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criteria set forth in this paragraph (b) *Provided, That:*

(i) The types of interest bearing securities and their terms and conditions are acceptable to the Maritime Administration;

(ii) All principal and interest of the interest bearing securities are unconditionally guaranteed in a form satisfactory to the Maritime Administration and neither the securities nor the obligation to pay interest on the securities is that of a party or a company related to the party within the meaning of section 482 of the Internal Revenue Code of 1954, as amended, and the regulations thereunder; and

(iii) The guarantor, which may be an affiliate of the party, must be either a person that has any unsecured securities with a credit rating of "Baa" or better if rated by Moody's Investors Services, Inc., or "BBB" or better if rated by Standard & Poor's Corporations, or a person whose commercial paper rated not lower than "Prime" by Moody's Investors Services, Inc. or "B" junior securities are rated in the highest grade by Moody's Commercial Paper Service or in one of the two highest grades by Standard & Poor's Corporations, and is otherwise acceptable to the Maritime Administration.

(4) *Common and preferred stocks.* The party or the party's trustee may invest in the following common and preferred stocks:

(i) Stock of domestic corporations which is fully listed and registered at the time of purchase on an exchange registered with the Securities and Exchange Commission as a national securities exchange and which would be acquired by prudent men of discretion and intelligence in such matters who are seeking a reasonable income and the preservation of their capital; and

(ii) Preferred stock of a corporation if the common stock of that corporation meets the requirements of this paragraph and if the preferred stock of such corporation would meet such requirements but for the fact that such preferred stock cannot be listed and registered as required because it is nonvoting stock.

(c) *Limitations on investments—(1) Interest bearing securities.* The value of securities of any one issuer held in the

Fund compared to the value of the total assets of the fund shall not exceed 10 percent in the case of non-governmental securities referred to in paragraph (b)(2)(i) of this section.

(2) *Common and preferred stock.* The value of common and preferred stock of any one issuer held in the fund shall not exceed 25 percent of the value of the total assets of the fund. In no case may more than 60 percent of the value of the total assets of the fund be invested in common or preferred stock.

(3) *Margin or short sale.* No interest bearing securities or common and preferred stock shall be purchased on margin or be sold short for the account of a fund.

(4) *Related company investments.* Funds shall not be invested in the interest bearing securities or common and preferred stock of the party or of a company related to the party within the meaning of section 482 of the Internal Revenue Code of 1954, as amended, and the regulations thereunder.

(5) *Subsequent investments.* If at any time the fair market value of the interest bearing securities or common and preferred stock in the fund is more than the limitations stated in this paragraph (c), any subsequent deposit to or withdrawal from the fund or investment made within the fund shall be made in such a way as tends to restore the fund to a posture in which the fair market values of such securities or stock do not exceed such limitations. Values of such securities and stocks shall be the fair market values as determined by the party on the last day of each semi-annual and annual reporting period.

[41 FR 4265, Jan. 29, 1976, as amended at 42 FR 34882, July 7, 1977; 43 FR 51636, Nov. 6, 1978; 55 FR 34928, Aug. 27, 1990]

§ 390.9 Qualified withdrawals.

(a) *In general—(1) Defined.* In accordance with section 607(f) of the Act, qualified withdrawals are those made from a fund in accordance with the agreement, but only if they are for:

(i) The acquisition, construction or reconstruction of a qualified agreement vessel;

(ii) The acquisition, construction or reconstruction of barges or containers

which are part of the complement of a qualified agreement vessel; or

(iii) The payment of the principal on indebtedness incurred in connection with the acquisition, construction or reconstruction of a qualified agreement vessel or a barge or container which is part of the complement of a qualified agreement vessel.

(2) *Tax aspects of a qualified withdrawal.* For the tax aspects of a qualified withdrawal, see section 607(g) of the Act and §3.6 of the joint regulations (§391.6 of this chapter).

(b) *Purpose of qualified withdrawals—*
 (1) *Acquisition of qualified agreement vessels.* (i) The term *acquisition of a qualified agreement vessel* shall mean any transaction, including a corporate merger, where the party obtains a proprietary interest in an existing vessel and such a proprietary interest will, in the opinion of the Maritime Administrator, further the purposes and policies of the Act. See §390.3 (relating to policy considerations).

(ii) Qualified withdrawals for the acquisition of a qualified agreement vessel shall only be allowed for amounts determined by independent appraisal to be the fair market value of the vessel, at the time of the acquisition, or the actual cost directly allocable to acquiring only the vessel, whichever is less.

(2) *Construction of qualified agreement vessels.* The term *construction of a qualified agreement vessel* shall mean the construction of a vessel with the aid of qualified withdrawals.

(3) *Reconstruction of qualified agreement vessels.* Once an agreement has been entered into, the term *reconstruction of a qualified agreement vessel* shall mean any improvement to an existing vessel which increases the vessel's competitiveness and involves an aggregate sum in excess of \$100,000. The Maritime Administrator may waive the monetary limit in this subparagraph in the case of small vessels.

(4) *Payment of principal on indebtedness.* Section 607(f)(1)(C) provides that any indebtedness which the party proposes to pay through qualified withdrawals must be shown to the satisfaction of the Maritime Administrator to have been incurred in direct connection with the acquisition, construction or

reconstruction of a qualified agreement vessel. The fact that indebtedness is secured by an interest in a qualified agreement vessel is insufficient by itself to demonstrate the direct connection. It is not necessary that the lien or mortgage securing the indebtedness be on the vessel. For example, if the party mortgages an office building in order to finance the construction of a vessel, payments of principal on the mortgage may be made with qualified withdrawals.

(c) *Limitations on qualified withdrawals—*(1) *Capitalized costs requirement.* All qualified withdrawals must be for costs which are capitalized under the Internal Revenue Code of 1954, as amended, and the regulations thereunder and so reported on the party's Federal Income Tax return.

(2) *Executed contract requirement and reimbursement of general funds.* Qualified withdrawals may be made for the purpose of reimbursing general funds subject to the following limitations:

(i) Qualified withdrawals may not be made until a construction, reconstruction or acquisition contract is executed. However, the party may reimburse its general funds for expenditures applicable to the construction, reconstruction or acquisition contract which occurred prior to the date of contracting if such reimbursements are made within 120 days from the date of such contracting.

(ii) The party may also reimburse its general funds for expenditures which could have been paid initially by a qualified withdrawal, if such reimbursements are made within 120 days of such expenditure.

(iii) The party may reimburse its general funds for expenditures made prior to the time an agreement or amendment is entered into, but after the party has made application therefor, if such expenditures would otherwise qualify for reimbursement pursuant to paragraphs (c)(3) (i) and (ii) of this section but for the fact that an agreement or amendment has not been executed, and if such reimbursement is effected within 120 days of the execution of an agreement or amendment.

(3) *Prepayment of indebtedness.* The party shall not prepay principal on indebtedness with qualified withdrawals

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without the prior written consent of the Maritime Administrator.

(4) *Qualified withdrawals paid to related persons.* A withdrawal, including payments for indebtedness, paid to a related person, within the meaning of section 482 of the Internal Revenue Code of 1954, as amended, and the regulations thereunder, shall not constitute a qualified withdrawal unless the Maritime Administrator determines that no portion of such payment constitutes a dividend, a return of capital or a contribution of capital under the Internal Revenue Code. Transactions which include payments to a related person, will be approved if the cost of the item to be acquired, constructed or reconstructed through qualified withdrawals is or was at the time of the acquisition, construction or reconstruction its fair market value. The party must obtain the prior written permission of the Maritime Administrator before any qualified withdrawals may be paid to a related person. Any such withdrawal prior to approval shall be a non-qualified withdrawal.

(d) *Permission to make qualified withdrawals.* Once a program has been approved, prior approval of the Maritime Administrator is not required for specific qualified withdrawals except as provided in paragraphs (c)(4) and (c)(5) of this section. However, the Maritime Administrator will give prior approval to qualified withdrawals upon written request.

[41 FR 4265, Jan. 29, 1976, as amended at 55 FR 34929, Aug. 27, 1990]

§ 390.10 Nonqualified withdrawals.

(a) *In general—(1) Defined.* Any withdrawal from a fund which is not a qualified withdrawal is a nonqualified withdrawal.

(2) *Tax aspects of a nonqualified withdrawal.* For the tax aspects of a nonqualified withdrawal, see section 607(h) of the Act and § 3.7 of the joint regulations (§ 391.7 of this chapter).

(b) *Permission required—(1) In general.* The prior written permission of the Maritime Administrator is required before a nonqualified withdrawal may be made.

(2) *Failure to secure permission.* A nonqualified withdrawal made without the prior written permission of the Mari-

time Administrator shall constitute a material breach of the agreement unless the Maritime Administrator shall determine that failure to obtain prior written consent was excusable. See § 390.13 (relating to failure to fulfill a substantial obligation under the agreement).

(3) *Types of nonqualified withdrawals which will be permitted.* Generally, the Maritime Administrator will give permission to make nonqualified withdrawals when:

(i) The party has incurred operating losses from the operations of agreement vessels which have impaired his working capital and it becomes necessary to reimburse its general funds to the extent of such losses;

(ii) The party desires to make an expenditure for research, development or design and such an expenditure is incident to new and advanced ship design, machinery and equipment;

(iii) The withdrawal would be a qualified withdrawal except for the fact that there is no tax basis left that can be reduced; or

(iv) The party demonstrates, to the satisfaction of the Maritime Administrator, that it cannot fulfill its program due to circumstances beyond its control or due to a change in circumstances which makes the completion of its program economically unfeasible.

§ 390.11 Sale or other disposition of agreement vessels.

(a) *Eligible agreement vessels.* The sale or other disposition (including mortgages) of eligible agreement vessels shall not require prior approval of the Maritime Administrator, but shall require written notification within 10 days after the sale or other disposition. Such notification shall include a description of the transaction, the identity of the transferee, the proceeds to be realized, the date of the transaction and whether the proceeds will be deposited into the fund.

(b) *Qualified agreement vessels—(1) In general.* If a qualified agreement vessel whose basis has been reduced through the application of qualified withdrawals is sold or disposed of (including mortgaged) within one year, interest on the amount of gain attributable to