond without the consent of Chemical.

Six months later, on January 2, 1963, chemical informed Landesbank that Seatrade had defaulted in payments due December 31, 1962. Upon failure of Seatrade to remedy the default, Landesbank instructed Chemical to declare the loan due and to take all steps necessary for the protection of Landesbank's interests. On January 14, 1963, Chemical was instructed by the German bank to file the libel which has given rise to this case.

The SS. WESTHAMPTON was sold on March 28, 1963, by order of the District Court to a United States citizen. The sale was confirmed and the net proceeds, \$2,551,104.41, were paid into the Registry of the District Court. Chemical's claim to a priority in the proceeds was challenged by objecting creditors on the ground that the indenture did not create a "preferred mortgage" under the Ship Mortgage Act because the holder of the bond secured by the indenture was not a citizen of the United States. The District Court agreed, basing its decision on the finding that Landesbank was the real mortgagee since it had a considerable measure of potential control over the mortgaged property, the SS. WESTHAMPTON. The exception set out in 46 U.S.C.A.

§ 911(5), that:

"The term 'mortgagee,' in the case of a mortgage involving a trust deed and a bond issue thereunder, means the trustee designated in such deed," was held to be inapplicable, the phrase "bond issue" being read by the court to mean a "public bond issue."

We agree with the District Court's conclusion that the mortgage in question is not entitled to the claimed preference, but we arrive at this result by a somewhat different course of reasoning.

I

The debate below revolved around the meaning of the phrase "bond issue" as used in the Ship Mortgage Act, 46 U.S.C.A. § 911(5). Chemical contended that this phrase referred to the issue of bonds, whether to a single investor or to a larger number. Such a reading would make the citizenship of the bondholder irrelevant under the Ship Mortgage Act. The objectors answered that the meaning of "bond issue" is unclear since it could reasonably be understood to refer only to the distribution of bonds to the general public. To clear up the alleged uncertainty, it has been argued below and in this court that an interpretation should be given the term consistent with the statutory purpose of the Ship Mortgage Act. That purpose is then stated by the objecting creditors to be to permit an American trustee to act for a heterogeneous group of bondholders, some of whom might be aliens, but not to permit evasion of the general policy against foreign control. They therefore would limit the reading of section 911(5) to apply to "public" bond issues, with the result that while the Ship Mortgage Act expressly grants a preference to a mortgage held by an American trustee, the objecting creditors read into the statute a qualification—namely, that the bonds issued under such a mortgage shall be held by not less than some unspecified number of holders. This approach was adopted by the District Court.

We do not share the court's view that the meaning of the phrase "bond issue" was ambiguous when adopted by Congress in 1920. The minimal ambiguity that allegedly exists today is attributable to events occurring since the passage of the Act. No evidence was offered to show that the phrase had any meaning in 1920 other than its literal one, the issue of a bond or bonds. The supposed ambiguity was imported into the statute by the objectors' contention that the phrase might refer to public issues only. The record affords no support for the proposed distinction between public and private issues. The only testimony as to the meaning of "bond issue" in 1920 was that of several bankers called by the appellants. They all testified that "bond issue" was always understood by the financial community to mean the issue of a single or any number of bonds. While the cogency of this testimony may be arguable,¹ the fact remains that it was the only evidence offered on this point.

The District Court nevertheless found an ambiguity by referring to three post-1920 sources, none of which was addressed to the distinction the objectors are urging in this case. The first authority relied on is the *Encyclopedic Dictionary of Business Finance* published by Prentice-Hall in 1960. On page 23 that volume defines "bond issue" as "a class of bonds offered to the public at the same time." The second reference is to the testimony of a witness before the Merchant Marine and Fisheries Subcommittee in 1954 when that committee had under consideration a proposed amendment to Title XI of the Merchant Marine Act, which provides for government insurance of ship mortgages. The witness, Rudolph Hecht, chairman of the shipowner's committee that proposed the amendment, seemed to assume that a bond issue would involve the interests of a large number of persons. House Hearing on H.R. 8637, p. 18, 83d Cong., 2d Sess. (1954). Thirdly, the following dictum was cited:

"In placing ship mortgages upon a stronger basis as securities, the Congress had in mind, and expressly included, trust deeds securing issues of bonds to the public." *Detroit Trust Co. v. The Barlum*, 293 U.S. 21, 40 (1934).

None of the authorities cited makes a distinction between "public" and "private" issues and all of them can be read to embrace the issue of a single bond to a single member of the "public."

Much of the apparent difficulty in this case is caused by the artificiality of the distinction between "public" and "private" bond issues. The record shows no instance where precisely such a distinction has been drawn. The objectors meet this deficiency by making the distinction themselves, then arguing that the evidence does not clearly show that Congress did not adopt such a distinction. A public-private dichotomy did not exist until Congress made reference to public and nonpublic offerings in section 4(1) of the Securities Act of 1933, 48 Stat. 77 (1933), 15 U.S.C.A. § 77(d) (1958). Congress used the word "issue" to distinguish classes of securities and not the number of purchasers. See *Loss, Securities Regulation* 577, 591 (1961). Thus we fail to find an ambiguity justifying abandonment of the literal meaning of "bond issue"—the issue of a bond or bonds.

As the District Court points out, however, a literal meaning may be rejected if its adoption would frustrate the statutory purpose giving rise to the Ship Mortgage Act. Review of the ends attempted to be accomplished reveals just the opposite, that acceptance of any construction other than the literal one will undercut the congressional purpose. The 1920 Act cannot be understood without reference to earlier history.

At the beginning of the First World War the American ocean-going merchant marine was almost nonexistent. Congress, concerned with the scarcity of domestic shipping, the withdrawal of ships by aliens and inflated freight rates, adopted the Shipping Act of 1916, 39 Stat. 728 (1916), now codified with amendments in 46 U.S.C.A. §§ 801-42 (1958).² Congress hoped that the small private merchant marine that did exist could be preserved by insuring that control over American ships would remain in domestic hands. To achieve this end section 9 was adopted, the predecessor of 46 U.S.C.A. § 808. Paragraph 2 of that section provided that no ship purchased from the Maritime Board could be leased, sold or chartered to "any person not a citizen of the United States," without first obtaining the approval of the Secretary of Commerce. Paragraph

¹ Not only were these bankers just at the beginning of their careers in 1920, but there is no indication that any factual situation ever arose which required a decision to be made as to the meaning of the phrase "bond issue."

² See House Rep. No. 659, 64th Cong., 1st Sess., 50 (1916).

3 added that such approval would similarly have to be obtained for the transfer during a war or national emergency of any ship registered under our laws. The Shipping Act of 1916 was thus enacted to preserve what merchant marine we did have.

In the year following the passage of this Act German submarines began to decimate allied shipping. Foreign capital made systematic attempts to replenish their losses by gaining control of American vessels.³ To thwart such raiding activities Congress added section 37 to the Shipping Act, 40 Stat. 901 (1918), 46 U.S.C.A. § 835 (1958). This section enlarged on paragraph 3 of section 9 by providing that it shall be unlawful during a war or national emergency to do the following without first obtaining the approval of the Secretary of Commerce:

"(b) To sell, mortgage, lease, charter, deliver, or in any manner transfer * * * to any person not a citizen of the United States, (1) any such vessel or any interest therein * * *."

"Mortgages" were added to the list of restrictions because they had "proved to be a common device by which foreign capital has sought to obtain control of American vessels." 56 Cong. Rec. 8026 (1918). Then in 1920 section 9 of the Shipping Act was amended to extend the added restrictions of section 37 to peacetime transfers of interests in ships documented under the laws of the United States. 41 Stat. 994 (1920). 46 U.S.C.A. § 808 (1958). The Shipping Act, as amended, thus had a positive end and a negative means—it was hoped that our merchant marine might be built up and preserved by preventing its slipping into foreign hands.

At the close of the First World War a new situation arose which gave rise to pressures eventually resulting in the Ship Mortgage Act of 1920. When the war in Europe ended the United States Government owned 1,280 oceangoing flag ships. Gilmore and Black, *The Law of Admiralty* 570 (1957). Promptly Congress authorized the dismantling of this fleet and its sale to privately owned shipping lines. H.R. Rep. No. 443, 66th Cong., 1st Sess., 4, 9 (1919). It was soon realized, however, that this result could not be accomplished unless considerable new capital could be attracted to the private shipping industry. To this end the Ship Mortgage Act of 1920 was enacted.

Investment in shipping has been frustrated over the years by the absence of an effective security device. The common law mortgage was of little use in the shipping industry because it was not considered by admiralty courts to be a maritime contract. This meant that it would be subordinate to all maritime liens whenever they attached. *Bogart v. The Steamboat John Jay*, 58 U.S. 399 (1854); see Gyory, *Security at Sea: A Review of the Preferred Ship Mortgage*, 31 Ford. L. Rev. 231 (1962). The Ship Mortgage Act breathed new life into ship mortgages by according them a preference over most subsequently attaching maritime liens. 41 Stat. 1004 (1920), 46 U.S.C.A. § 953 (1958). However, a mortgage was not eligible for this preferred treatment unless the mortgagee was a citizen of the United States, and the term "mortgagee, in the case of a mortgage involving a trust deed and a bond issue thereunder," was defined as "the trustee designated in such deed." 41 Stat. 1000 (1920). 46 U.S.C.A. §§ 922 (a) (5), 911 (5) (1958). This citizenship requirement, unlike that of the Shipping Act, was absolute and could not be waived by the Secretary of Commerce.

The essential purpose of Congress in enacting the Ship Mortgage Act was to promote ship financing by affording substantial security to investors. *Merchants & Marine Bank v. The T. E. Welles*, 289 F. 2d 188, 193 (5th Cir. 1961). Unquestionably the attractiveness of any investment is diminished when there is uncertainty as to its validity. The Ship Mortgage Act thus speaks in absolutes. Mortgages to noncitizens are put wholly outside the preferential benefits of the Act, but in the case of a bond issue the citizenship of the trustee is made controlling. A reading of the phrase "bond issue" that incorporates an uncertainty into the Ship Mortgage Act and seriously impairs marketability should not be favored unless the statutory language makes it unavoidable.

The District Judge was rightly troubled by the many casual references in the legislative history to issues of bonds to large numbers of investors. It must be conceded that bond issues and trust indentures were originally devised to avoid the necessity of issuing a security document to each member of a large group of creditors. One mortgage was executed to a trustee and he held it in trust for all the creditors. *Butler v. Bahm*, 46 Md. 541, 546 (1877).

³ See House Rept. No. 568, 65th Cong., 2d Sess. (1918).

When speaking of bond issues it was only natural that the image evoked was that of a large number of bondholders, but no legal result had ever turned on the number of bondholders under a trust indenture. Though Congress may have assumed unconsciously that large numbers of investors would likely be involved, this assumption was not incorporated into the statute. The objecting creditors offer no feasible rule for determining at what point a "bond issue" is excluded from the meaning of the Ship Mortgage Act because of the diminished number of bondholders.

An argument vaguely similar to that addressed to us in this case was rejected by the Supreme Court in *Detroit Trust Co. v. The Barlum*, 293 U.S. 21 (1934). There objecting creditors contended plausibly that a ship mortgage is not eligible for preferred status when the proceeds are used for nonmaritime purposes. The Court held that the intensive analysis by Congress when the Ship Mortgage Act was passed and the specificity of the statutory provisions prevented the Court from reading in qualifications not found on the face of the statute.

"We are not at liberty to imply a condition which is opposed to the explicit terms of the statute * * *. To hold that a mortgage is not within the Act which the Act itself states is within it, is not to construe the Act but to amend it. The question of policy—whether different terms should have been imposed—is not for us. We may not add to the conditions set up by Congress any more than we can subtract from them." *Detroit Trust Co. v. The Barlum*, 293 U.S. 21, 38 (1934).

The legislative history of the Ship Mortgage Act does not permit, much less does it compel, the interpretation urged upon us. Extensive references have been made to the hearings and debates preceding the adoption of the Shipping Act and its amendments to show that Congress was concerned with the amount of control that was being exercised over American ships by aliens. This concern led to restrictions on mortgages to noncitizens, and, it is argued, the restrictions would be meaningless if a foreign investor could secure the same objective by taking a bond instead of a mortgage.

It is beyond question that the possibility of alien control was of vital concern to Congress but the legislation primarily designed to meet that evil was found in the Shipping Act, rather than the Ship Mortgage Act. Questions of alien control should be fought out under these statutory provisions where the Secretary of Commerce, acting through the Maritime Administration, is granted the discretion to approve or condemn the control sought in a particular case.

The Ship Mortgage Act comes into play only after the degree of alien control has been determined and there has been approval under the Shipping Act, since only a "valid mortgage" under the Shipping Act is eligible for preferred status under the Ship Mortgage Act. If the degree of control by the alien is deemed by the Administration not inconsistent with the national interest it will give its approval under the Shipping Act. There is no indication that Congress meant to require a second application of discretion under the Ship Mortgage Act to determine whether the security interest should be preferred. The preference follows if the mortgagee or trustee is an American citizen and the other provisions of the Ship Mortgage Act are met.

The distinction made by the Ship Mortgage Act in respect to citizenship is among security devices that have already met Administration approval as provided by the Shipping Act. The provisions of the Ship Mortgage Act encourage certain investments by aliens, those made as bondholders. Not encouraged are those made by aliens as mortgagees, even if the mortgage has been approved by the Maritime Administration.

The heart of the objectors' contention is that an alien secures almost as much potential control by taking a single bond for an entire issue under a trust indenture as by taking the mortgage directly. If this is true, it is said that there would have been no reason for Congress to encourage one and not the other. The validity of this suggestion turns on the question whether in 1920, when the distinction was made between direct mortgages and bond issues, there was a significant difference between the status of a mortgagee and that of the owner of all the bonds issued under a trust indenture.⁴

As bondholder Landesbank is in a less dominant position than it would have been as direct mortgagee, for in that case it could foreclose the mortgage solely

⁴ It is conceded that the trust indenture in this case is the standard one and there is no indication that it differs significantly from the trust indentures in use in 1920.

on its own initiative. The bondholder, it is true, can also initiate a foreclosure but only after certain conditions have been satisfied. A demand must first be made on the trustee to foreclose. The bondholder may then proceed if the trustee refuses to act, unless the refusal is based on a legitimate reason. The bondholder may not proceed until the validity of the reason has been ruled on by a court. *Nashua Savings Bank v. Burlington Electric Light Co.*, 99 Fed. 14 (S.D. Iowa 1900).

The trustee has an independent role and is within his rights in refusing to obey a bondholder whose instruction is illegal. *Central Trust Co. v. Owsley*, 168 Ill. App. 505 (1914). See also *Huffman v. Gould*, 327 Ill. App. 428, 435, 64 N.E. 2d 773, 777 (1946). The Shipping Act makes it illegal for anyone to transfer any interest in an American ship to a noncitizen without the approval of the Maritime Administration. 46 U.S.C.A. §§ 808, 835. The trustee might with impunity refuse to foreclose the mortgage when the potential purchaser of the ship is a noncitizen. Indeed the trustee would be criminally liable if he made a transfer in violation of the statute. His refusal to act would certainly delay the foreclosure, and might entirely prevent the bondholder from foreclosing directly.

The alien as mortgagee is more likely to disregard American law since he is beyond the jurisdiction of American courts. This practical immunity is also important when the American shipowner-debtor is undergoing a judicially supervised reorganization. If a mortgage is held by an American trustee a bankruptcy court, for example, could enjoin the trustee from foreclosing pending an equitable resolution of the debtor's financial problems. If an alien held the mortgage directly he would be personally beyond the jurisdiction of the American courts, freer to proceed as he alone thought best.

It was also clear in 1920 that a trustee's loyalties were not exclusively to the bondholders. A duty was owed to the debtor as well. *Wright v. Chandler*, 180 Ill. App. 476 (1913); *Charles Green Real Estate Co. v. St. Louis Mutual House Bldg. Co.*, 196 Mo. 358, 93 S.W. 1111 (1906); *Ashuelot R.R. Co. v. Elliott*, 57 N.H. 397 (1874). This dual duty could conceivably frustrate a bondholder's desire for immediate foreclosure and sale when the debtor is trying to work out a plan that will enable him to continue in business.

Finally, bondholders are bound by the good faith actions of the trustee. 4 Cook, *Corporations* 3564 (1923). The decision of a trustee as to the timing of a foreclosure, the maintenance of the secured property or the schedule of payments on the debt could easily conflict with and frustrate the bondholder's desires.

When an investor takes a bond under a trust indenture he gives up some of the power that would be available to him as mortgagee.⁵

We have seen then that in 1920 Congress was acting to some extent with divergent, if not contradictory, motivations. On the one hand it sought to exclude alien interest in American shipping. To achieve this goal the Shipping Act was amended to reaffirm and extend to peacetime the provision adopted during World War I, voiding the transfer of "any interest" in an American ship to a noncitizen, unless the transfer was approved. At the same post-war session, however, there was a consensus that investment in American shipping should be encouraged, including investments by aliens. The latter purpose was implemented by the enactment of the Ship Mortgage Act, according a preference to certain maritime mortgages. Mortgages to aliens, even if approved, were not eligible for preference under this latter Act, but "bond issues" to aliens were encouraged. Furthermore, as pointed out in *Detroit Trust, supra*, Congress wished to delineate clearly the area of favored investments so that they would be readily marketable.

We construe the Ship Mortgage Act then to implement this purpose. We hold that the term "bond issue" includes a single bond representing a whole issue to a single investor. The mortgage to Chemical is therefore entitled to preferred status if it is otherwise valid.

II

For a mortgage to be entitled to preferred status under the Ship Mortgage Act, it must first be a "valid" mortgage. 46 U.S.C.A. § 922(a). The trustee in

⁵ There were and are important reasons why a single lender might choose to take a whole bond issue under a trust indenture rather than a direct mortgage. The investor may want to have someone else manage the debt or he may want to make it possible to split up the investment for wider distribution at some time in the future.

bankruptcy of the Seatrade Corporation contends that the mortgage upon which Chemical is suing was rendered invalid by the issuance of a bond for the amount of the mortgage to Landesbank, an alien bank, without the approval of the Maritime Administration in violation of the Shipping Act. 46 U.S.C.A. § 835(b). That section voids the transfer of "any interest" in an American ship to a noncitizen during a war or national emergency if the transfer is made without the approval of the Maritime Administration.⁶ This contention rests on two assumptions: first, that the bond issued to Landesbank is an "interest" in the SS. WESTHAMPTON; and second, that the transfer of the bond to an alien, illegal because made without Maritime Administration approval, infects the mortgage under which it was issued. We believe that both of these assumptions are justified.

The Shipping Act provides no definition of the term "interest." It was first used in 1918 when section 37, now 46 U.S.C.A. § 835(b), was added. As noted above, Congress was concerned by the continued inroads on American shipping by alien interests. The 1916 restriction forbidding unapproved "sales, leases and charters" of domestic vessels had not proved effective. To plug loopholes that had been discovered in this language Congress added a prohibition against the transfer of "any interest" in an American ship during war or national emergency, unless the transfer was first approved by the Maritime Administration.

The proposed amendment, set out in H.R. 12100, was designed to combat attempts "by every device which legal ingenuity could suggest to evade" the terms of the 1916 Act. 56 Cong. Rec. 8026 (1918). A war was in progress and Congress was in a mood for extreme measures. Congressman Saunders of Virginia, a member of the House committee that had considered the amendment, expressed the sense of the committee:

"We have sought to make the language used so sweeping and comprehensive that no lawyer, however ingenious, would be able to work out any device under this section to keep the letter, while breaking the spirit of the law." 56 Cong. Rec. 8029 (1914).

Concern was expressed on the floor of the House that the bill as reported out was too restrictive. It was noted that the broad language would restrict a sale to an alien of a single share of stock in a corporation owning an American ship, thus severely damaging the negotiability of such stock. Congressman Saunders, unmoved by the suggestion as to the consequences to negotiability, explicitly answered that the legislation was intended to cover such minority stock holdings. 56 Cong. Rec. 8037 (1918).

The legislative history of the 1918 amendment pointedly demonstrates the extent to which Congress was prepared to go in preventing or at least controlling the degree of any alien interest in American shipping. It also shows the congressional purpose that a share of stock should be considered an "interest" in the property owned by the issuing corporation. No reference was made, however, to bonds covered by a deed of trust secured by a mortgage on an American ship.

The term "interest" can have a variety of meanings. The most precise is the real property usage, an estate in land, that was developed by the English common law. *Ladd v. Ladd*, 49 U.S. 9 (1850). The term has also been used to indicate any claim in or upon property. *Ormsley v. Ottman*, 85 Fed. 492, 497 (8th Cir. 1898). As we are construing a penal provision we adopt the narrower definition though it is far from clear that Congress employed the term "interest" in a technical sense.

In a mortgage-trust indenture the property securing the debt is conveyed to a mortgagee-trustee.⁷ Chemical thus holds the legal title to the mortgaged property, the SS. WESTHAMPTON. When the bond was issued by the trustee the relation of trustee and cestui que trust arose between it and the bondholder, Landesbank. *York v. Guaranty Trust Co. of New York*, 143 F. 2d 503 (2d Cir. 1944), *rev'd on other grounds*, 326 U.S. 99 (1945); *Land Title Bank & Trust Co. v. Baron*, 341 Pa. 241, 19 A. 2d 62 (1941); *Sprigg v. Commonwealth Title Ins. & Trust Co.*, 206 Pa. 548, 56 Atl. 33 (1903). Landesbank's "interest" in the ship is the interest of a trust beneficiary in the property legally held by the trustee.

⁶ A national emergency was proclaimed by the President in 1950. Proc. No. 2914, Dec. 16, 1950, 15 Fed. Reg. 9029 (1950). The proclamation is still in effect.

⁷ The mortgage-trust indenture from Seatrade to Chemical provides as follows:

"[B]y these presents does hereby grant, bargain, sell, remise, release, convey, assign, assign, transfer, mortgage, deliver and pledge, or cause to be granted" the SS. WESTHAMPTON.

See *O'Beirne v. Alleghany & Kingua R.R. Co.*, 151 N.Y. 372, 45 N.E. 873, 875 (1897).

Scholars have long debated whether the beneficiary of a trust has a property interest in the trust res or merely a personal right against the trustee. See, e.g., Scott, *The Nature and the Rights of the Cestui Que Trust*, 1917 Col. L. Rev. 269 (1917); Stone, *The Nature and the Rights of the Cestui Que Trust*, 1917 Col. L. Rev. 467 (1917). The courts have had less trouble with this question. The Supreme Court has held that beneficiaries of a trust have an interest in the property to which the trustee holds legal title. *Senior v. Braden*, 295 U.S. 422 (1935); *Brown v. Fletcher*, 235 U.S. 589 (1915).

A bondholder is not a general creditor, but has specific rights with respect to the mortgaged property. He is entitled to protection against the unlawful acts of the trustee or others resulting in waste or destruction of his security. *Ikelheimer v. Consolidated Tobacco Co.*, 59 Atl. 363 (N.J. Eq. 1904). He may sue to prevent the impairment of his security without reference to the maturity of his bonds. *Whitmore v. International Fruit & Sugar Co.*, 214 Mass. 525, 102 N.E. 59 (1913).

Although a bondholder has less control over the secured property than a direct mortgagee he still possesses a considerable degree of control. The negotiations leading to this mortgage were carried on between the investor and the debtor, here Landesbank and Seatrade. As a general proposition, the trustee must do as he is told by the bondholder unless the instructions are illegal or immoral. The convenience of mortgaging the ship to a trustee should not obscure the fact that the debt secured is that owed to the bondholder.

"Although the mortgage and its agreements are made to and with the [trustee] yet the promise of the [debtor] is for the payment of money to the holder of the bonds, and it was to furnish security for the performance of that promise that the mortgage instrument was executed and delivered. The bondholders are the beneficiaries of the mortgage or deed of trust, and that instrument contains, in effect, a contract made for their benefit through a trustee as a convenient intermediary." *O'Beirne v. Allegheny & Kingua R.R. Co.*, 151 N.Y. 372, 383, 45 N.E. 873, 875 (1897).

In the early years following the enactment of the Ship Mortgage Act the administrative officials seem to have had no doubt that Congress was concerned with alien ownership of bonds. A few years after the First World War the predecessor of the Maritime Administration, the Shipping Board, was asked to rule whether the assignment of a bond to an alien would violate section 961(d) of the Ship Mortgage Act.⁸ The Board, refusing to approve such a transfer, stated:

"Is it not therefore clear that Congress had in view the prohibition against an interest and a right under a mortgage being assigned either directly or as incidental to the assignment of the debt? It is easy to imagine that a person not a citizen of the United States might acquire all of the bonds secured by a mortgage. It would thus become the owner of the entire interests under the mortgage and obviously such a transaction is the very one which Congress sought to prohibit."⁹

We are led to the conclusion therefore that, both as a general principle and in the contemplation of Congress, a ship mortgage bond is an interest in the ship mortgaged.

The Maritime Administration, however, in several recent opinion letters, has ruled that a bond is not an "interest" in the mortgaged ship and that it will therefore not exercise its discretion in determining whether the particular bond issue is permissible.¹⁰ This position has been taken without any apparent consideration of the legislative history of the Shipping Act or the Shipping Board's earlier rulings under 46 U.S.C.A. § 961(d). Complete reliance was placed on the definitional section of the Ship Mortgage Act, 46 U.S.C.A. § 911(5),

⁸ "No rights under a mortgage of a vessel of the United States shall be assigned to any person not a citizen of the United States without the approval of the Secretary of Commerce." 46 U.S.C.A. § 961(d).

⁹ Letter of January 2, 1924, from Chauncey G. Parker, General Counsel, addressed to Messrs. Squire, Sanders & Dempsey, The Leader-News Building, Cleveland, Ohio. A similar ruling was made in a letter of April 6, 1927, from Chauncey G. Parker, General Counsel, addressed to Messrs. Denegre, Leovy & Chaffe, 724 Whitney Central Building, New Orleans, Louisiana.

¹⁰ See, e.g., Letter from E. Robert Scaver, General Counsel, to Charles S. Cunningham, One Twenty Broadway, New York 5, New York, May 11, 1959; Letter from James L. Pimper, General Counsel, to Robert E. Kline, Jr., Munsey Building, Washington 4, D.C., October 19, 1960.

which as we have seen, defined "mortgagee" as the trustee where there is a deed of trust and a bond issue. Such an analysis is fallacious and completely unwarranted.

First, the definitions found in 46 U.S.C.A. § 911(5) refer only to terms used in the Ship Mortgage Act. Second, the term defined by 46 U.S.C.A. § 911(5) is "mortgagee"; the disputed word in the Shipping Act is "interest." Third, the definition of "mortgagee" in the Ship Mortgage Act was adopted two years after the insertion of the term "interest" into the Shipping Act. Fourth, the Shipping Board, when construing section 961(d) of the Ship Mortgage Act, did not indicate that section 911(5) affected in any way its exercise of discretion in determining whether to permit the assignment of bonds to noncitizens. See *supra*, at p. 21.

The only possible explanation for the later policy of the Maritime Administration is its unconscious assumption that 46 U.S.C.A. § 911(5) of the Ship Mortgage Act impliedly amended the Shipping Act to delete the interest of a bondholder from those interests requiring approval. There is no indication in the legislative history that such a result was intended. Implied amendment is not favored if two pieces of legislation can be reconciled. We have already seen that such a reconciliation is both possible and rational: Transfers of bonds to aliens must first be approved by the Maritime Administration. If approval is given and there is an American "mortgage" the mortgage is eligible for preferred status under the Ship Mortgage Act. In adopting the Ship Mortgage Act in 1920 the endeavor of Congress was to avert foreign control while encouraging private investment, whatever the nationality of the investor. Mortgages to aliens were not encouraged because they were thought to involve too much potential control. Yet it was believed that in selected cases some mortgages in alien hands might safely be permitted to take an unpreferred status. Bond issues, however, presented more variables than mortgages. There might be one bondholder or the holdings might be diffused among a thousand, the control exercised by each bondholder varying accordingly. If the Maritime Administration approved the bond issue then the mortgage securing it was eligible for a preference if the mortgagee was an American citizen.

The effect of an unapproved, hence illegal, bond issue on the mortgage to the trustee is a less troublesome question. The debt is represented by the bond; the trustee only holds the mortgage for the protection of the bondholder. Chemical has no personal interest in the mortgage. The mortgage and the bond represent one loan. If one fails, so does the other.

Chemical argues that great weight should be given to the recent attitude of the Maritime Administration that bonds are not interests in the ship mortgaged. While it is true that courts, as a general rule, pay great deference to administrative decisions they do so only for certain compelling reasons.¹¹ Many of those reasons are not present in this case. The recent rulings were not an exercise of quasi-legislative discretion vested by statute in the Administration. They were interpretations of statutory language. *Manhattan Co. v. Commissioners*, 297 U.S. 129, 134-35 (1936). They were not substantially contemporaneous with the passage of the Act, see *United States v. American Trucking Ass'n's, Inc.*, 310 U.S. 534, 549 (1940), nor are they representative of a long standing agency practice. See *United States v. Shreveport Grain & Elevator Co.*, 287 U.S. 77, 84 (1932). The overruling of decisions facing in the opposite direction, made during the 1920's, was not based upon a re-examination of the underlying facts and policies that should be considered a part of the legislation construed. *National Labor Rel. Bd. v. Globe Automatic Sprinkler Co.*, 199 F. 2d 64, 68 (3d Cir. 1952). In any event, the alien lender in this case did not ask the Maritime Administration to approve the issuance of the bond.

We recognize the resulting embarrassment when an administrative body, misinterpreting a statute, declines to exercise its lawful jurisdiction. A court, however, for the reasons above stated, may not, in the present circumstances, ignore the statute's command. Being invalid the mortgage is not entitled to the claimed preference.

The order of the District Court is

Affirmed.

¹¹ The weight given a decision of an administrative agency "will depend upon the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade, if lacking power to control." *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944) (Jackson, J.).

Senator BARTLETT. You noted that the bankruptcy trustees did not learn that the bill had been introduced until June 18. It was introduced on June 10, with a statement subsequently that the Commerce Committee issued a press release. We realized that it isn't always possible for all interested parties to become familiar immediately with bills that are introduced in Congress.

We realize, too, that this hearing followed rather quickly the introduction of the bill. That was because it was represented that an urgent situation existed. Some of the testimony given this morning by—I should say the proponents of the bill consider this a crisis rather than an urgent matter.

Mr. STOKES. We understand that perfectly, Mr. Chairman.

Senator BARTLETT. But, we are going to hold the record open so you may submit the memorandum of law to which you referred and we are going to take further testimony on this bill. The date hasn't been finally fixed, but it will in all likelihood be July 7, 8, or 9. We will make a sure determination just as soon as we can and if you will leave your card with the committee staff, we will notify you as soon as the date is settled.

(The memorandum follows:)

MEMORANDUM SUBMITTED ON BEHALF OF TRUSTEES FOR SEATRADE CORP.

CONSTITUTIONALITY OF RETROACTIVE APPLICATION OF S. 2118

Theodore W. Kheel and Raymond J. Scully are the trustees in reorganization under chapter X of the Bankruptcy Act for Seatrade Corp., the owner of the vessel *Westhampton*. The decision of the Court of Appeals for the Fourth Circuit in *Chemical Bank New York Trust Company v. The Steamship Westhampton* which invalidated the first preferred ship's mortgage on that vessel, led to the introduction of S. 2118.

The trustees' concern with S. 2118 is its retroactive effect on the rights of creditors in litigation now pending with regard to mortgages on the *Westhampton* and on two other vessels. The trustees maintain that the rights of the different classes of creditors in the proceeds of the sale of the property claimed to be subject to the mortgages accrued upon commencement of the foreclosure proceedings against each of the vessels, and that it would be unconstitutional to cut down these rights retroactively as contemplated by the present draft of the bill.

Retroactive legislation runs counter to our basic common law tradition

There is a deep felt aversion to retroactive legislation in this country based on the desire for certainty in the law. Madison expressed it in terms of protecting the people from the "fluctuating policy" of the legislature. The *Federalist*, No. 44 at 279 (Lodge Ed. 1888).

The decision in the *Westhampton* case carried out the original policy of the Shipping Act of 1916, which was to build up our merchant marine and to prevent foreign capital from gaining control of American vessels. A change in this policy now should not affect the rights of creditors already involved in foreclosure proceedings. (It was not until recently—over 40 years after the passage of the act—that the Maritime Administration first voiced the interpretation it is now advocating). See *Chemical Bank New York Trust Company v. The Steamship Westhampton*.

The aversion to retroactive legislation is also based on the fact that it enables Congress to pass laws with exact knowledge of who will benefit. If S. 2118 is to apply to the pending litigation it will be for the express benefit of three German tanks. It would thus be open to the criticism of being a partial piece of legislation, designed to advance particular private interest.

Finally there is the strong common law tradition that while a court's decision may relate to past conduct, a legislature should declare law for the future. *Claridge Apartments Co. v. Commissioner* (323 U.S. 141 (1944)). This prin-

ciple is particularly applicable here, where the mortgage trustee is already pursuing its case in the courts.

Retroactive legislation must be based on a clearly discernible and overriding public policy

The fifth amendment to the U.S. Constitution provides:

"No person shall * * * be deprived of * * * property without due process of law; nor shall private property be taken for public use without just compensation."

In giving content to this amendment the courts have required that retroactive legislation involve a clearly overriding public purpose. *Lynch v. United States* (292 U.S. 571 (1934)); *Treigle v. Acme Homestead Assn.* (297 U.S. 189 (1936)).

Retroactive legislation affecting contractual and other rights has been sanctioned by the courts only when grave matters of public policy or overwhelming matters of public interest were involved as in times of war or acute depression; e.g., *Home Building & Loan Assn. v. Blaisdell* (290 U.S. 398 (1934) mortgage moratorium); *Fleming v. Rhodes* (331 U.S. 100 (1947) price control); *Norman v. Baltimore & Ohio R.R. Co.* (294 U.S. 240 (1935)) gold clause as applied to private obligations but unconstitutional as applied to Government obligations, *Perry v. United States* (294 U.S. 330 (1935)).

Where matters are of a private contractual nature the courts do not generally see fit to uphold retroactive statutory provisions which interfere with individual or corporate rights which have already accrued. *Treigle v. Acme Homestead Assn.* (297 U.S. 189 (1936)); *Pennsylvania Coal Co. v. Mahon* (260 U.S. 393 (1922)).

There is no public purpose sufficient to justify the retroactive application of S. 2118

The memorandum submitted by Senator Bartlett in support of the proposed legislation indicates that its prime purpose is to eliminate any undermining of public confidence as to the validity of ship mortgage bonds heretofore or hereafter insured by the U.S. Government under title XI of the Merchant Marine Act of 1936 and to insure their marketability in the future. Its purpose is to protect the principal method presently being used to finance the ship replacement program of subsidized lines and to prevent possible Government liability on bonds and mortgages on which it heretofore issued incontestable policies of insurance. This is the announced public purpose of the bill.

S. 2118 also affects noninsured bonds and mortgages but no reasons were given by the sponsor for their inclusion in the legislation, the result of which will be a particular benefit to private financial interests—foreign banks which failed to secure the required approval of the Maritime Administration. To apply it retroactively where rights have already accrued would undoubtedly be stricken as unconstitutional as not based on a general public need. *Treigle v. Acme Homestead Assn.* (297 U.S. 189 (1936)); *Ettor v. City of Tacoma* (228 U.S. 148 (1913)).

Clearly there can be no overwhelming public policy to validate retroactively private bonds and mortgages in which the Government has no interest for the sole benefit of a few foreign banks.

Retroactive application of S. 2118 where foreclosure litigation was pending would substantially impair the rights of creditors

The rights of creditors in the *Westhampton*, and the other foreclosure proceedings in which the bankruptcy trustees are involved, vested upon the commencement of the proceedings. *Ettor v. City of Tacoma* (228 U.S. 148 (1913)). Any retroactive change in the law would impair the liens and cut down the rights which had already accrued and hence would be unconstitutional. *Coombes v. Getz* (285 U.S. 434 (1932)), *Ettor v. City of Tacoma*, and *Lynch v. U.S.* (292 U.S. 571 (1933)), where it was held:

"Contracts between individuals or corporations are impaired within the meaning of the Constitution whenever the right to enforce them by legal process is taken away or materially lessened" (p. 580).

In other words, where a retroactive statute destroys the legal incidents of a preexisting right the court will not sustain its retroactive application.

It is immaterial that the parties to the *Westhampton* and other mortgage foreclosure proceedings originally thought that there was a valid first preferred

mortgage on the vessels. It is unconstitutional to apply a statute retroactively in order to validate that which was otherwise invalid and destroy a preexisting right. *Forbes Pioneer Boat Line v. Board of Com.* (258 U.S. 338 (1921)) :

"To say that the legislature simply was establishing the situation as both parties knew from the beginning it ought to be would be putting something of a gloss upon the facts. We must assume that the plaintiff went through the canal relying upon its legal rights and it is not to be deprived of them because the legislature forgot" (p. 340).

A factual situation parallel to that with which the bankruptcy trustees are concerned was presented in *Louisville Joint Stock Land Bank v. Radford* (295 U.S. 555 (1935)). The Frazer-Lemke Act was passed just before the foreclosure sale on the mortgage. This act enabled a defaulting mortgagor who had been adjudged bankrupt to retain possession of the foreclosed property for 5 years upon payment of reasonable rent during which period he could redeem the property by paying off the mortgage at its then appraised value. The Court held that the act was unconstitutional in that it resulted in the "taking of substantive rights in specific property * * * acquired prior to the act," and that "the taking of these rights from the mortgagee effects a substantial impairment of the security" (pp. 590, 595). The lien had been abridged and this was not cured by the fact that the mortgagee retained rights in the property. Accord: *W. B. Worthen & Co. et al. v. Kavanaugh* (295 U.S. 56 (1935)).

In the instant case if S. 2118 should be made effective retroactively it would substantially limit the liens of maritime creditors which existed at the time the foreclosure proceedings were instituted even though they retain some rights to the fund. This would constitute a sufficient impairment of the rights of creditors under the fifth amendment.

S. 2118 should not be made applicable to pending litigation

It is submitted that the retroactive application of S. 2118 to the pending legal proceedings would be unconstitutional in that it destroys the legal incidents of preexisting rights of lien and other creditors and serves no general overriding public purpose benefiting as it does only private foreign financial interests.

The trustees have suggested that the bill be amended by the addition of a fifth section to read in substance as follows:

"Nothing in this Act shall be construed to alter retroactively the rights of any secured or unsecured creditor of the owner of a vessel in any litigation pending upon the effective date of this Act."

Should the committee wish to amend the bill to meet the objections of the Maritime Administration it is submitted that the following substitute section 5 would be appropriate:

"Nothing in this Act shall be construed to alter retroactively any rights which were the subject matter of litigation pending on the date of the enactment of this Act."

Mr. STOKES. Thank you very much Mr. Chairman.

Senator BARTLETT. Are there any further witnesses?

**STATEMENT OF ROBERT S. HOPE, KOMINERS & FORT,
WASHINGTON, D.C.**

Mr. HOPE. Mr. Chairman, I would like to make a very brief statement. My name is Robert S. Hope. I am a partner of Mr. Kominers', and I would like to say on behalf of CASL that we have absolutely no objection to the point raised by Mr. Kheel's attorney and no objection to the amendment.

Senator BARTLETT. Thank you. Yes, sir?

**STATEMENT OF JOHN BARNUM, CRAVATH, SWAINE & MOORE,
NEW YORK, N.Y.**

Mr. BARNUM. My name is John Barnum, Senator. I am a member of the firm of Cravath, Swaine & Moore. We are counsel for the

Chemical Bank New York Trust Co., and I certainly don't propose to argue the merits of the *Westhampton* case in this forum.

Senator BARTLETT. Sit down.

Mr. BARNUM. But I would—in view of the statements made by Mr. Stokes this morning, on page 5 of his prepared statement—I would like to take exception to two of those statements. The inference is inescapable that it is the Chemical Bank that has proposed this legislation, and the further inference is inescapable that there was a moral obligation upon the Chemical Bank to serve notice of this legislation upon the bankruptcy trustees.

I think that there is no foundation for either inference, and I wish that Mr. Stokes, in the brief time he had heard of this bill, between June 18 and today, had taken time to ascertain the facts.

I would like to ask the committee for permission to submit a memorandum of law which will, in effect, be in opposition to the memorandum which Mr. Stokes will submit.

Senator BARTLETT. Permission granted.
(The memorandum follows:)

MEMORANDUM OF CRAVATH, SWAINE & MOORE, ATTORNEYS, CHEMICAL BANK
NEW YORK TRUST CO.

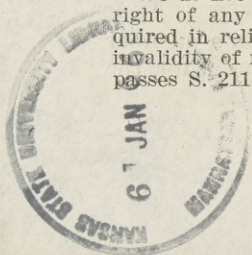
S. 2118 would amend the Shipping Act, 1916, and the Ship Mortgage Act, 1920, so as to make clear that all existing and future ship mortgages and ship mortgage bonds are and will be valid (assuming other requirements are met) so long as the trustee-mortgagee is a U.S. citizen as defined in the Shipping Act, 1916, even though bondholders looking to the mortgage as security may not be. Clarification of the law is made desirable by the decision of the U.S. Court of Appeals for the Fourth Circuit in *Chemical Bank N.Y. Trust Co. v. S.S. "Westhampton"* ("the *Westhampton* case"). On April 5, 1965, that court held that a bond is an "interest" in a mortgaged vessel within the meaning of 46 U.S.C. 835(b), and that therefore issuance of a bond to a noncitizen requires prior approval by the Maritime Administration, even though the trustee-mortgagee is a citizen. The illegal transfer of the bond, the court went on to say, "infects" the mortgage securing the bond. Therefore, the court held, the claim of Chemical Bank New York Trust Co., as trustee for a German bank, is not entitled to the preferred status under the Ship Mortgage Act which the parties to the financing contemplated when the loan was made.

The Maritime Administration had previously ruled on many occasions that its approval was not necessary in such a case. At the June 23, 1965, hearing held by this subcommittee on S. 2118, Carl C. Davis, General Counsel of the Maritime Administration, testified that in the opinion of the Maritime Administration the fourth circuit's decision is "wrong" (transcript of hearing, pp. 9, 10). Mr. Davis reiterated that view when he testified again on July 15, 1965. Addressing himself on that occasion to the question whether the bill should be retroactive across the board, Mr. Davis also said:

"As we stated in our testimony on this bill on June 23, 1965, we believe the bill should be retroactive and that there should be no exception to such retroactivity. We believe that under the *Westhampton* decision, either the vessel will ultimately be forfeited to the United States or the creditors who contracted with the owner on the basis that the preferred mortgage was valid will obtain a windfall gain. This is the reason we think S. 2118 should be retroactive. And we think there should be no distinction among creditors with regard to retroactivity" (prepared statement, p. 3).

The effect of S. 2118, therefore, would be not only to fulfill the expectations of the parties to the financing, but also to conform to the practice of the Maritime Administration.

We do not urge the Congress to interfere with any property or other vested right of any creditors involved in pending litigation, or with any rights acquired in reliance upon or as a result of a final judicial determination of the invalidity of mortgages involved in litigation. We believe that, if the Congress passes S. 2118 to clarify the shipping laws, the courts will be diligent to pro-



fect any such rights. This memorandum is submitted in support of the proposition that legislation designed to clarify the law could and should apply equally to all outstanding ship mortgages and bonds.

The decision of the Supreme Court in *McFaddin v. Evans-Snyder-Buel Co.* (185 U.S. 505 (1901)), is a startlingly close precedent. The most significant difference appears to be that there the residence of the mortgagor, rather than the citizenship of the bondholder, invalidated the mortgage in the eyes of the lower court—until Congress amended the relevant statute. Evans had loaned \$130,000 to one Blocker to purchase cattle, and had taken back a note and a mortgage on the cattle. The mortgage was timely filed in the Indian territory court, in the district where the cattle were located. Thereafter McFaddin, a creditor of Blocker, obtained a judgment against Blocker and, with notice of the mortgage on the cattle, attached the cattle. McFaddin sought to levy on the attachment, Evans interpleaded, and the district court sustained the attachment against Blocker. (McFaddin did not have a judgment against Evans at that point, but that should not be a material distinction; the point is that all the parties were already engaged in litigation.)

After several trials on the interpleader, the case went to the court of appeals for the Indian territory which held for McFaddin because Blocker was not a resident of the Indian territory. At the time of the levy, the law required that such mortgages be filed in the county in which the mortgagor resides. Thus, the court concluded, the mortgage was invalid. Evans appealed to the eighth circuit.

Between the time the district court sustained the attachment and the Indian territory appellate court held the mortgage invalid, Congress amended the law to say that, if a mortgagor is a nonresident of the Indian territory, the mortgage shall be recorded in the district in which the property is situated. The amendment also provided that:

"All mortgages of personal property in the Indian territory heretofore executed and recorded in the judicial district thereof in which the property was situated at the time they were executed are hereby validated" (185 U.S. at 507). Evans invoked the new act, the eighth circuit sustained the validity of the new act as applicable to the present case, and the Supreme Court affirmed. The Supreme Court pointed out that McFaddin's position "is very different from that of a purchaser for a valuable consideration without notice of an alleged prior incumbrance" (185 U.S. at 511). The Court continued:

"And we agree with the circuit court of appeals, that while it is not necessary to enter into the question of the comparative equities of the parties, yet, when the validity of the curative act is to be passed upon, that, in circumstances like those of the present case, the act cannot be justly impugned as depriving the attaching creditor of property within the meaning of the Constitution" (*ibid.*).

The Supreme Court has uniformly sustained statutes which operate retroactively with the aim of restoring the parties to their original expectations. In *McNair v. Knott* (302 U.S. 369 (1937)), the Court said:

"There is nothing novel or extraordinary in the passage of laws by the Federal Government and the States ratifying, confirming, validating, or curing defective contracts. Such statutes, usually designated as 'remedial,' 'curative,' or 'enabling,' merely remove legal obstacles and permit parties to carry out their contracts according to their own desires and intentions. Such statutes have validated transactions that were previously illegal relating to mortgages, deeds, bonds, and other contracts. Placing the stamp of legality on a contract voluntarily and fairly entered into by parties for their mutual advantage takes nothing away from either of them" (302 U.S. at 372-373). (Footnote omitted.) See *Williams v. Paine* (169 U.S. 55, 79 (1897)); *Seese v. Bethlehem Steel Co.* (168 F. 2d 58 (4th Cir. 1948)). On a number of occasions the Supreme Court has also held that remedial statutes passed by State legislatures do not violate the due process clause of the 14th amendment. See, e.g., *West Side Belt RR v. Pittsburgh Const. Co.* (219 U.S. 92 (1911)); *Gross v. United States Mortgage Co.* (108 U.S. 477 (1883)); *Erwell v. Dags* (108 U.S. 143 (1883)).

The Supreme Court has also upheld curative legislation that was enacted after a decision that upset expectations had become final. *Paramino Lumber Co. v. Marshall* (309 U.S. 370 (1940)); *Watson v. Mercer* (33 U.S. (8 Pet.) 88 (1834)).

Here, of course, the *Westhampton* decision has not even become final. (The fourth circuit is considering Chemical's petition for reargument in banc.) The courts have frequently upheld curative statutes enacted in the midst of litigation.

tion, after court decisions which are overcome by the curative statute, but which have not become final at the time of the enactment of the statute. In *Goddard v. Frazier* (156 F. 2d 938 (10th Cir.), cert. denied, 329 U.S. 765 (1946)), the court upheld curative legislation enacted by Congress after an adverse decision in the court of appeals and the district court. The court said:

"Where the object and effect of the curative statute is to 'correct an innocent mistake, remedy a mischief, execute the intention of the parties, and promote justice, then both as a matter of right and of public policy' the law is constitutionally valid * * *. Furthermore, a legislative act which cures the illegality or defect may be passed and become operative after suit is brought to enforce the rights accruing by reason of the illegality or defect. The bringing of the suit vests in a party no right to a particular decision" (156 F. 2d at 942).

Likewise, curative legislation passed by the U.S. Congress while a case was on appeal was upheld by the Texas Supreme Court in *National Carloading Corp. v. Phoenix-El Paso Express, Inc.* (176 S.W. 2d 564, 569-70 (Tex. 1943), cert. denied, 322 U.S. 747 (1944)). See *Graham & Foster v. Goodcell* (282 U.S. 409 (1931)).

Congress has been held, moreover, to have the power in bankruptcy cases to apply legislation changing the order of priorities in bankruptcy matters to proceedings pending at the time of the enactment of the legislation. *New York Credit Men's Adjustment Bureau, Inc. v. A. Jesse Goldstein & Co.* (276 F. 2d 886 (2d Cir. 1960)); *Coin Mach. Acceptance Corp. v. O'Donnell* (192 F. 2d 773 (4th Cir. 1951)).

Accordingly, we join the Department of Commerce in urging that the subcommittee adopt S. 2118 in its original form and leave to the courts the determination whether any parties to pending litigation would be treated unfairly by application of the new act to those cases.

Mr. BARNUM. Thank you, sir.

Mr. STOKES. I would like to say I didn't mean to cast any reflections at all on the behavior of counsel for Chemical. I was merely pointing out the fact that we were caught fairly short, and we realize, of course, that we are technically on notice of anything that appears in the record.

If there was any reflection on the behavior of counsel for Chemical, I wish to apologize.

Senator BARTLETT. The committee will not so infer. This has been one of the mildest hearings in a long time. [Laughter.]

The committee will stand in recess on this particular bill until July 7, 8, or 9, and, tomorrow morning, we are meeting in room 457, Old Senate Office Building, on S. 1958.

SHIP MORTGAGE BONDS

FRIDAY, JULY 9, 1965

U.S. SENATE,
COMMITTEE ON COMMERCE,
SUBCOMMITTEE ON MERCHANT MARINE AND FISHERIES,
Washington, D.C.

The subcommittee met at 10:10 a.m., in room 1318, New Senate Office Building, Hon. E. L. Bartlett presiding.

Senator BARTLETT. The committee will be in order to continue hearings on S. 2118.

The first witness this morning is Thomas L. Meyer, Washington representative, Seafarers International Union.

Mr. Meyer.

STATEMENT OF THOMAS L. MEYER, WASHINGTON REPRESENTATIVE OF THE SEAFARERS INTERNATIONAL UNION OF NORTH AMERICA, AFL-CIO

Mr. MEYER. Mr. Bartlett, before I proceed with my testimony, in reading it over this morning I noticed that on page 4—and possibly this should be off the record—

(Off the record.)

Senator BARTLETT. All right.

Mr. MEYER. Thank you, sir.

Mr. Chairman, my name is Thomas L. Meyer. I am the Washington representative of the Seafarers International Union of North America. I greatly appreciate this opportunity to appear before your committee.

I would like to comment on S. 2118, introduced by Senator Bartlett (by request), on June 10, 1965. This bill proposes to amend certain sections of the Shipping Act of 1916 and the Ship Mortgage Act of 1920 dealing with the transfer of "interests" in American-flag vessels to aliens. The bill, itself, says nothing whatsoever specifically concerning "Title XI: Government-Insured Mortgages," but the memorandum in support of the bill which was prepared for presentation by Senator Bartlett talks only about Government-insured mortgages.

The attorneys for the Seafarers pension and welfare plan and the Seafarers vacation plan have been litigating the case of *Chemical Bank New York Trust Company v. The Steamship Westhampton* since January 1963, and there is a recent decision in this case by the Court of Appeals, Fourth Circuit, which is given as the reason for this legislation.

Our lawyers tell us that neither the U.S. District Court of Maryland nor the Court of Appeals for the Fourth Circuit has said anything whatsoever about Government-insured mortgages, and our case does not involve a Government-insured mortgage, but involves a mortgage wherein a German bank is the sole bondholder with the broadest type of control imaginable over the trustee, Chemical Bank New York Trust Co., under a trust indenture.

Accordingly, our case, wherein the courts have held that the mortgage is not a valid preferred ship mortgage because it violates our statutes, in no way involves Government-insured mortgages. However, let us assume the language of the Court of Appeals for the Fourth Circuit might possibly have some effect on Government-insured mortgages, as is stated in the memorandum.

If the proponents of the bill had come to us, we obviously would have cooperated in supporting legislation clarifying anything that needed clarifying because, as we understand, in Government-insured mortgages, the Government, under the law, always has complete control of the situation regardless of who may own the bonds, and no vessel insured can ever be operated or purchased by aliens through foreclosure or otherwise without governmental approval.

If S. 2118 covered only Government-insured mortgages or bonds I wouldn't be speaking here today.

The "joker" is that this bill, quietly and between the lines, covers all trust indenture mortgages, past, present, and future, insured and uninsured, regardless of who the trustee may be, who owns the bonds, and what control is given to the alien bondholder over the trustees by the trust indenture itself.

We say that this bill, if passed, enables aliens to obtain control of American-flag vessels through the trust indenture mortgage device, where no Government insurance is involved, contrary to the law, contrary to the decision of our U.S. courts, contrary to congressional intent from 1916 to date, and contrary to all known rulings by the Shipping Board or Maritime Administration from 1920 until 1949.

As early as 1924, the General Counsel of the U.S. Shipping Board took the firm position that no bond should be sold or assigned to an alien without previous approval of the U.S. Shipping Board under section O(d) of the Ship Mortgage Act of 1920, which is one of the sections which this bill seeks to amend. The General Counsel, in his written opinion, stated:

It is easy to imagine that a person not a citizen of the United States might acquire all of the bonds secured by a mortgage. It would thus become the owner of the entire interest under the mortgage and obviously such a transaction is the very one which Congress sought to prohibit.

The changes proposed by S. 2118 seek to enable bonds to be held by aliens, even if the alien holds the only bond or all the bonds issued, contrary to the aforementioned 1924 opinion of the General Counsel of the Shipping Board, and contrary to the present decision of the Court of Appeals for the Fourth Circuit.

I understand that this bill, S. 2118, if passed as drawn, would enable even a Russian bank, which could not directly be the mortgagee, to indirectly be the mortgagee, by having an American citizen as trustee who could be living in Russia and even be an employee of the bank and then the Russian bank itself hold the only bond issued under a

trust indenture, which would give the Russian bank holding the bond complete control over the trustee. All of this could be done without requiring the approval of the Maritime Administration or any other governmental agency.

What could be more ridiculous and contrary to the welfare of our American merchant marine, contrary to the security of our country, and contrary to the intent of Congress.

We oppose any such changes to the law regarding uninsured mortgages and suggest that this committee should also oppose such changes.

Secondly, we want to protest and object to the manner in which this legislation was brought into being. The *Westhampton* case has been in litigation in the U.S. courts since January 1963, is still in litigation and in all probability will end up in the Supreme Court. While this litigation still is pending, the attorneys for the Committee of American Steamship Lines, without notifying us or our attorneys, quietly, and without a true and full explanation of the effect of this bill, requested Senator Bartlett to introduce the bill as an emergency measure on June 10, 1965. Had we not been alert, a matter as vital as this bill could possibly have quietly slipped through, to the detriment of our entire country. Since the bill is drawn to have a retroactive effect it would wipe out the decisions of our U.S. courts thereby harming many American citizens who have claims against the *Westhampton*. This also would result to the detriment of general creditors of the Kulukundis companies involved, including the U.S. Government itself which is looking for more assets of Kulukundis in an effort to collect certain moneys which the Government claims are due.

This, we say, is not the way in which members of CASL or people represented by CASL, should be conducting themselves if they truly are interested in developing our merchant marine, and are desirous of obtaining the full support of the American people behind our merchant marine.

I suggest that this committee urge that all interested Government agencies and departments check into the effect of this proposed bill, and that they be given a reasonable opportunity to be heard. We strongly and urgently recommend that if any change is made in the law, it be a simple change excluding "Title XI: Government Insured Mortgages" from the sections involved, since the law regarding Government-insured mortgages already assures that the vessels affected cannot pass into alien ownership or control through the mortgage device.

Again, I thank you for the opportunity of appearing before your committee.

Senator BARTLETT. Thank you.

I am going to give Mr. Foster an opportunity in a moment to ask some questions. But before doing so, I want to say only that I disagree emphatically with one part of your statement, that is where you said that "this bill could have been quietly slipped through."

My experience has been the Seafarers International and all others, as a matter of fact, interested in the merchant marine are too alert to allow any such thing to happen.

Mr. MEYER. We try to be, sir.

Senator BARTLETT. Mr. Foster?

Mr. FOSTER. Thank you, Mr. Chairman.

Mr. Meyer, would you state again for the committee how the SIU is concerned, involved in the *Westhampton* case?

Mr. MEYER. Yes, sir. We have at the moment, I believe, about \$103,000 involved in contributions to our various funds, which are owned by the owners of the vessel, the *Westhampton*. These are obligations of the ship to deposit to the account or for the men who were employed aboard the ships, at least the *Westhampton* prior to the time it got into its present financial difficulty.

Mr. FOSTER. And if this legislation were passed in its present form that would, by itself, defeat your claim?

Mr. MEYER. As I understand it; yes, sir, on the advice of attorneys.

Mr. FOSTER. There was proposed at one time during some earlier hearings an amendment which would have the effect of saving any rights in litigation pending at the time the act would become law.

Would this meet your objections?

Mr. MEYER. Mr. Foster, I would prefer—we have here today as another witness, the attorney for the various pension and welfare funds of the Seafarers International Union, and I would think that Mr. Kaplan would probably be better qualified as the attorney for the fund to answer that particular question.

Mr. FOSTER. In other words, you made some suggestions but in terms of specific wording he would be in a position to be of assistance.

Mr. MEYER. Yes; Mr. Kaplan would be in position to suggest changes to you, sir.

Mr. FOSTER. Your concern is, as I understand it, that the Russians might take control of the American fleet?

Mr. MEYER. They could very well, if they acquired enough bonds of the various American-flag ships, and as I understand it, there is nothing to stop them from acquiring these interests, and transferring the ships to foreign flags, thereby defeating the entire purpose of the American merchant marine.

Of course, it would terminate the employment of our men. Once they went in—under the foreign flag under the proposed bill it could be done. I don't say this is going to be done but it could very readily be done legally.

Mr. FOSTER. You seriously think this is a threat?

Mr. MEYER. Oh, yes, anything that is ambiguous, this particular thing, we consider anything a threat to the American merchant marine today. Too many powers working against us.

Mr. FOSTER. But you don't consider it a threat if the vessel has on it a title XI mortgage?

Mr. MEYER. No, sir; we believe this is enough protection, sufficient protection under a title XI mortgage to assure that this does not happen.

Mr. FOSTER. The protection you have under title XI mortgage that you don't otherwise have is what?

Mr. MEYER. Would you repeat that, sir?

Mr. FOSTER. The protection that you have under a title XI mortgage that you do not otherwise have is what?

Mr. MEYER. Well, the Government assumes, takes over the obligations and so forth and has control of the disposition of the vessel under title XI where it doesn't have it under these private mortgages.

Mr. FOSTER. The disposition of the vessel?

Mr. MEYER. Well, the sale and control of the vessel itself; under title XI.

Mr. FOSTER. In other words, under title XI the Government can either approve or disapprove a sale of a vessel but if the vessel is financed through private channels that then the operator can transfer the vessel at will to a foreign flag.

Mr. MEYER. I wouldn't say that it would transfer the financial interest and sell the vessel under the terms of the mortgage. The vessel could be sold without the control or necessary consent of the U.S. Government agencies involved.

Mr. FOSTER. What would happen in a situation like that? Could you elaborate on that just a bit more in just what steps would be involved there?

Mr. MEYER. Well, I will do the best I can, Mr. Foster.

As I understand it, the bank, the trustee, could take over the vessel, a local—a holder of the bonds could take over the vessel itself, and then as the trustee of a ship they could in turn put the vessel up for sale and it could then be bought by the bondholder; it might be an alien bondholder. They could buy the vessel to protect their own particular rights and then put the vessel under a foreign flag.

Senator BARTLETT. On that point you say they may buy the vessel under those circumstances?

Mr. MEYER. Yes, sir.

Senator BARTLETT. Well, to do so wouldn't they have to offer the highest price?

Mr. MEYER. I would assume the highest price would be the one.

Senator BARTLETT. Then they don't have a sure way of acquiring the vessel. Someone else might put up more money.

Mr. MEYER. Well, they having the primary interest in this thing I would assume they would wish to protect their investment.

Senator BARTLETT. I am thinking specifically here in a situation where the U.S. Government might know that if this transaction were consummated that the vessel would go to the Soviet Union, I would imagine the Government would move in there.

Mr. MEYER. Well, sir, we don't know what the Government's position would be in such a case, and rather than permit or leave this to the action of the U.S. Government to possibly hope they would claim the vessel we have no assurance that they would.

Senator BARTLETT. All right.

Mr. FOSTER. As I recall, the Government—a representative from the Maritime Administration, came before the committee before and testified in favor of the legislation.

Mr. MEYER. Sir, I didn't have a copy of his testimony, and it might be in my office but I haven't read it.

Mr. FOSTER. I only mention that in respect to the point you made on page 5 of your statement in which you suggested that the committee urge all interested Government agencies and departments to check with the proposed bill to give them a reasonable opportunity to be heard.

Mr. MEYER. Well, there may be other Government agencies involved in this particular legislation, sir, aside from Maritime that in one way or another might have an interest, so if there are others than

Maritime we wanted to be sure that every agency was consulted on this particular proposal.

Mr. FOSTER. Thank you, Mr. Chairman.

Senator BARTLETT. Mr. Meyer, further in that connection we will agree, I assume, that the Maritime Administration is the principal agency having an interest.

Mr. MEYER. Yes, sir.

Senator BARTLETT. As Mr. Foster noted, it is true that Mr. Davis, the General Counsel of that Administration, came before the committee when the first hearing was held on this bill on June 23 of this year and supported it. It is also true that he said at the conclusion of his testimony that insofar as he knew the views of the Department of Justice had not yet been presented.

Now, in respect to notification of Government agencies, I believe it to be the practice of congressional committees to solicit the opinions of those departments directly affected and those only, although that doesn't mean that any department might not become involved because there is clearance which has to be provided by the Bureau of the Budget which has the responsibility of checking with all agencies that might conceivably have an interest.

Mr. Davis, in testifying, said that there was no objection on the part of the administration to the Maritime Administration's presenting a statement favoring the bill, outright endorsement of the bill. There was a notation, though, in Mr. Davis' testimony that the Bureau of the Budget had not yet obtained the views of the Department of Justice, and I would assume, of course, that this committee as well as the Bureau, would desire to know what the Department of Justice thinks about this bill, whether it is for it or whether it is against it, but I think the record ought to be clear on the point that the Maritime Administration did, for the reasons that Mr. Davis stated, favor the bill.

In other words, I suggest just as a matter of interest to you that you might want to examine the transcript and note what Mr. Davis had to say on June 23.

Mr. MEYER. I shall.

Senator BARTLETT. Now, a question arose in my mind as you testified, and I doubt whether you are any more capable than I of answering it, it isn't of any importance but perhaps you know, you say that even a Russian bank could gain control of a ship if this bill were to become law.

My question is this: Is there a Russian bank or is there just the Russian bank?

Mr. MEYER. I understand, sir, there is a Russian bank or maybe the Russian bank would be a better word. There is one in Vienna or I should say Austria, I assume it is Vienna and also one in London.

Senator BARTLETT. Is this just one Russian bank, a single bank controlled by the Government, the Soviet Union?

Mr. MEYER. Yes, sir.

Senator BARTLETT. That is your understanding?

Mr. MEYER. Yes, sir, that is my understanding.

Senator BARTLETT. I don't have any further questions at this time, Mr. Meyer.

Thank you very much.

Mr. MEYER. Thank you, sir.

Senator BARTLETT. The next witness will be Mr. Kaplan.

Let the record show that the committee has requested a report of the Department of Justice. No such report has yet been submitted. The committee will make an urgent request of the Department to submit a report within the very near future.

Mr. Kaplan, we are glad to have you here.

STATEMENT OF SOLOMON KAPLAN, ATTORNEY, SEAFARERS VACATION PLAN AND SEAFARERS PENSION & WELFARE PLAN, BALTIMORE, MD.

Mr. KAPLAN. Thank you.

Mr. Chairman, my name is Solomon Kaplan. I am an associate in the law firm of Sol C. Berenholtz with offices in the Maryland National Bank Building, Baltimore, Md. I appear today as counsel for the trustees of the Seafarers Vacation Plan and Seafarers Pension & Welfare Plan in opposition to S. 2118.

Our basic opposition to S. 2118 is that the bill as proposed affects not only title XI Government-insured mortgages, but also affects uninsured mortgages.

In addition, the bill is drawn to have a retroactive effect, so that it will nullify the decisions of the U.S. District Court for the District of Maryland and the U.S. Court of Appeals for the Fourth Circuit, in the case of *Chemical Bank New York Trust Company v. The Steamship Westhampton*.

Finally, the bill as proposed, will enable aliens, where mortgages are not insured under title XI, to acquire control of American-flag vessels indirectly through the trust indenture mortgage device, although Congress has specifically provided in 46 U.S.C. 922(a)(5) that the mortgagee of American-flag vessels must be a U.S. citizen as designated in 46 U.S.C. 802 and 888.

The *Westhampton* litigation has been in the U.S. courts since January 1963. The Seafarers Vacation Plan, and others claiming maritime liens against the *Westhampton* have attacked the validity of the alleged first mortgage in that case. The attack on the mortgage has been basically a narrow one pertaining to the facts of that particular case.

In the *Westhampton* case, Chemical Bank New York Trust Co. is the trustee, and the sole bondholder is a German bank. The bond is for almost \$1 million, payable only in German marks, and the trust indenture gives the bondholder virtually complete control of Chemical and the vessel.

In effect, Chemical is nothing more than the controlled agent of the German bank under the trust indenture. For example, the trust indenture provides that in the event of a default the trustee, when directed by the bondholder, must take possession of the vessel without legal process and operate it. When directed by the bondholder, the trustee must sell the vessel without a court proceeding. At such sale the bondholder, in this case we are dealing with a German bank, may buy the vessel. It is only with the bondholder's consent that the ship-owner can cure events of default.

Further, the trust indenture provides that the bondholder may remove the trustee at any time, and for any or no reason. There are

many other facts in the *Westhampton* case to show the complete control which the German bank had over the trustee.

The U.S. district court in Maryland, and the Court of Appeals for the Fourth Circuit, have both held that the mortgage to the German bank is not a preferred ship mortgage. The reasoning of the court of appeals differs from the reasoning of the district court, but a petition has now been filed on behalf of the German bank requesting that the case be reargued before the full court of appeals.

The Committee of American Steamship Lines have also filed a motion to be allowed to appear as amicus curiae, and have also filed a memorandum. Counsel for the creditors attacking the validity of the German mortgage were also given an opportunity to file their comments on the petition and motion.

While this case is still pending, this bill has been introduced, and has been drawn so as to have retroactive application and thereby nullify the decisions of our U.S. courts.

It should particularly be noted that after Chief Judge Rozel C. Thomsen, of the district court in Maryland, had rendered his initial opinion holding that the German bank did not have a preferred ship mortgage, he withdrew the opinion and specifically requested the U.S. Government to express its views, and a memorandum was filed on behalf of the Government.

The official position of the Government, as expressed through the Department of Justice, was that it took no position on the correctness of the court's withdrawn opinion. The Maritime Administration expressed its own views, somewhat to the contrary, in a separate section of the Government memorandum. Government witnesses from the Maritime Administration and Customs then testified before the district court, and Government counsel was heard. That was counsel from Admiralty and Shipping Section of the Department of Justice.

On appeal, the Government expressly informed the court of appeals that it did not wish to appear or file any memorandum. There again the Government refers to the Admiralty and Shipping Section of the Department of Justice.

The contention now being made by the proponents of this bill is that the reasoning of the court of appeals, which held that the bond to the German bank is an interest under a mortgage and cannot be transferred to an alien without the consent of the Maritime Administration, may be interpreted as casting doubt on the validity of title XI insured mortgages and bonds.

The *Westhampton* case does not involve a Government-insured mortgage, and the court of appeals in no way considered title XI mortgages in connection with its decision.

Insofar as title XI Government-insured mortgages are concerned we have no objection to the statutes involved being amended so as to eliminate any possible doubt as to the validity of these mortgages and bonds. We take this position because Congress has already provided in title XI, 46 United States Code sections 1271 to 1280, for the type of controls which prevent any alien bondholder from ever being able to operate the vessel or to cause the vessel to be sold to an alien.

For example, under the statute and regulations, the Government must approve of the trustee. The Government must approve of each and every provision of the trust indenture. The mortgage can only

be foreclosed with the consent of the Government. Essentially the only right that the bondholders have is to declare a default through the trustee, in which event, the Government pays off the bondholders, and takes an assignment of the mortgage and of the rights of all of the bondholders.

For these reasons, we do not oppose an amendment to the proposed bill which would limit its application to mortgages insured pursuant to the Merchant Marine Act of 1936. We suggest, however, that even in this regard, the amendment should not be made retroactive.

We have no strong feelings as to the retroactivity in regard to title XI but I comment on that in a few moments.

We vigorously oppose the bill as drafted to the extent that it affects uninsured mortgages. Firstly, we oppose the bill because it has been given a retroactive application, and it would nullify our successful litigation in the U.S. courts. Even more important, we oppose the bill because it would enable aliens, through the trust indenture mortgage device, to obtain control of American-flag vessels contrary to our laws as they now exist.

We point out that if this bill is passed as proposed, it will enable, either in peacetime or when this country is at war or in a period of national emergency, any alien to be the real mortgagee, simply by being the sole bondholder under a trust-indenture type mortgage, and arranging to have an American citizen act as trustee, even though this American citizen may be living in the same country as the bondholder, and perhaps even be an employee of the bondholder, and the trust indenture would give the alien bondholder complete control over the trustee. All of this would be permitted, if this bill should be passed as drafted, without requiring the approval of the Secretary of Commerce or any other governmental agency.

Congress never intended any such result in the existing law, and the proposed amendments as they apply to uninsured mortgages will not express the "true" intent, the true in quotes, intent of Congress as suggested in the memorandum prepared for Senator Bartlett by the proponents of the bill.

We can show that from 1918 to date, Congress has at all times expressed its determination that the mortgage device should not be used by aliens as a means of obtaining control over U.S.-flag vessels. There was nothing in the original Shipping Act of 1916 regarding mortgages. Mortgages were first covered by amendments to the act made in 1918, at which time section 835 was added, which section the proposed bill seeks to amend.

To depart from the statement for a moment, in 1918, at the hearings that took place, Mr. Alexander, the chairman of the House Committee on Merchant Marine and Fisheries, stated, and this appears in the Congressional Record, 56th Congressional Record 826:

Not only sales and charters to foreigners but mortgages to foreigners without the consent of the Shipping Board are made unlawful. This is because a mortgage has proved to be a common device by which foreign capital has sought to obtain control of American vessels.

In 1920, Congress added 46 U.S.C. 808 to carry into peacetime what it had enacted in 1918 for time of war and national emergency. The proposed bill also seeks to amend section 808.

Congress also enacted the Ship Mortgage Act of 1920, and particularly 46 U.S.C. 961(d), which the proposed bill seeks to amend.

Congress also provided in 1920, in 46 U.S.C. 922(a)(5), that in order for anyone to have a preferred ship mortgage the mortgagee must be a citizen of the United States within the meaning of sections 802 and 888.

In other words, Congress has seen fit to impose the same type of controls regarding who shall be the mortgagee of an American vessel as it has imposed in regard to who shall be the owner of an American vessel. Sections 802 and 888 initially applied to ownership as enacted in 1916, and as strengthened in 1918.

In 1920 Congress particularly in connection with the Ship Mortgage Act made the same requirement in regard to citizenship the same rigid requirement in regard to citizenship, as to mortgagees as existed in case of owners and stockholders.

From 1920 to date Congress has never changed its basic position in this regard although there have been some minor modifications of the statutes. It should be noted that in each of the three sections involved, Congress provided flexibility by enabling the sale, mortgage, or transfer of any interest in a vessel with the approval of the Secretary of Commerce. The proposed bill makes the transfer of an interest to an alien valid, without the approval of the Secretary of Commerce.

S. 2118, in essence, contends in the case of a mortgage involving a trust deed and a bond issue thereunder Congress was not concerned as to the citizenship of the bondholder since the trustee, under 46 U.S.C. 911(5), is deemed the mortgagee. A careful review of the entire legislative history will show that the only reason for the enactment of section 911(5) was that in the case of a trust indenture with a bond issue held by many investors, which is what Congress had in mind, one trustee was needed in order to speak on behalf of all of the bondholders when necessary to declare a default under the mortgage, or to extend time to the owner of the vessel, or to otherwise administer the duties required under the trust indenture. There is nothing whatsoever in the legislative history of section 911(5) which would indicate that Congress intended that any bonds could ever be held by aliens, without the consent or approval of the Secretary of Commerce, merely because the trustee was a citizen of the United States.

Tokyo Rose, of course, was also a citizen of the United States and I assume any alien who really wanted to find someone to be trustee, an individual, in any country in the world, Russia or any others, they can find some American citizen who will act as trustee, and they control the mortgage and in essence be the mortgagee.

The administrative agencies involved, and particularly the Maritime Administration and its predecessor, the U.S. Shipping Board, have not uniformly interpreted the applicable statutes over the past 45 years.

In an opinion rendered on January 2, 1924, the General Counsel for the U.S. Shipping Board held that bonds secured by a mortgage or deed of trust should not be sold to aliens without the previous approval of the Board.

The opinion stated, in part:

* * * Is it not therefore clear that Congress had in view the prohibition against an interest and a right under a mortgage being assigned either directly

or as incidental to the assignment of the debt. It is easy to imagine that a person not a citizen of the United States might acquire all of the bonds secured by a mortgage. It would thus become the owner of the entire interests under the mortgage and obviously such a transaction under the mortgage and obviously such a transaction is the very one which Congress sought to prohibit.

Again in 1927, the General Counsel for the Shipping Board in an opinion stated:

I might add that the Board considers that its approval must be obtained before bonds or notes, the payment of which is secured by a mortgage on a vessel of the United States, can be legally assigned to an alien.

For a period of approximately 30 years from the time of the enactment of the statutes involved, these two rulings were apparently followed.

However, in 1949, without citing any authority whatsoever for the administrative change in interpretation, and without referring to the aforementioned opinions, the Chairman of U.S. Maritime Commission took the position that only the citizenship of the trustee need be considered, and such citizenship is not affected by the ownership of the bonds secured by the mortgage. We have been unable to find any opinions covering the years 1949-57, but since 1957, the Maritime Administration has indicated, when requested, that its approval would not be required when bonds were transferred to aliens. The Maritime Administration, however, has generally qualified its opinions by stating that the trust indenture must provide that the bondholder will not acquire any interest in or control over the mortgage or the vessel.

It is apparent from the foregoing that the Court of Appeals for the Fourth Circuit, in holding that the transfer of a bond to an alien is the transfer of an interest in a vessel requiring the approval of the Secretary of Commerce, does nothing more than reaffirm the position taken from 1918 to 1949 by the administrative agency having responsibility in this area.

We submit that Congress should not amend the laws involved insofar as they pertain to uninsured mortgages. These laws have been in existence now for almost half a century, and to our knowledge there is no evidence whatsoever that they have had any detrimental effect on our merchant marine. To amend the laws as proposed, we submit, would enable alien interests to obtain control of a segment of our merchant marine through the trust indenture mortgage device.

Since 1918, Congress has consistently sought to prevent any such alien control, either directly or indirectly. In any event, it would be most unjust, and of questionable legality, to amend the laws retroactively, so as to affect vested, judicially determined rights of other parties.

In regard to title 11 Government-insured mortgages, as I have stated previously, we do not oppose any amendments which will be helpful. We suggest that S. 2118 be amended to apply only to title 11 mortgages. We suggest that this can be done simply by inserting after the word "mortgage" the words "insured pursuant to the Merchant Marine Act, 1936 (46 U.S.C. 1271-1280)" on line 8, page 1 of the bill as printed, and on lines 10 and 22 on page 2 of the bill as printed.

I have made these insertions in the bill which I present to the committee and would like to be made a part of the record.

Senator BARTLETT. That will be done.

The information referred to follows:)

[S. 2118, 89th Cong., 1st sess.]

A BILL To clarify sections 9 and 37 of the Shipping Act, 1916, and subsection O(d) of the Ship Mortgage Act, 1920, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 9 of the Shipping Act, 1916 (46 U.S.C. 808), is amended by adding at the end of the third paragraph thereof the following: "*Provided, however,* That any bond, note, or other evidence of indebtedness hereafter made or issued under a trust indenture in connection with a mortgage insured pursuant to the Merchant Marine Act, 1936 (46 U.S.C. 1271-1280) on a vessel shall not be deemed to be such an interest in the vessel, the sale, mortgage, delivery, or transfer in any manner of which without the approval of the Secretary of Commerce is prohibited by this section, if the trustee designated in such trust indenture is a citizen of the United States within the meaning of section 2 of the Shipping Act, 1916 (46 U.S.C. 802)."

SEC. 2. Section 37 of the Shipping Act, 1916 (46 U.S.C. 835) is amended by adding at the end of section (b) thereof the following: "*Provided however,* That any bond, note, or other evidence of indebtedness hereafter made or issued under a trust indenture in connection with a mortgage insured pursuant to the Merchant Marine Act, 1936 (46 U.S.C. 1271-1280) on a vessel shall not be deemed to be such an interest in the vessel the sale, mortgage, delivery, or transfer in any manner of which without first obtaining the approval of the Secretary of Commerce is prohibited by this section, if the trustee designated in such trust indenture is a citizen of the United States within the meaning of section 2 of the Shipping Act, 1916 (46 U.S.C. 802)."

SEC. 3. Subsection O(d) of the Ship Mortgage Act, 1920 (46 U.S.C. 961(d)) is amended by adding at the end of the first sentence thereof the following: "*Provided, however,* Any bond, note, or other evidence of indebtedness hereafter made or issued and secured by a mortgage insured pursuant to the Merchant Marine Act, 1936 (46 U.S.C. 1271-1280) on a vessel of the United States shall not be deemed to constitute a right under such mortgage within the meaning of this subsection if such mortgage is held by a trustee who is a citizen of the United States within the meaning of section 2 of the Shipping Act, 1916 (46 U.S.C. 802)."

SEC. 4. If any provision or portion of this Act, or the application thereof in any particular circumstance, is held invalid, the remainder of the Act and the application of such provision or portion to other circumstances shall not be affected thereby.

MR. KAPLAN. In the bill I have just passed to the reporter, I have also deleted the words "heretofore or" on lines 6, 8, and 21; line 6 would be on page 1, and lines 8 and 21 on page 2 of the bill as printed.

SENATOR BARTLETT. What is the meaning of those changes?

MR. KAPLAN. We frankly have no strong feeling about this aspect of it. If Congress and if the Maritime Administration or CASL feel that the amendment is acceptable to them, in other words, that S. 2118 would meet their needs insofar as title II Government-insured mortgages are concerned, and that there is need for it to have a retroactive application, we don't feel strongly on this point.

We have the normal reluctance of enacting any bill or making any change retroactive for the constitutional questions that may arise as a result of it. But aside from that we are not concerned really with title II because, as I have stated previously, when it comes to title II Government-insured mortgages, all the controls necessary to prevent any alien control or ownership of the vessel already exist and have already been enacted by Congress.

I thank you for this opportunity of appearing before your committee.

Senator BARTLETT. Aside from the fear of the group that you represent, that enactment of the bill into law might lead to alien control, what is the particular interest of the seafarers in this issue?

Mr. KAPLAN. Well, we have two interests. You are already familiar, Senator Bartlett, with the interest in the pending litigation in the *Westhampton* case. The result of that litigation for the trustees of the pension and welfare and vacation plans alone amounts to approximately \$100,000 in contributions that are due the trustees under not only the *Westhampton* but two other vessels, one of which is in India—was in India—and the other of which is in Port Said having similar mortgages involved the same as the *Westhampton*.

So, we have an initial interest of approximately \$100,000 in contributions.

From the point of the seafarers and also from the trustees, there is always a concern of strengthening and enlarging the American merchant marine, keeping the vessels that are now under American flag remaining under American flag.

Obviously from the point of view of the SIU at any time one vessel goes under a foreign flag, is controlled by aliens or transferred to a foreign flag, they lose the jobs for their members.

To that extent the country loses a vessel which is part of the merchant marine and they no longer can rely upon in time of war or national emergency.

Congress has always been concerned—even when they have had a surplus of vessels, even in 1918, and in 1920—they were always concerned about vessels even though they had surplus vessels, getting into foreign control and into foreign ownership without the control and approval of the Secretary of Commerce.

The law as now drawn does not prevent either mortgages or the transfer of vessels to foreign flag. All that it does is that it imposes a control in which the Secretary of Commerce has control over whether it will or not be transferred or whether a mortgage will or will not be placed on a vessel which mortgage is controlled by an alien. It is that control that we still want to see exist.

Now, you questioned Mr. Meyer about the fact that the Maritime Administration has indicated its support of this bill through their spokesman, Carl Davis, who spoke here.

Well, as I have indicated before, it is no secret that the views of the Maritime Administration, in regard to the problems which exist and affect this litigation and indirectly affect this legislation, the Maritime Administration and the views of the Admiralty and Shipping Section of the Department of Justice have not been the same, and for 2½ years they have been unable to reconcile their views in the litigation, and the brief that was filed with Judge Thomsen in three sections of it the Admiralty and Shipping Section of the Department of Justice traced the history of the law and indicated they had no views as to whether the *Westhampton* mortgage was valid or invalid.

In one section of the brief, the Maritime Administration indicated its views; namely, that they thought—they didn't quite state so but they thought—that the *Westhampton* mortgage was valid. They have now taken the square position through Mr. Davis that they think the decision of the fourth circuit is wrong.

They did not file any brief. Neither the Admiralty and Shipping Section or the Maritime Administration filed any brief before the fourth circuit. I assume that the Maritime Administration didn't do so because without the consent of the Admiralty and Shipping Section or the Department of Justice they were unable to do so because their views are that, as they now express them, they want the *Westhampton* mortgage to be upheld.

But there is a conflict between two Government agencies involved, and there is a conflict now between the interpretations and rulings that are made by the Maritime Administration today and the rulings that were made for a period of 30 years before its predecessor.

For some reason they do not want the responsibility of ruling whether or not an alien does or does not have a right to be the transferee or the owner of a bond. When they have been asked the question: "If your consent is required will you approve of the transfer to an alien or will you approve of the mortgagee being an alien?" we have a record of one or two opinions in which they state that it is the policy of the Maritime Administration not to permit an alien to be the mortgagee.

But exactly what they say they will not do directly, they are willing to do indirectly now by permitting any American citizen trustee, regardless of where he lives, regardless of whether he is an individual or a corporation, regardless of what controls exist or do not exist in the trust indenture, if there is just that one factor, they are willing to let an alien be the sole bondholder.

We think they are incorrect in their approach, but this is their approach and this is the explanation, frankly, for Mr. Davis' remarks in regard to uninsured mortgages.

Senator BARTLETT. Tell me something about the *Westhampton* as a ship, what type ship is it?

Mr. KAPLAN. The *Westhampton* was originally a T-2 tanker, war-time-built tanker, and what was done with the *Westhampton*, and with the *Bridge Hampton*, *South Hampton* and several other vessels, these vessels were converted in foreign shipyards, and they were enlarged, they were cut in half, midbodies were added, certain changes were made, and they were made much more valuable vessels than they were originally. In some cases, and in the case of the *Westhampton*, the original proposition was for the German bank, who was paying off part of the bill of Kulukundis to the German shipyard, for a little less than a million dollars, a certain amount of the money for the repairs were paid directly by the Kulukundis Co. sea trade, and the balance of it, approximately a million dollars, was paid to the German shipyard in Germany.

The money never came to this country at all, and the German bank, in turn, at first requested that they be a direct mortgagee. They were informed, and this appears from the record of the case that under American laws they could not be the mortgagee because they were an alien.

It was then set up on the basis of Chemical being the trustee and they holding the sole bond. They weren't even happy in having that bond payable in American dollars. They wanted that bond payable in German marks.

Senator BARTLETT. Why?

Mr. KAPLAN. They had more confidence that the German mark would not fluctuate to the same extent as the American dollar would fluctuate.

Senator BARTLETT. Were they right or wrong?

Mr. KAPLAN. I don't know. I am not a banker. Perhaps some of the bankers who testified last time can answer that better than I can, sir.

Senator BARTLETT. How many sailors are required to operate the *Westhampton*?

Mr. KAPLAN. I wouldn't know exactly. Perhaps Tom Meyer would know better than I.

Senator BARTLETT. Approximately?

Mr. KAPLAN. I imagine it would be approximately 35 to 40.

Senator BARTLETT. In your testimony, Mr. Kaplan, you said that after 30 years had expired the Chairman of the Maritime Commission in 1945, and I quote:

Without citing any authority whatsoever for the administrative change in interpretation, and without referring to the aforementioned opinions, took the position that only the citizenship of the trustee need be considered and such citizenship is not affected by the ownership of the bonds secured by the mortgage.

That is the end of the quotation.

Now, in addition to his failure, as you say, to give any authority, did he give any reasons?

Mr. KAPLAN. No; he did not. And in addition thereto, no explanation has ever been given to the U.S. district court in Maryland or to the fourth circuit to this date as to why there was the administrative change on the part of the Maritime Administration that took place in 1949.

Senator BARTLETT. That policy determination has remained in effect to this day?

Mr. KAPLAN. There have been one or two cases which, in which they have disapproved particular proposed transactions because they have taken the position that the trust indenture or the manner in which it was handled would give the holder of the note or bond an interest in the vessel.

If you recall, I stated that all through the years the Maritime Administration has qualified its position in correspondence, and its opinions by stating that they are either assuming or requiring that the trust indenture will be such that the holder of the bond will not have any interest in the vessel itself or control the vessel.

Now, although they have said that, in practice we can't find where they have really dug into trust indentures except in one or two cases, and when I say "we" in terms of our efforts to check the records, the court, Judge Thomsen specifically asked the Admiralty and Shipping Section to check all Government records from 1916 to date, both Customs and Maritime or any other sources, to obtain the benefit of all opinions, and after 1949 no one has been able to come up with anything for the years 1949-57.

Then in 1957 we have a series of written letters in which the Maritime Administration has taken the position that where you have got an American trustee, under those circumstances they don't care in essence who holds the bonds.

Senator BARTLETT. The committee will be in recess briefly.

(Short recess.)

Senator BARTLETT. The committee will be in order.

So, nowhere, Mr. Kaplan, do you find in any record whatsoever a reason for the change in Maritime policy, Maritime Administration Commission, or whatever the name may have been at the moment?

Mr. KAPLAN. That is correct.

Senator BARTLETT. In whose hands is *Westhampton* now?

Mr. KAPLAN. The *Westhampton* was sold on public auction through the U.S. district court in Maryland. It was sold under the American flag as under the law it must be sold when it is sold in an American court.

When it is sold in a foreign court it can be sold and transferred to other flags, but when it is sold in an American court it must be sold under the American flag. I don't know the name of the company that owns it, but it is still operating now under the American flag, and it is still being manned by the SIU.

Senator BARTLETT. Did the German bank seek to intervene in respect to the sale?

Mr. KAPLAN. The German bank was the original libellant in the case through Chemical. Chemical is the trustee for the German bank. They were the ones, the mortgage became due one day, 2 days or 3 days later, they extended no further time, they immediately attached the vessel, and tried to get the vessel sold within a matter of days or weeks after that.

The court did postpone the sale so that some effort could be made by the owner of the vessel to try to make arrangements so that the vessel would not have to be sold in public auction.

But the German bank, through Chemical, and through its attorneys, has been in the case from the very moment that it started in January 1963.

Senator BARTLETT. The main reason, as I understand it, for your opposition to the bill, in the form it is now drawn, and presented to the committee, is that it would enable aliens to obtain control of American flag vessels.

Mr. KAPLAN. I would say that it is a main reason. We also have a hundred thousand dollar interest in there as well on the moneys that are due the trustees of the various plans, and I just cannot ignore that.

But in terms of the long-range reason from the SIU and from the point of view of the interest and welfare of our American merchant marine is that Congress has always recognized the fact that the mortgage is a device whereby people can obtain control, aliens could obtain control of American vessels, and we think that the Maritime Administration or the Secretary of Commerce should be required to consent to any alien mortgage or the transfer of any bond to an alien.

How then will they know to what extent they can or cannot really rely on our vessels remaining under the American flag?

Senator BARTLETT. You have named this as a more important reason than the litigation.

Mr. KAPLAN. Yes, I would say it is more important than a hundred thousand dollars, but I can't ignore a hundred thousand dollars, either.

Senator BARTLETT. Not even in these days of billions; I agree with that.

Mr. KAPLAN. Not even with million-dollar mortgages being talked about.

Senator BARTLETT. What is the situation, if you know, with reference to transfer of ownership of vessels under the so-called flag of convenience, I believe the SIU has another name for that.

Mr. KAPLAN. I am not sure I understand exactly what aspect of the problem you are driving at, Senator.

Senator BARTLETT. I don't blame you.

The ship flying a flag of convenience, as I shall term it, is owned by Americans, right? Can that ship be sold to alien interests without any reference to the U.S. Government?

Mr. KAPLAN. Well, I would say, but I am not 100 percent certain of that.

Senator BARTLETT. This is off the mainstream anyway, and I won't hold you to an answer to this because there is no reason why you should have an answer.

Mr. KAPLAN. There is one point in there I should like to comment on.

From the point of view of the unions, they are opposed, and we are opposed to flags of convenience because you end up having vessels flying under foreign flag being manned by seamen who are not American seamen. These jobs are being lost to American seamen.

Senator BARTLETT. We don't need to go into that. The Chairman perfectly understands the position of the SIU on that.

Mr. KAPLAN. Thank you.

Senator BARTLETT. I am still troubled, Mr. Kaplan. Here you are representing that there is a distinct probability, possibility, certainty, I guess, if this bill is the law, that aliens can gain control of these vessels, and yet the general counsel for the Maritime Administration, testifying before this very subcommittee on this very bill expressed no such feeling, and I must say this leaves the committee in a strange situation.

Are we to infer that the Maritime Administration has no interest in this subject which is, after all, a very important one?

Are we to infer that the Maritime Administration is deliberately seeking to create a situation where aliens can be in control of American-flag vessels?

Mr. KAPLAN. Senator Bartlett, we can't deny that, and it is common knowledge, that the Maritime Administration has from time to time in its own judgment contrary to views of others, transferred vessels from American flag to foreign flag, to flags of convenience, thereby generally when they are doing that, they are not concerned whether those vessels are or are not, sometimes are not concerned, whether those vessels are or are not going to be controlled or owned by Americans. Once they have—

Senator BARTLETT. Aren't ships flying that flag always assumed to be under the control of our Government in time of emergency?

Mr. KAPLAN. The Maritime Administration makes that representation but in fact it is—has been found that that is not always the case.

Senator BARTLETT. Can you give some examples of where it has not been the case? I am not speaking critically here, I want to find out.

Mr. KAPLAN. My understanding is that when it came to—some of these vessels were carrying cargoes to Cuba and to other ports where the policy of the Government was to the contrary, and they had considerable difficulty and sometimes were still unable to prevent that be-

cause they were under foreign flags and under charters and under different situations.

Senator BARTLETT. Were stern efforts made, in your opinion, by the Maritime Administration to prevent such shipping?

Mr. KAPLAN. I really couldn't answer that because that is really out of my interest and my field.

Senator BARTLETT. Do you look askance at the motivations of the Maritime Administration in respect to this bill from the standpoint of alien ownership?

Mr. KAPLAN. It is not a question of looking askance. I have never since I have been involved in this litigation now for 2½ years, to quite understand their position in regard to the litigation, the mortgage itself, and basically the issues involved in this bill.

Congress has made it so clear that they do not want an alien to be a mortgagee, and Congress has also made it clear that they do not want indirectly to be accomplished what is not to be accomplished directly, and if all that the Maritime Administration wants is a simple American trustee, to me they are avoiding congressional intent, because you can always find American trustees.

He can be an individual, as I have stated before, he can be a non-resident. It doesn't mean anything, and to some extent this has been a concern of Congress.

Once before when they were amending the provisions of the law in 1918, and this appears in part from the Congressional Record, 56th Congressional Record 8032, 8033, in 1918, and they were strengthening, Congress was strengthening, the provisions with dealing with avoiding the law through various devices and having aliens own our vessels, Mr. Edmunds stated:

I would like to call attention to the fact that the in the testimony of the attorney for the Shipping Board he called attention to the fact that some law firms in New York City who represented people abroad would buy a ship and all the stockholders would be members of this law firm and the stock being held in trust for foreign clients.

As I understand it this is to get around that arrangement—

When he is talking about "this is to get around" he is talking about the amendment of 802, 46 U.S.C. 802, to get around that arrangement.

Now, there you had Americans, American stockholders, who were members of the law firm holding stock in trust for aliens. What difference is there if you have an American trustee who might be an individual completely controlled by the trust indenture and otherwise by the alien interests being the trustee, but the alien being the real interest or the foreign bank or the foreign individual. It need not—there is nothing that says that the mortgagee need be a bank. It can be an individual, it can be a Russian steamship company, it can be any other foreign steamship company as distinguished from a bank, and I cannot truthfully understand their position, and they apparently in two and a half years have been unable to get the Admiralty and Shipping Section of the Department of Justice to back them up, and even the last remarks made by Carl Davis were to the effect that they had been unable to secure the views of the Department of Justice in the time available, and brief that the committee will want to have that Department's views in its consideration of the bill.

Although the issues involved have been paramount now in litigation for two and a half years, and the bill has been introduced now for a month, apparently we still do not hear from the Admiralty and Shipping Section of the Department of Justice and Maritime has still been unable to acquire their support.

Senator BARTLETT. Sir, that is not strange at all.

One time I was a delegate in Congress from the then great Territory of Alaska; the Department of the Interior asked me to introduce a bill. I introduced the bill. Throughout that Congress for a period of 2 years the Department of Interior which wanted this bill very much failed to make a report on it. I introduced in the Congress thereafter, and again the Department of Interior failed to report.

In the third Congress, the fifth year, the Department of Interior representatives came to me and said, "We need this bill very badly."

I introduced it again. During that Congress they reported on it and it was passed. So we should not be alarmed that the Department of Justice hasn't submitted a report on this bill since June 10.

Now, S. 2118 bears the notation, Mr. Kaplan, that it was introduced by me and it was introduced by request, and this is correct, of course. There was a principal reason why I did introduce that bill, and why fairly prompt hearings are being held upon it, and that reason was perhaps best described by an attorney who appeared before the subcommittee on June 23 and the witness was Odell Kominers, a partner in the law firm of Kominers & Fort here in Washington, and he appeared as counsel for the Committee of American Steamship Lines in support of S. 2118, and I want to read briefly from his testimony.

Public issues or bonds secured by mortgages insured under title II are the principal and least costly method of financing available to shipowners to carry out their replacement obligations.

Two of the CASL lines are now negotiating and must conclude in the very near future additional title II bond financing in the aggregate amount of about \$50 million. This vessel replacement program has been seriously jeopardized not only because questions have been raised regarding the validity of some title II bonds already sold but more importantly because the marketability of future title II bond issue is impaired as the result of a recent decision of the U.S. Court of Appeals for the Fourth Circuit—

And so on.

Then skipping a bit, and returning to a quotation from Mr. Kominers' testimony:

The mortgage and bond involved in the *Westhampton* case were not insured by the United States pursuant to the provisions of title II. However, the *Westhampton* decision of the Court of Appeals for the Fourth Circuit has created uncertainty regarding title II insured mortgage bonds due to the broad implications and immediate impact of the courts holding that a ship mortgage bond is considered an interest in the vessel with the result that the issuance, sale, or transfer of such bonds to a person not a citizen of the United States as defined in section 2 of the Shipping Act of 1916 was held to render the mortgage invalid since it did not have the prior approval of the Maritime Administrator.

That was the main contention of those who appeared for the legislation, that failure to act favorably upon it would create a situation whereby \$50 million worth of new ships could not be built under title II and, of course, that is a proposition of very real concern to all of us.

I wonder if you would care to comment on that?

Mr. KAPLAN. Senator Bartlett, we are just as concerned about that phase of it as—and that is why I have proposed an amendment to the

bill which would let the bill go through essentially as drafted except limiting it to title II Government-insured mortgages.

Senator BARTLETT. You want those ships built?

Mr. KAPLAN. We want the ships built, we want them financed the way they have been financed.

As a matter of fact, we want an expansion of that program to cover bulk carriers and as many other vessels as we can induce Congress to build in addition to the subsidized liners.

So, we don't want to do anything to impair the financing of these vessels, and to that extent we are in complete accord with CASL, and had this bill been introduced only as being applicable to title II Government-insured mortgages we would not be here today. It is only because the bill as drafted is so broad that it covers insured, uninsured, and not only covers uninsured but it covers uninsured retroactively, and for these reasons we do oppose it.

We are perfectly satisfied, and we will support any changes which will limit the application of S. 2188 to title II Government-insured mortgages so that financing of those vessels can go ahead just the same as before.

Senator BARTLETT. Mr. Kaplan, a suggestion was made in the testimony by Mr. Kominers which I read, that the validity of some title II bonds outstanding, title II financing, which is now outstanding, would be affected by the court decision made.

Do you think that situation will be cured by the amendment you have proposed, the amendments we have proposed?

Mr. KAPLAN. It would be cured to the same extent that S. 2118 as drafted, would cure it. I mean if it is not going to be cured by the bill as drawn it is not going to be cured by the bill as amended, and I think it would be completely cured.

Senator BARTLETT. Mr. Foster?

Mr. FOSTER. Thank you, Mr. Chairman.

Mr. KAPLAN. I have some extra copies of the bill with the interlineations if it might be of some help to you.

Mr. FOSTER. Mr. Kaplan, in order to clarify a couple of points, under the present law as referred to in the first page of your statement, the mortgagee of American-flag vessels must be a U.S. citizen, and does that mean at the present time this could be, that the mortgagee could be, an insurance company or some type of a corporation or does citizen mean they would have to be a voting, red-blooded American?

Mr. KAPLAN. There are various definitions and provisions in section 802 which define "citizen," and the various—and it varies in companies—for instance, it varies on whether the vessel is under a sales coastwise or whether it is sales foreign as to the percentage of foreign stock ownership that might exist.

But what you are driving at is a question of whether some State governments, some pension trusts—

Mr. FOSTER Yes.

Mr. KAPLAN. Some of those, that type of agency may or may not be a citizen within the meaning of section 802.

As a layman, I would think they were, but they are in categories that question might arise as to whether or not they are a citizen. That is conceivable. There was a time when there was some question of whether the Reconstruction Finance Corporation was a citizen of the

United States, and Congress had to pass an amendment to make certain that it was a citizen of the United States.

Someone mentioned that the Metropolitan Life Insurance Co. might not at one time or would not at one time have been a citizen of the United States because of one Canadian director, I think that it had, and the law was amended so that now there can be an alien director or more than one alien director provided that the aliens can never reach a point where they are more than a minority needed to constitute a quorum.

So, again Congress indicated its concern that they still were just as concerned as ever to make sure that there was real American control of vessels or mortgages.

It may or may not be necessary to further amend the law to clarify the status of State governments or pension trusts. I wouldn't want to voice an opinion on that. But these State governments and these pension trusts, to my knowledge, have only invested in title II Government-insured mortgages, so that the amendment of this bill to limit it to title II I think will cover all the problems which arise in that regard.

Mr. FOSTER. On page 7 of your statement you pointed to this decision in 1949 by the Chairman of the U.S. Maritime Commission.

I wondered if you would have a copy of that that could be made available for the record? It could be otherwise obtained but I didn't know whether you had one available or not.

(The information requested above follows:)

U.S. MARITIME COMMISSION,
June 30, 1949.

Re query whether U.S. citizen trustee under mortgage securing bonds held by aliens may be preferred mortgagee of U.S. vessel.

Hon. FRANK DOW,
*Acting Commissioner of Customs,
Treasury Department, Washington, D.C.*

MY DEAR MR. DOW: Referring to your inquiry in the subject matter dated April 11, 1949, it is our understanding that pursuant to the provisions of subsection B (5) of the Ship Mortgage Act, 1920, the citizenship of a trustee named in a deed of trust securing a bond issue is determined (for the purpose of determining its eligibility as a preferred mortgagee) by applying the requirements of section 2 of the Shipping Act, 1916, and such citizenship is not affected by the ownership of the bonds secured by such mortgage.

Sincerely yours,

PHILIP B. FLEMING, *Chairman.*

Mr. KAPLAN. I have a copy of that printed in the record of the case and I have that with me and I can make that available to you.

Mr. FOSTER. Thank you.

As I understand your thought as of 1949 then to date the United States has been exposed to the danger that you are expressing concern over, and that is the danger that foreign alien interests could become trustees controlling the U.S. citizen mortgagee; is that correct?

Mr. KAPLAN. I would say at least from 1957. We find no opinions between 1949 and 1957. But that theoretically is true from 1949 as well.

Mr. FOSTER. My problem is this: if the danger has existed for over 15 years, have you got any indication that any of the U.S. vessels have been transferred to the foreign-flag during this period of danger as a result of the problem that you raised?

Mr. KAPLAN. There are, apparently no one has records dealing with mortgages, but dealing with the efforts of aliens as defined within the meaning of 46 U.S.C. 802 obtaining ownership of the vessels, after World War II there were many cases, and the Government seized, I think it was something like 30 or 40 vessels that aliens in violation of our laws had obtained title to. To what extent there have also been instances where this was obtained through the mortgage device, I cannot answer. We do not have those records.

Mr. FOSTER. I hope you see the problem. The problem is that you point there is a danger if we pass the bill and in your testimony you also mention the fact that this danger has existed for 15 years.

Mr. KAPLAN. Well, I say it has existed because the opinion has existed, but I also point out that lawyers representing Maritime interests have continued to ask questions of the Maritime Administration. There is correspondence that has continued from 1957 almost up to date where from time to time lawyers who are interested in placing mortgages on vessels, where the mortgages were to be held by aliens or there was to be a trustee and a bond issue to the alien, have asked opinions of the Maritime Administration, and although the Administration, the Maritime Administration, has told them that under these circumstances, generally they have told them that as long as you have an American trustee, it will be all right, they have always conditioned their remarks with a provision, provided that the bondholder will not obtain any interest in the mortgage or in the vessel.

So, that on the one hand it has been possible, and on the other hand, the Maritime Administration has been sort of holding a threat over these transactions.

If this law is amended, there will be open approval by Congress of this type of situation and I don't know that up to now there have been any great number of mortgages, not involving Government-insured mortgages, where aliens have held the bonds or have been the mortgagee. There have been comparatively few, to my knowledge.

Mr. FOSTER. You don't know of any case at all in which an alien trustee has been able to, through that device, transfer a U.S.-flag vessel to a foreign flag?

Mr. KAPLAN. I know of no case either way, whether they have tried or haven't tried.

Mr. FOSTER. You say that the position of the Maritime Administration in a sense has been indefinite, that they would write and indicate that if you had a U.S. citizen as mortgagee and you had a trust arrangement, that the citizenship, as it were, of the trustee is of no interest to them as long as the trustees didn't have control over the mortgagee.

If that were appropriately administered and policed and that policy followed—namely, that no trustee would have authority and control over the mortgagee—you would see no threat to the U.S. merchant marine by selling or by financing under that arrangement; is that true?

Mr. KAPLAN. Well, this is something that the law as now drawn enables the Maritime Administration to do right now. They could approve of these transactions if they were satisfied that control could not eventually pass over to aliens.

For instance, if we had the same controls in regard to uninsured mortgages that exist now as to title II mortgages, in other words, if the mortgagee—if the trustee had to be approved by the Maritime Administration, if there could not be a foreclosure of the mortgage without the approval of the Maritime Administration, if the terms of the trust indenture had to be approved by the Maritime Administration, if all of these controls also applied to uninsured as well as to insured Government mortgages, then the danger wouldn't exist.

But to pass the amendments as drawn without imposing the same controls is what creates the danger, in our opinion.

Mr. FOSTER. Do you believe that the bill as drawn, if passed would, in effect, not approve, as it were, what has been going on in terms of financing uninsured mortgages but would it in effect be a change that up to this time even the Maritime Administration, although maybe not energetically, but the Maritime Administration has been talking about approving arrangements or not having to approve, in effect, not having to approve an arrangement where the trustees didn't have control, but if this bill were passed they could even authorize or they wouldn't have to approve even if the trustees did have control.

Mr. KAPLAN. Well, you are using the word, Mr. Foster, "trustees" as distinguished from bondholders. The mortgagee is considered to be the trustee, in our case, it is Chemical, or it might be any other U.S. citizen. The bondholders are, of course, the ones that we are really concerned about under this type of trust arrangement.

Mr. FOSTER. Yes.

Mr. KAPLAN. And I agree with what you have just said in that up to now there has been some lipservice of control being required or an absence of control of the bondholder being required before the Maritime Administration says that their consent is not needed.

When the bill is amended there will be no holds barred.

Mr. FOSTER. Thank you, Mr. Chairman.

Senator BARTLETT. Mr. Kaplan, a situation has existed since 1949, as you have explained, regarding the Maritime Administration. To your knowledge, has any effort been made to seek a congressional directive giving firm instructions to the Maritime Administration so that the policies in effect up to 1949 would be followed?

Has any suggested legislation—

Mr. KAPLAN. Not to my knowledge.

Senator BARTLETT. I wonder why, if this fear has been so great, is now so great, and this fear has existed since 1949, I wonder why someone hasn't come before us and said, "Look, a very dangerous situation exists. You ought to do something about it."

Mr. KAPLAN. I can't answer that, Senator Bartlett.

Senator BARTLETT. Thank you.

The committee—unless you have something more to add?

Mr. KAPLAN. No; I do not.

Senator BARTLETT. The committee will stand in recess subject to the call of the Chair.

Thank you very, very much.

(Whereupon, at 11:50 a.m., the committee recessed subject to the call of the Chair.)

SHIP MORTGAGE BONDS

THURSDAY, JULY 15, 1965

U.S. SENATE,
COMMITTEE ON COMMERCE,
SUBCOMMITTEE ON MERCHANT MARINE AND FISHERIES,
Washington, D.C.

The subcommittee met at 9:50 a.m., in room 5110, New Senate Office Building, Hon. E. L. Bartlett presiding.

Senator BARTLETT. The subcommittee will be in order.

This is a continuation of the hearing on S. 2118. When the committee last met on July 9 the witnesses were Mr. Meyer and Mr. Kaplan on behalf of the Seafarers International Union, objecting to S. 2118 in the form it was introduced, and near the conclusion of the last hearing it was the decision of the committee that one further meeting, at least, and probably only one more, would be held so that some points raised by Mr. Meyer and Mr. Kaplan might be answered by Government witnesses. At that time, as I recall, it was said that an urgent request would be made of the Department of Justice for a report on this bill. My information is that the Department has not yet reported and does not care to send a witness here on this bill because of pending litigation.

Is that right, Mr. Foster?

Mr. FOSTER. Yes, sir.

Senator BARTLETT. Now we have before us this morning Mr. Carl C. Davis, General Counsel of the Maritime Administration of the Department of Commerce.

STATEMENT OF CARL C. DAVIS, GENERAL COUNSEL, MARITIME ADMINISTRATION, WASHINGTON, D.C.

Senator BARTLETT. You previously testified. Do you have a statement?

Mr. DAVIS. Yes; I do.

Senator BARTLETT. Before you come to that, however, I want to refer to statements made by Mr. Meyer or by Mr. Kaplan in the transcript of the last hearing, on pages 88, 89, 99, 100, 103, 104, 107, 113, 120, 123, 131, and 132, by either Mr. Meyer or Mr. Kaplan, originally or in response to questions from Mr. Foster or me relating to a particular subject which I thought made it advisable to reconvene the subcommittee on this bill.

Now I don't propose to read from each of those pages, but I shall indicate generally what is of real concern to the committee; namely, the statement made by those witnesses named that if the bill were to be

passed by the Congress and signed into law in its present form, it would, as first stated by Mr. Meyer, and now I quote:

* * * enables aliens to obtain control of American-flag vessels through the trust indenture mortgage device, where no Government insurance is involved, contrary to the law, contrary to the decision of our U.S. courts, contrary to all known rulings by the Shipping Board or Maritime Administration from 1920 until 1949.

That statement was on page 88 of the transcript. And on page 89 Mr. Meyers said:

I understand that this bill, S. 2118, if passed as drawn, would enable even a Russian bank, which could not directly be the mortgagee, to indirectly be the mortgagee, by having an American citizen as trustee who could be living in Russia and even be an employee of the bank and then the Russian bank itself hold the only bond issued under a trust indenture, which would give the Russian bank holding the bond complete control over the trustee. All of this could be done without requiring the approval of the Maritime Administration or any other governmental agency.

What could be more ridiculous and contrary to the welfare of our American merchant marine, contrary to the security of our country, and contrary to the intent of Congress?

Mr. Kaplan, on page 99, said, and once more I quote:

Finally, the bill as proposed will enable aliens, where mortgages are not insured under title 11, to acquire control of American-flag vessels indirectly through the trust indenture mortgage device, * * *.

And on the following page, page 100, Mr. Kaplan said, in direct reference to the *Westhampton* case, and I quote:

In effect, Chemical is nothing more than the controlled agent of the German bank under the trust indenture.

And there are other statements made on the pages which I cited, elaborating on the belief of the SIU witnesses, that the bill as now presented to the committee would or could set up a situation whereby aliens could come into control of American-flag vessels.

Now, those are the propositions, and that is the particular proposition, Mr. Davis, that engages the attention of the committee this morning.

In the meantime—I don't know, I have not yet read your statement, and I don't know whether it deals with this particular problem or not—in any case, will you present your statement and then, if that doesn't cover the entire situation, Mr. Foster and I will ask you some specific questions.

Mr. DAVIS. Mr. Chairman, that problem is covered in my statement, and I will be happy—

Senator BARTLETT. It is?

Mr. DAVIS. Yes; and I will be happy to elaborate on it.

Senator BARTLETT. Thank you.

Mr. DAVIS. Thank you for the opportunity to appear before your committee to present the comments of the Maritime Administration of the Department of Commerce, and of the Department, with respect to one, the amendment to S. 2118 proposed by Mr. Isaac N. P. Stokes on behalf of the trustees in reorganization proceedings for Seatrade Corp., the owner of the *Westhampton*; two, the amendment to S. 2118 proposed by the Seafarers International Union of North America, AFL-CIO; and three, the administration of the Shipping Act, 1916, the Ship Mortgage Act, 1920, and title XI of the Merchant Marine Act, 1936, by the Maritime Administration.

The court, in the *Westhampton* case, held that the mortgage involved was not entitled to preferred status under the Ship Mortgage Act, 1920, because the bond which was secured by the mortgage was an interest in a ship under section 37 of the Shipping Act, 1916, and the issuance of the bond to an alien had not been approved by the Secretary of Commerce.

S. 2118 would amend sections 9 and 37 of the Shipping Act, 1916, by including provisos which would state that any bond, note, or other evidences of indebtedness heretofore or hereafter made under a trust indenture in connection with a mortgage on a ship is not an interest in a ship within the meaning of those sections if the trustee is a citizen of the United States; and the bill would also amend section O(d) of the Ship Mortgage Act, 1920 (which provides that no rights under a mortgage of a vessel of the United States shall be assigned to a person not a citizen of the United States without the approval of the Secretary of Commerce and that any such assignment shall be void) to provide that any bond, note, or other evidence of indebtedness heretofore or hereafter made and secured by a mortgage on a vessel of the United States shall not be deemed to constitute a right under a mortgage within the meaning of that section if the mortgage is held by a trustee who is a citizen of the United States.

S. 2118 would be retroactive. The Stokes amendment would add a new section 5 to the bill which would provide that nothing in the bill shall be construed to alter retroactively the rights of any secured or unsecured creditor of the owner of the vessel in any litigation pending on the date of enactment of the act.

This amendment would save the rights of any secured or unsecured creditor of the owner in any such litigation, but we do not believe it would save the forfeiture rights of the United States with respect to any transaction involved in such litigation.

As we stated in our testimony on this bill on June 23, 1965, we believe the bill should be retroactive and that there should be no exception to such retroactivity.

We believe that under the *Westhampton* decision, either the vessel will ultimately be forfeited to the United States or the creditors who contracted with the owner on the basis that the preferred mortgage was valid will obtain a windfall gain.

This is the reason we think S. 2118 should be retroactive. And we think there should be no distinction among creditors with regard to retroactivity.

If, however, Congress desires to save the rights of secured and unsecured creditors that are now in litigation, we think they should also save the forfeiture rights of the United States. Attached hereto is an amendment which would accomplish this result.

Mr. Meyer testified that S. 2118 would permit a Russian bank to hold the bond if there was a U.S. citizen trustee of the mortgage; and if the trustee was living in Russia, this would give Russia control of the ship.

The trustee has no control over the ship unless the mortgage is in default, and if the mortgage is in default, and the trustee forecloses in a foreign court, he is obligated to request the foreign court to follow the U.S. law and sell the vessel only to a citizen of the United States.

If a U.S. citizen trustee wished to violate the law in this respect, there would be no need for him to go through this mortgage procedure. He could merely buy a ship and turn it over to an alien.

Mr. Meyer's recommendation was that S. 2118 should be confined to bonds secured by mortgages insured by the Maritime Administration. We are opposed to this recommendation because there is a substantial amount of ship financing done with bonds secured by trusts of uninsured mortgages.

We think the risk that S. 2118 would lead to foreign control of ships is negligible and the assistance S. 2118 would give to ship financing is very substantial. Adoption of Mr. Meyer's amendment might lead to applications for mortgage insurance that would not otherwise be made.

In the administration of the 1916, 1920, and 1936 acts, Maritime has in recent years regarded the U.S. citizenship of the trustee-mortgagee in trust indenture financings as controlling the preferred status of mortgages under the Ship Mortgage Act without inquiry as to the citizenship of note or bondholders and has regarded approval under sections 9 and 37 of the 1916 act of noncitizen bondholdings to be unnecessary irrespective of the number of holders.

Maritime's position finds support in the clear language of the Ship Mortgage Act relating preferred status of mortgages to the citizenship of the trustee-mortgagee, the legislative history of the Ship Mortgage Act, and related statutes, including the rejection by the House-Senate conference of a requirement of U.S. citizenship of bondholders as a condition to preferred status and the explanation of Ira Campbell, admiralty counsel, formerly serving with the U.S. Shipping Board, the principal draftsman of the Ship Mortgage Act, that—

by restricting the right of giving and assigning the mortgage, and selling the mortgaged vessel on foreclosure, to a citizen of the United States, as defined in the Shipping Act, it seems to me that the possibility of vessels passing out from under the American flag through foreclosure is sufficiently safeguarded.

There is a letter to the chairman, Commerce Committee, February 19, 1920, and hearings, Senate Commerce Committee, on establishment of an American merchant marine, 66th Congress, 2d session, page 2075; the recognition and the effect given to the clear language of the Ship Mortgage Act relating preferred status of mortgages to the citizenship of the trustee-mortgagee by courts in *Collier Advertising Service v. Hudson River Day Line* (14 F. Supp. 335 (S.D.N.Y. 1936)); *Moon Engineering Company v. American Steamship Valiant Power* (214 F. Supp. 555 (E.D. Va. 1963)); see also *Spencer C. Brook v. S. S. Southampton* (231 F. Supp. 278 (D. Ore. 1964)), and *Detroit Trust Company v. The Thomas Barlum* (293 U.S. 21, 40 (1934)); the consistent rulings, administrative actions, and regulations issued over a long period of time in conformity with such language, history, and decided cases; the equally clear language of title 11 of the 1936 act, including the definition of "mortgagee" as specifically excluding note and bond holders and the express authorization for the insurance of loans and mortgages financed by the "sale of bonds to the general public"; the requirement for implementation of the language and objectives of title 11 under the Ship Mortgage Act; the general rules of statutory interpretation stated in 1 U.S.C. 1; the absence of clear and compelling language that bonds are an "interest" in vessels under sections 9 and 37 of the 1916 act; the absence of legislative history showing that the term "interest" was intended to include bonds or notes secured by mortgage liens held by U.S. citizen trustees as authorized by the Ship Mortgage Act or showing that it was intended for such

mortgages to be subject to question as to validity solely on the basis of the bonds or notes being transferred to or held by noncitizens without approval; the disparity of treatment which would result if a bond or note as distinguished from a share of stock were to be regarded as an interest in a vessel under the 1916 act; the decision in *United States v. Stavros Niarchos* (125 F. Supp. 214 (D.D.C. 1954)), stating that the term "in any manner transfer" as used in section 9 is a "catchall" phrase which most reasonably should be construed as covering transactions, like those enumerated in section 9, dealing "directly with the vessel" and not as opening up "a whole new area of transactions," and holding that stock of a vessel-owning corporation is not an interest in the vessel owned requiring transfer approval under the 1916 act; the opinion of the Attorney General (29 Ops. Att'y Gen. 188 (1911)), that "alien stockholders have neither the legal nor equitable ownership of any part of the vessel"; the illogical result of treating a noncitizen bond or note holder's interest as a prohibited interest in a vessel as compared with the interest of a noncitizen direct maritime lienholder; the purposeless recording requirements which would flow from the treatment of bonds and notes as interests in vessels; the inability to reconcile the requirement for filing statements of citizenship under section 40 of the 1916 act with the sale of bonds to the public under the 1920 act or title 11 of the 1936 act; the clear legislative objective of the 1920 and 1936 acts of facilitating private financing for the American merchant marine; the need for both private and public bond issues to accomplish this objective; and the frustration of such objective through the control of noncitizen bondholdings under the 1916 act.

Senator LAUSCHE. That is the longest sentence I have ever read or the longest—how you were able to come out clearly, I can't understand. It is two pages long, isn't it?

Mr. DAVIS. It is a pretty long one.

Senator LAUSCHE. They seemed to be tied together. May I ask a question at this time?

Senator BARTLETT. Not, if you please, until I make a reply to your statement. The magazine, *New Yorker*, used to—I don't know whether it now does or does not—run a column called "The Nonstop Sentence Derby" and I have seen seven sentences longer than this. Now I yield.

Senator LAUSCHE. Tell me briefly why does this issue arise? Am I correct in my understanding that it is asserted that the holder of a bond issue under an indenture of trust becomes the holder of a direct interest in the ship?

Mr. DAVIS. That is what the court's holding was in the *Westhampton* case.

Senator LAUSCHE. That was the holding.

Mr. DAVIS. Bond issue under a mortgage.

Senator LAUSCHE. What is your position? That that holding must be rectified, that it was wrong?

Mr. DAVIS. Yes.

Senator LAUSCHE. It is like holding that a stockholder in a corporation that has a mortgage would be pretty near the equivalent of an interest holder, is that right?

Mr. DAVIS. Well, under the 1916 act; yes. And that is one of the examples that was given in the long sentence which I recited.

Senator LAUSCHE. Is the Department sponsoring this bill?

Mr. DAVIS. The Department is supporting the bill.

Senator LAUSCHE. Is it the general objective of the bill to eliminate what seems to be an injustice resulting from the decision?

Mr. DAVIS. Well, to eliminate a problem of administering the ship financing laws which we are charged with and, also, any injustice that might arise in something over \$400 million worth of mortgages which are presently outstanding which bonds might fall into alien hands.

Senator LAUSCHE. Who has this?

Mr. DAVIS. It is more than \$400 million just under title 11 alone. The Government is insuring them.

Senator LAUSCHE. Now then, there seems to be some provisions of the bill that you are not in agreement with and are suggesting rectification. Are those in the bill or have they come in by amendments?

Mr. DAVIS. They have come in by amendments.

Senator BARTLETT. Proceed, please.

Mr. DAVIS. Maritime's position gives recognition to the normal incentives and ability of owners to avoid defaults on their obligations; to the interposition of the U.S. citizen trustee as mortgagee under the 1920 act; to the provisions of the Ship Mortgage Act protecting the "interest of the mortgagee" against forfeitures for violations of law, providing for enforcement of mortgage liens "by the mortgagee," and affording protection to the "mortgagee" in respect of the surrender of documents of a vessel; to the substantial protection afforded by the interposition of the U.S. citizen trustee as mortgagee; to the amendability of the U.S. citizen trustee to American law, including the sanctions imposed by the 1916 and 1920 acts for unlawful acts; to the provision of the Ship Mortgage Act restricting the sale of vessels of the United States by district courts in suits in rem in admiralty to U.S. citizens; to the absence of known problems of alien control of American-flag vessels through bond or note holdings; to the policy of the Government of seeking sales of American-flag vessels by foreign courts in suits in rem consistent with American laws; to the risks inherent in the operation of American-flag vessels in foreign waters of losing control through foreign court actions, whether involving ordinary maritime liens, direct mortgage liens, trustee mortgage liens or other foreign actions, if those courts should fail to give extraterritorial effect to American laws; to the policy of the courts of giving effect to the manifest purpose of the 1920 act to make ship mortgages attractive and secure as investments for persons supplying essential financing to the shipping industry; to the relaxation of citizenship requirements by the Congress in 1958 and 1959, Public Law 85-902 and Public Law 86-327; and to the existence of cogent reasons requiring departure from the two letter decision rendered by the Shipping Board in the 1920's.

Senator BARTLETT. That sentence is a formidable runnerup.

Senator LAUSCHE. Go ahead.

Mr. DAVIS. Two decisions in the 1920's were to the effect that mortgage bonds issued under trust deeds constitute rights under mortgages within the meaning of 46 U.S.C. 961(d) and should not, therefore, be sold to noncitizens without approval.

It was concluded that bonds held by aliens were prohibited rights under mortgages unless approved. But these earlier decisions had their shortcomings.

Judged by their content, they failed to take into account the legislative history showing that section 961(d) was included as a part of the 1920 act to restrict the assignment of mortgages to noncitizens; and that the House-Senate conference rejected a requirement of U.S. citizenship of bondholders as a condition to preferred status of mortgages. Also they failed to give due consideration to the interposition of the citizen trustee.

These earlier decisions were in effect overruled in 1936 by the decision in the *Hudson River Day Line* case, supra, where the U.S. District Court for the Southern District of New York enforced a mortgage, securing bonds sold to the public, in which the lien was held by a citizen trustee, without inquiry as to the citizenship of the bondholders, and without approval under section 9 or 37 of the 1916 act or section 961(d).

The court stated at page 338 :

A mortgage is not a preferred one unless the mortgagee is a citizen of the United States (46 U.S.C. 922). In the case of a mortgage involving trust deed and bond issue, the necessary citizenship is that of the trustee (46 U.S.C. 911) * * *.

The *Valiant Power* case, supra, in which the U.S. District Court for the Eastern Division of Virginia upheld the preferred status of a similar mortgage securing a single bond issued to and held by an alien, had the same overruling effect in 1963.

In this case the court stated at page 559 :

"Congress has seen fit to make the citizenship of the trustee the primary consideration in determining whether the mortgage is held by a citizen of this country (46 U.S.C. 911(5)), and in ascertaining the validity of any preferred mortgage (46 U.S.C. 922(a)(5)) * * *. The fact that Congress has only provided for citizenship status of the mortgagee-trustee is a clear indication that foreign capital was not to be excluded in financing U.S.-flag vessels.

The earlier decisions were also effectively overruled by the Congress when it enacted section 1111 of title XI of the 1936 act authorizing the deposit of bond proceeds with the Maritime Administration in the case of the sale of bonds "to the general public." With the restricted marketability of bonds required by these two earlier rulings this legislation would have been inoperable.

CONDITIONALLY PROPOSED AMENDMENT TO S. 2118

If the committee is of the view that S. 2118 should be amended by the addition of a new section 5 to modify the retroactive provisions of the bill, the Department of Commerce urges that such new section 5 should read as follows :

SEC. 5. Nothing in this Act shall be construed to alter retroactively any forfeiture rights the United States may have under the Shipping Act, 1916, with respect to any vessel, or interest in a vessel, which has been or is hereafter held by a court of competent jurisdiction to have been transferred, without the approval of the Secretary of Commerce to any person not a citizen of the United States, through the issuance of a purported preferred mortgage to a trustee who is a citizen of the United States and issuance or transfer, without the approval of the Secretary of Commerce, to a person not a citizen of the United States, of a bond or bonds secured by the trust of such mortgage, if the foreclosure validity or preferred status of such purported preferred mortgage is in litigation on the date of enactment of this Act; and nothing in this Act shall be construed to alter retroactively the vested rights of any secured or unsecured creditor of the owner of such vessel, or of the vessel, if the foreclosure, validity

or preferred status of such mortgage is in litigation on the date of enactment of this Act. Within the meaning of this section, "citizen of the United States" means such citizen as defined in section 2 of the Shipping Act, 1916.

Senator BARTLETT. Thank you, sir. On page 9, Mr. Davis, referring to some decisions made in the 1920's, you said, "These earlier decisions had their shortcomings," and then later you went on to say, "They were in effect overruled in 1936 by the decision in the *Hudson River Day Line* case." What I am trying to learn is whether or not that statement is at all related to Mr. Kaplan's declaration to the committee the other day, and I quote again:

In 1949, without citing any authority whatsoever for the administrative change in interpretation and without referring to the aforementioned opinion, the Chairman of the U.S. Maritime Commission took the position that only the citizenship of the trustee need be considered and such citizenship is not affected by the ownership of the bonds secured by the mortgage.

Is there a relation?

Mr. DAVIS. Yes, there is a relation.

Senator BARTLETT. Then, can you explain to me how it was that in the 1936 decision it overruled the previous conclusions? It was not until 1949 that the Maritime Commission issued an opinion on this.

Mr. DAVIS. The question didn't come up, Mr. Chairman, between the time of the *Hudson Day Line* decision in 1936 to 1949, when the earlier decisions were overruled.

Senator BARTLETT. Now you have said that the earlier decisions had their shortcomings.

Mr. DAVIS. Yes.

Senator BARTLETT. And you have said that a conclusion was reached when the district court ruled in the *Hudson River Day Line* case. Mr. Kaplan, in response to several questions on this subject, said that there was no history whatsoever to indicate why the Chairman of the Maritime Commission acted as he did in 1949. He just did, without any supporting evidence or without any further explanation. Do you have anything to offer on that point?

Mr. DAVIS. That was before the Chairman, in 1949?

Senator BARTLETT. Right.

Mr. DAVIS. No; I don't have anything to offer on that. I have just recited to the committee the things that I regard as not having been considered in the 1920 decisions and court decisions that came about in 1936, after the 1920 decisions.

Senator BARTLETT. I understand that. But what I am trying to get at is whether these are your speculative reasons as to why he ruled as he did in 1949 or whether the files indicate that these might have been the reasons why he did as he did in 1949.

Mr. DAVIS. Mr. Chairman, I don't have any history that I could show you. In fact, the files do not show these factors which I have just recited to the committee were before the Commission when it made its change in 1949.

Senator BARTLETT. These would be your opinions.

Mr. DAVIS. These are my opinions; yes, sir.

Senator BARTLETT. All right. You said elsewhere that adoption of Mr. Meyer's amendment might lead to applications for mortgage insurance that would not otherwise be made. How would that hurt?

Mr. DAVIS. Well, because—well, there is a three-fourth-percent premium charge which is not otherwise applicable to American-flag ships,

and in addition to that—well, some of the mortgages which have been issued have been terminated. This would again require Government insurance, in essence where it would not be involved. About the only financing you will end up with is that supported by Government insurance.

Senator BARTLETT. I think it was both Mr. Meyer and Mr. Kaplan who submitted that the Congress should not move in here and intervene in a matter that is now before the courts, and a ruling has been made favorable to their interest, and that this is not correct procedure. Do you have any reply to that?

Mr. DAVIS. My response to that is that this is consistently done, frequently done under our system of Government and I don't see any objection to it.

Senator BARTLETT. If you were on the other side, you would see violent objection, I would assume.

Mr. DAVIS. Well, I might.

Senator BARTLETT. You said—

Mr. DAVIS. May I further amend that by saying that I think our statements in our prepared statements with respect to their wanting the advantage of a windfall is also applicable in regard to your statement here.

Senator BARTLETT. Who is going to get that windfall?

Mr. DAVIS. That could go one or two ways. It could go to the U.S. Government if the ship is forfeited or to secondary creditors if the ship is not forfeited. Creditors who contracted with the vessel, knowing at the time that there was a ship mortgage on the vessel.

Senator BARTLETT. You said, in your prepared statement, Mr. Davis, that if a mortgage should be in default and the trustee forecloses in a foreign court, he is, and I am saying your exact words, "Obligated to request the foreign court to follow U.S. law and sell the vessel only to a citizen of the United States." Would that be true, if you know, if this action were brought in a foreign court?

Mr. DAVIS. I don't know about—yes; it would be true that we would make such representations if this action were brought in a foreign court. I can say this: I do believe I am as qualified as anyone to testify on that point because I have handled many of these cases in foreign courts and not in one instance have I ever failed to get the foreign courts to comply with our law. This is including United Arab Republic, Port Said, Ceylon, India, France, Tokyo, Singapore, Israel, and Hong Kong.

Senator BARTLETT. Tokyo Rose involved in any of these proceedings?

Mr. DAVIS. I didn't find her as a party in interest, sir.

Senator BARTLETT. But your main point there in reference to that very situation is that this is rather immaterial anyway because you wouldn't have to go through that elaborate procedure because he would only have to buy the ship and turn it over to the alien.

Mr. DAVIS. That is right. Of course he would be subject to the sanctions just as the trustee would be subject to them.

Senator BARTLETT. That is all the questions I have. Thank you very much for your return appearance.

Mr. FOSTER. Just a couple of questions. Have you got a copy that you could make available to the committee of your latest letter opin-

ions on under what conditions you would need to get approval from the Maritime Administration when there is a sale to an alien?

Mr. DAVIS. Do we have a copy of our regulation covering that? Well, at any time there is a sale to an alien, you must get our approval.

Mr. FOSTER. Of bonds?

Mr. DAVIS. Not of bonds.

Mr. FOSTER. Let me be more specific. I understood from the hearings that the committee conducted last week on the matter that recently the Maritime Administration had answered the question as to whether or not the Maritime Administration needed to give approval when there was a sale to an alien bondholder.

Mr. DAVIS. Yes; I can furnish you with a copy of that.

(The information requested above follows:)

U.S. DEPARTMENT OF COMMERCE,
MARITIME ADMINISTRATION,
Washington, D.C., July 21, 1965.

HON. WARREN G. MAGNUSON,
Chairman, Senate Commerce Committee,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: As requested during the course of the July 15 subcommittee hearings on S. 2118, I am enclosing a copy of the Maritime Administration's letter of August 17, 1962, to Mr. Houston H. Wasson regarding the SS *Saint Christopher*, which letter is the latest of the letter decisions of the Maritime Administration to the effect that the mortgaging of an American-flag vessel to a mortgagee, trustee who is a citizen of the United States does not require the prior approval of the Maritime Administration under sections 9 and 37 of the Shipping Act, 1916, as amended (46 U.S.C. 808 and 835).

I hope that this letter will be of assistance to you.

Sincerely yours,

(S) CARL C. DAVIS,
General Counsel.

U.S. DEPARTMENT OF COMMERCE,
MARITIME ADMINISTRATION,
Washington, D.C., August 17, 1962.

Re SS *Saint Christopher*.

MR. HOUSTON H. WASSON,
Lovejoy, Morris, Wasson & Huppuch,
New York, N.Y.

DEAR MR. WASSON: Reference is made to your letter, dated August 16, 1962, in which you advise that the Beaverdam Tanker Co., Ltd., the Liberian owner of the Liberian-flag vessel *Saint Christopher*, proposes to sell the said vessel to a U.S. citizen corporation and document the same under the laws of the United States.

In connection therewith you request advice as to whether or not the prior approval of the Maritime Administration will be required under any law or statute administered by it, in order that the U.S. citizen-owner of the vessel may place a first preferred mortgage on the vessel in favor of the Marine Midland Trust Co., of New York, as mortgagee and trustee under a trust deed and a bond issue thereunder.

The Maritime Administration and the U.S. Bureau of Customs have ruled that in their opinion there is no reason, under the Ship Mortgage Act, 1920, as amended, why a mortgage naming a U.S. citizen-trustee may not be recorded as preferred because an alien named as beneficiary under a trust agreement does not meet the requirements for citizens set forth in section 2 of the Shipping Act, 1916, as amended (46 U.S.C. 802).

In this connection reference is made to section 30, subsection B(5) of the Ship Mortgage Act, 1920, as amended (46 U.S.C. 911), which provides that "the term 'mortgagee' in the case of a mortgage involving a trust deed and a bond issue thereunder means the trustee designated in such deed." The citizenship of the trustee is controlling. Under these circumstances such an arrangement would constitute the mortgaging of an American-flag vessel to a U.S. citizen-mortgagee,

and as such it would not require the prior approval of the Maritime Administration under sections 9 and 37 of the Shipping Act, 1916, as amended (46 U.S.C. 808 and 835). The proposed alien bondholders, in this case, Banque Francaise de Commerce Exterior, will not acquire any interest or control over the mortgage or the vessel and will not acquire any rights or interests other than those of a bondholder as set forth in the trust deed or indenture under which the bond or bonds is or are issued, these rights or interests being limited to the collection of the money paid for the bonds plus interest.

In the event that the U.S. citizen-mortgagee and trustee—namely, the Marine Midland Trust Co.—for any reason whatsoever should become possessed of the vessel under the trust deed or indenture, the approval of the Maritime Administration would be required before such mortgagee and trustee could transfer the vessel to any non-U.S. citizen-buyer or to the Banque Francaise de Commerce Exterior, the French Bank (46 U.S.C. 808 and 835). In this connection reference is made to section 30, subsection O (e) of the Ship Mortgage Act, 1920, as amended (46 U.S.C. 961) which provides that no vessel of the United States shall be sold by order of a district court of the United States in any suit in rem in admiralty to any person not a citizen of the United States.

The foregoing is not to be construed as an approval by the Maritime Administration that the above-described mortgage will be accepted for recordation and endorsement as a preferred ship mortgage by the U.S. Bureau of Customs. It is, therefore, suggested that you submit your proposal to the Bureau of Customs for an official ruling thereon.

Sincerely yours,

(S) GRAYDON L. ANDREWS,
Deputy General Counsel.

Mr. FOSTER. The committee was informed at that time that the position taken by the Maritime Administration was that there was no need unless the trust arrangement gave the bondholders control over the trustee mortgagee; is that correct?

Mr. DAVIS. Yes. There is a provision in there of the type that you are talking about, the purpose of the provision is to make it clear that the arrangement is a financing arrangement.

Mr. FOSTER. But you would, by having that provision in there, assume that there are certain types of trust arrangements in which the bondholders would have to be approved, is that true?

Mr. DAVIS. No. As long as they are citizen trustees, the law controls it.

Mr. FOSTER. Why would you have in your letter opinion that they do not need to be approved unless they have control?

Mr. DAVIS. Well, that was out of an abundance of caution.

Mr. FOSTER. Thank you, Mr. Chairman. Is it your opinion that it is possible, through the type of arrangement that was made in the *Westhampton*, to circumvent the requirement of the present law that the mortgagee be an American citizen, a U.S. citizen?

Mr. DAVIS. No. It would not be possible to circumvent, and, incidentally, the three ships involved in this instance is a good example of that.

Mr. FOSTER. You have pending litigation in foreign courts similar to the *Westhampton* case here in the United States?

Mr. DAVIS. Yes, involving the other two vessels and the requirement with respect to their sale has been imposed by the court, that they be sold to citizens of the United States and these are sister ships of the very ship we are talking about here. That is in Port Said and Bombay.

Mr. FOSTER. Thank you.

Senator BARTLETT. So the record will be complete, will you identify the gentleman with you?

Mr. DAVIS. Yes. This is Mr. John R. Tankard, Assistant General Counsel in charge of the Division of Mortgage and Marine Insurance. Senator BARTLETT. Thank you once more, gentlemen.

The committee will be in recess.

(Whereupon, at 10:35 a.m., the subcommittee was adjourned.)

(Various communications and letters received by the committee follow:)

DEPARTMENT OF STATE,
Washington, July 20, 1965.

Hon. WARREN G. MAGNUSON,
Chairman, Committee on Commerce,
U.S. Senate.

DEAR MR. CHAIRMAN: On July 8, 1965, the Embassy of the Federal Republic of Germany delivered an aide memoire, dated July 6, 1965, to the Department of State. This aide memoire concerns the decision of the Fourth Circuit Court of Appeals in the *SS "Westhampton"* case and the currently pending Senate and House bills (S. 2118 and H.R. 9494) relating to this matter.

The Embassy has requested that we bring to your attention its views, and we are accordingly forwarding to you, without comment, a copy of the aide memoire.

Sincerely,

DOUGLAS MACARTHUR II,
Assistant Secretary for Congressional Relations.

AIDE MEMOIRE OF THE EMBASSY OF THE FEDERAL REPUBLIC OF GERMANY,
WASHINGTON, D.C., JULY 6, 1965

The U.S. Court of Appeals for the Fourth Circuit, in the case of *SS "Westhampton"*, has recently ruled that bonds issued against a mortgage held by a New York bank being invalid because the bondholders being aliens and the transaction not having been approved by the Maritime Administration. In contrast to this opinion the Maritime Administration's regulations do expressly not require the approval.

The mortgagee and trustee is the Chemical Bank New York Trust Co. The bondholder is the Hamburger Landesbank, which has financed 70 percent of the cost of converting the vessel in a German shipyard. In the court's opinion the mortgage is not entitled to a preferred status in bankruptcy proceedings, this would mean that the bondholders would lose their money. The case is still pending; petition for reargument has been sought, it is also possible that the Supreme Court of the United States agrees to hear the case, if appealed.

Two other vessels, involved in the same bankruptcy, have been arrested in Port Said and Bombay. Their conversion has been financed by the Bremer Landesbank as bondholder. The trustee and mortgagee is likewise the Chemical Bank. The cases are pending before an United Arab Republic and an Indian court. These courts are expected to apply the respective U.S. laws; that would mean, that their decisions will directly depend on the final decision in the "*Westhampton*" case.

The court of appeals' decision arose, apart from the particular case, a general legal uncertainty and, subsequently, began to influence the market for ship mortgage bonds. To avoid a serious jeopardy for the U.S. merchant marine replacement program, a bill (S. 2118), was introduced to the Senate by Senator Bartlett. The proposed bill would assure the security of bondholders, whether foreign or American, by making certain amendments to the Shipping Act of 1916, and to the Ship Mortgage Act of 1920. By making the amendments retroactive, the bill assures an equitable treatment of the pending cases.

First hearings had been held on June 23. There was no opposition except to the retroactive feature, which was opposed, quite understandably, by the trustee for *Westhampton's* owner. Further hearings are scheduled later this month.

Meanwhile another bill (H.R. 9494) was introduced to the House of Representatives by Congressman Garmatz. This bill is in general similar to the bill mentioned above; but it carries a particular clause (sec. 5), stating that the act shall not have a retroactive effect. The supporters of this bill want to have it passed as soon as possible, in order to avoid any further interruption of their current ship financing. They are obviously not interested in the question of

retrospectiveness itself, but they fear that the passage of the bill S. 2118 could be delayed for this reason.

The Government of the Federal Republic of Germany would consider the bill H.R. 9494, if it passes, discriminatory and in contradiction to the Treaty of Friendship, Commerce, and Navigation, signed at Washington on October 29, 1954. The Government of the Federal Republic of Germany wants to inform the Department of State of its opposition to the bill and asks that its point of view should be brought to the attention of the agencies of the U.S. Government, committees, and Members of the U.S. Congress being concerned with this proposed legislation.

WASHINGTON, July 6, 1965.

DEPARTMENT OF STATE,
Washington, August 31, 1965.

HON. WARREN G. MAGNUSON,
*Chairman, Committee on Commerce,
U.S. Senate.*

DEAR MR. CHAIRMAN: On July 19, the Department forwarded to you a copy of an aide memoire, dated July 8, 1965, from the Embassy of the Federal Republic of Germany. This aide memoire concerned the decision of the Fourth Circuit Court of Appeals in the SS "*Westhampton*" case and two pending congressional bills (H.R. 9494 and S. 2118) on the subject.

On August 19, the Embassy of the Federal Republic of Germany delivered to the Department a note verbale, dated August 17, referring to their earlier aide memoire and commenting upon what appears to be a proposed pending amendment to S. 2118. In accordance with their request, we are forwarding to you a copy of this note verbale.

Sincerely yours,

DOUGLAS MACARTHUR II,
Assistant Secretary for Congressional Relations.

NOTE VERBALE OF THE EMBASSY OF THE FEDERAL REPUBLIC OF GERMANY,
WASHINGTON, D.C.

The German Embassy presents its compliments to the Department of State and has the honor to refer to the Embassy's aide memoire, dated July 6, 1965.

The German Government has been informed of certain developments of the pending legislation concerning the issue of bonds on ship mortgages. The general idea of such legislation (bills S. 2118 and H.R. 9494) has been to state that a bond issued under ship mortgage indenture was not "an interest in a ship under section 37 of the Shipping Act, 1916", and that, subsequently, no approval of respective transactions by the Secretary of Commerce (Maritime Administration) would be required. As the only but most important difference between the two bills H.R. 9494 has included an exclusionary clause which would provide that nothing in the proposed legislation should be construed to alter the rights of any creditor "in any legislation pending upon the effective date of this act". The German Government has regarded this clause as discriminatory and expressed its view in the aide memoire mentioned above.

Recently a new version of bill S. 2118 has been prepared. This draft adopts the rationale of the court of appeal in the *Westhampton* case that a bond is an "interest" in mortgaged property and consequently would permit the transfer of such interest only with approval of the Secretary of Commerce. The new draft would, however, permit the trustees to obtain the approval of existing bonds from the Secretary of Commerce within 1 year but states expressly that this provision shall not be applicable to bonds being in litigation.

In the view of the German Government this draft would have not only the generally discriminatory effect of the bill, H.R. 9494 but, by virtue of existing circumstances, is directed only against the three German banks involved in pending litigation concerning three American ships. (In the case of the fourth vessel, a sister ship of the *Westhampton*, financed by a virtually identical mortgage, the bond of which was held by a Greek bank, the mortgage was held valid by a U.S. district court, the Greek bank having been paid in full.) It would appear, under fundamental principles of law and justice, that if the retroactive approval of bond issuance will be applicable, then it should not exclude such in litigation because German banks are involved.

The adoption of such discriminatory amendment unquestionably would compound the adverse effect that the *Westhampton* decision already has had on the commercial relations of our two countries. The Government of Germany shares the frequently expressed views of the U.S. Government as to the mutual benefits to be derived from the free interchange of investment capital. But such benefits certainly cannot be attained by the enactment of discriminatory legislation against German banks who had acted in entire good faith, pursuant to advice and in accordance with the regulations of the Maritime Administration.

Finally the German Government should like to point out again that the intended alteration of bill S. 2118 would, like bill H.R. 9494, violate articles I paragraph 1, V paragraph 3, VII paragraph 2 and 4, and IX paragraph 2 of the Treaty of Friendship, Commerce and Navigation, signed at Washington on October 29, 1954. Therefore, it requests that the Department of State be kind enough to bring again the views herewith expressed to the attention of the Justice Department, the Maritime Administration, the House Committee on Merchant Marine and Fisheries, and the Senate Committee on Commerce, Subcommittee on Merchant Marine and Fisheries.

WASHINGTON, D.C., August 17, 1965

DILLON, READ & Co., INC.,
New York, August 17, 1965.

Re Senate bill 2118.

SENATE COMMITTEE ON COMMERCE,
U.S. Senate Building,
Washington, D.C.

(Attention of Senator Edward L. Bartlett).

GENTLEMEN: This letter supports the enactment of Senate bill 2118, an act written to clarify two shipping acts in order to eliminate questions as to the validity of certain obligations secured by mortgages on American-flag vessels.

The decision of the U.S. Court of Appeals for the Fourth Circuit dated April 5, 1965, in the case entitled *Chemical Bank New York Trust Company v. Steamship "Westhampton"* made the validity of a ship mortgage dependent upon the citizenship of the holder of each bond. In our opinion the above decision will impose serious limitations on the negotiability of ship mortgage bonds, and eliminate purchasers such as financial institutions, the citizenship status of which is unclear.

Our firm has placed ship mortgage bonds having a principal value of many millions of dollars with a number of financial institutions. Such investors require a high degree of certainty as to the validity of the ship mortgage. The existence of doubts created by the above decision will make obligations issued under trust indentures and secured by mortgages on U.S.-flag vessels unattractive when compared with alternative investments.

It is our understanding that S. 2118 would affect changes which would remove all doubts as to the validity of ship mortgage bonds without in any way affecting existing laws which require the trustee-mortgagee of U.S.-flag vessels to meet the citizenship requirements of existing U.S. shipping laws.

We therefore support the enactment of Senate bill 2118.

Very truly yours,

PETER M. FLANIGAN, *Vice President.*

BANK OF AMERICA,
NATIONAL TRUST & SAVINGS ASSOCIATION,
San Francisco, Calif., July 2, 1965.

Hon. E. L. BARTLETT,
U.S. Senate, Committee on Commerce, Subcommittee on Merchant Marine and Fisheries, Senate Office Building, Washington, D.C.

DEAR SENATOR BARTLETT: This letter is being written in support of Senate bill 2118.

Bank of America National Trust & Savings Association acts as trustee for, and its corporate trust division administers, numerous issues of title XI bonds secured by preferred ship mortgages on U.S.-flag vessels. It contemplates acting in this capacity in the pending American President Lines, Ltd., financing referred to by Mr. George H. Schreiner, vice president and treasurer of that company, in his testimony before this committee on June 23, 1965. It is also trustee for

bonds previously issued to finance construction of vessels soon to be delivered and on which valid first preferred ship mortgages must be placed.

The decision of the fourth circuit court in the "*Westhampton*" case holding that "a ship mortgage bond is an interest in the ship mortgaged" has created great uncertainty as to the validity of such preferred ship mortgages.

In common with other trustees, we have previously been advised that when all conditions precedent to the delivery of the bonds have taken place, including the determination of our own American citizenship, the bond purchaser receives an instrument secured as to payment by a preferred ship mortgage regardless of the number of holders or the status of their citizenship.

It has always been our position that holders of bonds issued under a trust indenture do not acquire a direct interest in the security as such. Their rights, in the event of default, being limited to the benefits accruing from the realization upon the security by the trustee in accordance with the indenture provisions.

As a result of the "*Westhampton*" decision it is our considered opinion that in the absence of remedial legislation clarifying the appropriate provisions of the Shipping Act, 1916, and the Ship Mortgage Act, 1920, the marketability and negotiability of ship mortgage bonds is gravely impaired and the interest cost to issuers will be greatly increased.

For these reasons, we strongly urge the speedy enactment of Senate bill 2118, and feel that it implements the clear intent of Congress to provide a readily acceptable method of financing the replacement of the U.S. merchant fleet.

Sincerely,

SAMUEL B. STEWART,

Executive Vice President and General Counsel.

FIRST NATIONAL CITY BANK,
New York, N.Y., June 18, 1965.

Re Senate bill 2118.

SENATE COMMITTEE ON COMMERCE,
U.S. Senate Building, Washington, D.C.

(Attention: Senator Warren Grant Magnuson, chairman).

GENTLEMEN: We write this letter in support of the enactment of Senate bill 2118, an act to amend several shipping acts to eliminate questions as to the validity of certain obligations secured by mortgages on American-flag vessels.

Our bank holds corporate obligations having a principal value aggregating many millions of dollars, which were issued under trust indentures, each providing that the security held thereunder by the trustee and which includes one or more mortgages of American-flag vessels, is held for the benefit of the holders of all of the obligations outstanding under such indenture. In some cases there may be only one other holder besides ourselves and in other cases there may be numerous holders.

We are advised that the U.S. Court of Appeals for the Fourth Circuit in a decision handed down April 5, 1965, in the case entitled *Chemical Bank New York Trust Company v. SS "Westhampton"* approved such trust indenture arrangements where a trustee-mortgagee satisfies the citizenship requirements of the U.S. shipping laws. However, we are also advised that a portion of the court's decision casts substantial doubt upon the validity of the underlying mortgage security unless each holder of the obligations issued thereunder can establish that he and all of his predecessors in the chain of title complied with such citizenship requirements. One of the purposes of providing for issues of corporate obligations under a trust indenture, even where such obligations are at the time of original issue held by a relatively small number of investors, is to afford a ready means of liquidating all or a portion of the investment at a future time should the circumstances of the investor so require. In our opinion, the decision of the court will impose serious limitations on the marketability of corporate obligations secured by mortgages of American-flag vessels.

The competition for investment capital of the kind required for financing the U.S. merchant marine is such that investors demand a high degree of certainty as to the validity of the underlying security. The existence of doubts such as those which are now widespread in the investment community as a result of the "*Westhampton*" decision has made and will continue to make corporate obligations issued under trust indentures and secured by mortgages of U.S.-flag vessels relatively unattractive as compared with other available secured investments.

It is our understanding that the changes which would be effected by Senate 2118 would restore U.S. ship mortgage financings to the investment status which they were thought to enjoy prior to the decision in the *Westhampton* case without in any way affecting the law which requires the trustees acting as mortgagees of American-flag vessels to meet the rigorous citizenship requirements of the U.S. shipping laws.

For the reasons stated we urge the early enactment of Senate bill 2118.

Very truly yours,

R. GRAHAM,

Vice President, Transportation Department.

LIFE INSURANCE ASSOCIATION OF AMERICA,
Washington, D.C., August 11, 1965.

Hon. E. L. BARTLETT,
U.S. Senate,
Washington, D.C.

DEAR SENATOR BARTLETT: Our association represents a number of life insurance companies which have substantial investments in the form of bonds and notes secured in some instances by Government-insured ship mortgages and in other instances by uninsured ship mortgages. By far the greater portion of such investments is secured by uninsured mortgages. Accordingly, we have been following with great interest developments in connection with this proposed legislation.

The original form of S. 2118 dealt satisfactorily with the problems created by the *Westhampton* case for life insurance company investors. Some of the suggested revisions of this bill would, we believe, create some very real problems. We would hope that legislation could be enacted which would eliminate the problems growing out of the *Westhampton* case, for the millions of dollars now invested in mortgages on American-flag vessels, whether made under the Government-insured program or otherwise.

We would be particularly concerned if this legislation were restricted either to future investments or to insured mortgages (whether future or existing). Legislation so restricted would not only fail to meet the problems for existing insured mortgages and for noninsured mortgages but would add to the uncertainties already created by the *Westhampton* case.

We understand that the argument has been made that uninsured ship mortgage bonds in registered form—the form in which such bonds are customarily acquired by insurance companies in direct placements—do not need the protection of the proposed legislation because such bonds are not transferable and hence are not subject to the risk of being acquired by noncitizens. There is no legal basis for this argument. Such registered bonds are freely transferable under the transfer provisions of the financing documents which do not require that transferees be U.S. citizens. Such registered bonds therefore need the protection of the proposed legislation to the same extent as nonregistered bearer bonds.

In summary we would hope that the bill would be effective both retroactively and prospectively and that it would cover both uninsured and Government-insured investments.

If we can be of assistance to you or your staff, I hope you will feel free to call upon us.

With best regards, I remain,
Sincerely,

WARREN G. ELLIOTT, *Assistant Counsel.*

METROPOLITAN LIFE INSURANCE CO.,
New York, N.Y., June 21, 1965.

Re S. 2118.

SENATE COMMITTEE ON COMMERCE,
U.S. Senate Building,
Washington, D.C.

(Attention of Senator Warren Grant Magnuson, chairman).

GENTLEMEN: Metropolitan Life Insurance Co. wishes to go on record in support of the subject bill, S. 2118.

Metropolitan has for many years made substantial long-term loans through the purchase of ship mortgage bonds to finance ship construction programs of U.S. companies engaged in American-flag operations.

For many years such institutional ship financing (including financing through preferred ship mortgages insured by the U.S. Government under title XI of the Merchant Marine Act, 1936) was feasible because of the availability, under the applicable U.S. shipping statutes, of an arrangement whereby the mortgagee under the ship mortgage was a trustee under a trust indenture, who was a citizen of the United States within the requirements of such statutes. So long as the trustee-mortgagee was a U.S. citizen the citizenship of the holder to whom the bond was issued or transferred was of no significance. This was the view held by the financial and shipping communities, as well as the Maritime Administration. In this situation Metropolitan frequently has participated with other institutional lenders in purchasing ship mortgage bonds issued under such indentures and placed privately with such lenders.

We understand that the U.S. Court of Appeals for the Fourth Circuit handed down a decision dated April 5, 1965, in the *Westhampton* case, holding that, while the private placement of the bond in a trust indenture-mortgage bond financing complies with such statutes, nevertheless, since "a ship mortgage bond is an interest in the ship mortgaged," if any bond is initially issued to or subsequently transferred to a noncitizen without prior Maritime Administration approval under section 37 of the Shipping Act, 1916, the bond is illegal and invalid and the validity of the underlying mortgage is adversely affected.

Institutional financing through ship mortgage bond issues requires, with complete certainty, as security for the bonds a valid preferred mortgage under the Ship Mortgage Act, 1920, as well as ready marketability of such bonds secured thereby. If the validity of the preferred ship mortgage can be put in jeopardy by the citizenship status of any individual bondholder, a situation would then exist which would raise serious questions as to the feasibility for institutional lenders to participate in such ship financing.

We believe that a practical solution to the problem raised by this *Westhampton* decision is to clarify the Federal statutes involved so that they will operate to the same effect as they were construed by the U.S. Maritime Administration as well as by the financial and shipping communities prior to the *Westhampton* decision.

We therefore favor the early enactment of bill S. 2118 and would request that your committee act favorably on this bill.

Very truly yours,

CHURCHILL RODGERS, *General Counsel.*

NEW YORK LIFE INSURANCE CO.,
New York, N.Y., June 22, 1965

Re bill S. 2118.

U.S. SENATE COMMITTEE ON COMMERCE,
Senate Building, Washington, D.C.

(Attention of Senator Warren Grant Magnuson, chairman).

GENTLEMEN: New York Life Insurance Co. writes this letter in support of the enactment of Senate bill 2118.

For many years our company and other investors have been purchasing bonds issued under trust indentures in reliance upon the rulings and views of the U.S. Maritime Administration that the citizenship requirements of the above mentioned acts would be satisfied whenever the indenture trustee-mortgagee was a U.S. citizen.

The language used by the U.S. Court of Appeals for the Fourth Circuit in the case of *Chemical Bank New York Trust Company, Trustee, Mortgagee v. SS "Westhampton"* is so broad and general in scope as possibly to impair the marketability of these bonds and future bonds of this character.

To remove the questions raised by this decision and to insure the continued confidence of investors in these bonds, we respectfully urge approval of S. 2118 by your committee and its enactment by the Congress of the United States.

Sincerely yours,

R. MANNING BROWN, Jr.,
Executive Vice President.

THE NORTHWESTERN MUTUAL LIFE INSURANCE CO.,
 Milwaukee, Wis., June 22, 1965.

Re S. 2118.

SENATE COMMITTEE ON COMMERCE,

U.S. Senate Building,

Washington, D.C.

(Attention of Senator Warren Grant Magnuson, chairman).

DEAR SIRS: The Northwestern Mutual Life Insurance Co. wishes to go on record in support of bill S. 2118.

Northwestern has over the years made substantial investments in ship mortgage bonds to finance ship construction programs of U.S. companies engaged in American-flag operations. These bonds have been issued under trust indentures in favor of U.S. corporate trustees and have been secured by preferred ship mortgages running to the trustee. In some instances Northwestern has been the sole investor and in other instances there have been a number of other bondholders.

We understand that the U.S. Court of Appeals for the Fourth Circuit handed down a decision on April 5, 1965, in the *Westhampton* case holding that a ship mortgage bond is an interest in the mortgaged ship and that, even though the trustee is a U.S. citizen, the initial issuance or subsequent transfer of a bond to a noncitizen, without prior Maritime Administration approval, invalidates the bond and the preferred status of the mortgage. This decision runs counter to a longstanding interpretation of the Ship Mortgage Act by the Maritime Administration as well as the settled views of the financial bar and the investment community.

Institutions doing ship mortgage financing must be able to be certain that the bonds which they hold will be secured by a valid preferred mortgage and will be readily marketable. If the validity of the mortgage can be put in jeopardy by the citizenship status of individual bondholders, which of course can change from time to time as transfers are made, it seems to us that we and other institutional lenders would have grave reservations about further participation in U.S. ship financing.

It is our belief that the changes proposed by S. 2118 would restore U.S. ship mortgage financing to the status which it was thought to enjoy prior to the decision in the *Westhampton* case. The bill would not change the requirement that the trustees acting as mortgagees of American-flag vessels would have to be U.S. citizens.

We therefore urge the early enactment of bill S. 2118 and respectfully request that your committee act favorably on the bill.

Very truly yours,

RICHARD F. MOONEY, *General Counsel.*

