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HR70-14

19 August 1950

MEMORANDUM FOR THE RECORD - COVERT COMBINATIONS COMMITTEE.

SUBJECT: Plan for the acquisition of the operating assets of C.A.T., Inc. (WTC), and the control and management of holding and operating companies established for this purpose.

History and Background:

1. This history of Civil Air Transport as begun and operated by General Chennault and Whiting Willauer is a complicated story. In an effort to simplify the terminology, the word "CAT" alone will be used to denote the operating facilities consisting of some 30 odd planes engaged in unscheduled freight operations in southeast China and between Hong Kong and Formosa under the direction of General Chennault and Whiting Willauer. "CAT Partnership" will refer to the working arrangement under which Chennault and Willauer operated CAT up to 5 February 1950. "C.A.T., Inc. (WTC)" will refer to the United States Corporation to which CAT facilities were transferred on 5 February, whose corporate name has now been changed to Willauer Trading Company (WTC). "CAT, Incorporated" will refer to the new CIA corporation which will purchase the assets and continue the operations of C.A.T., Inc. (WTC).

2. The originating point in the development of CAT is a Panama corporation known as EIC Cathay, S.A., a venture capital business established by the Corcoran brothers and William Youngman and their families at the end of the war. Thomas Corcoran had been connected with General Chennault off and on for some period of time. As the idea of the CAT operation developed, EIC Cathay decided to back the airline and permission was obtained from the Chinese Nationalist Government to operate a freight line, although that Government objected to an American corporation conducting such a business. Consequently, CAT Partnership was formed. It was, in a general way, the operating agent for EIC Cathay and beneficial interests in CAT Partnership were split among Chennault, Willauer, the Corcorans, Youngman, one Taylor, and some Chinese interests, with the greater bulk of the interest being in the Corcorans, Chennault, Willauer and Youngman.

3. CAT was profitable until at least the early spring and summer of 1949. As the Communist regime spread its control over China, CAT was forced to withdraw from post after post until in the summer of 1949 it maintained a thin bend of operations stretching from Kuning to southeast China to Hainan and Taiwan, with considerable business in Hong Kong and some business with such ports as Haifong, Hanoi and other large business centers. It was obvious at this time that there would be further restrictions on operations in China by reason of the spread of the Communist regime. Youngman is reported to have advised liquidation since

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at this time CAT could meet all its obligations including repatriation and bonuses for pilots and would still have valuable assets for disposition. Chennault and Willauer disagreed and attempted to continue the operation.

4. In the Fall of 1949, Corcoran became concerned at the possibility of the Communist regime asserting control over CAT assets. He therefore formed a corporation called Civil Air Transport, Incorporated, of Delaware, to which he could transfer CAT if it were necessary to establish title in the United States. However, in November 1949, Chennault and Willauer became involved in a collateral matter which arose out of the defection of the crews of China National Airlines Corporation and China Air Transport Corporation. These two airlines were corporate creatures of the Nationalist Government except for a 20% PanAm interest in CABC. To prevent these valuable air assets from going to the Communist regime by default, Chennault and Willauer entered into an agreement with the Nationalist Government and the corporate officers under the Nationalist Government to purchase CNAC and CABC giving in exchange therefor their personal notes except for a cash payment to PanAm to buy out its interest. Shortly thereafter Civil Air Transport Incorporated of Delaware was substituted for Chennault and Willauer as purchaser of these airlines and has since been attempting to gain control of the assets by legal proceedings in Hong Kong and in the United States.

5. CAT, meanwhile, has been obliged to reduce its operations from about 100 flying hours a month to the intermittent use of about 10 planes, and during the Fall of 1949, evacuated Hanking and other mainland stations. Evacuation costs and decreased revenues seriously impaired the working capital of the company and liquidation appeared inevitable. At this time OPC was faced with prospect of the loss of the only commercial airline in the Far East which could be utilized in the furtherance of OPC operations. Negotiations were therefore opened up which culminated in a contract between OPC and CAT under which OPC procured [redacted] carrier services in return for appropriate fees, and a commitment to underwrite net operating deficits up to [redacted] for the month of November and December 1949, and January 1950.

6. During this period, the owners of CAT became alarmed at the possibility that the Communist Government would attempt to seize CAT assets, and it was therefore determined to place title thereto in an American corporation. Accordingly, Corcoran formed C.A.T., Inc. (WTC), and on or about 5 February, the entire CAT business was transferred from CAT Partnership to C.A.T., Inc. (WTC).

7. With the fall of Shanghai and Hainan, CAT operations were reduced to minor flights on the island of Formosa, occasional flights between Hong Kong and Formosa and a charter flight to Tokyo. Willauer and Chennault began to explore commercial possibilities on the periphery of the eastern Asiatic coast in Korea, Japan, Philippines, Indo-China, Indonesia and Siam. As no immediate possibilities developed, the company

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fell into severe financial straits due to the heavy cost of maintaining the essential nucleus of the business. In March it looked as if there might be a forced liquidation which would mean sale of the assets. Such a sale, even through reputable brokers, very possibly would result in the assets passing to Communist control. Therefore, Willauer returned to this country to seek additional financial backing. OPC was presented with the problem that without further financial support bankruptcy of C.A.T., Inc. (WTC) was inevitable; the result of which would not only be the loss of C.A.T., Inc. (WTC) as an operational tool, but also the possible acquisition of the airline by the Communists. Accordingly, OPC induced Willauer to continue his attempts to seek new flight operations, and to preserve the corporation as a going concern. Through an agent, R. P. Dunn, of Washington, OPC agreed to support C.A.T., Inc. (WTC) operations through June 1950, and obtained an option to buy the assets of C.A.T., Inc. (WTC) on the following terms: To pay off current obligations of C.A.T., Inc. (WTC), Dunn's principals, CIA, hereinafter referred to as Dunn, loaned C.A.T., Inc. (WTC) [redacted], and agreed to advance [redacted] in working capital as needed during the months of April, May and June. In exchange, Dunn obtained an option to purchase the assets of C.A.T., Inc. (WTC) on or before 30 June, for an additional [redacted] in cash, thus in effect making the purchase price [redacted] if the option was exercised. The purchase price was negotiated largely on allegations made by Willauer, and OPC's appraisal of a rough itemization of the major properties.

8. It was understood that if Dunn exercised the option, he would form a new corporation to operate CAT, and would engage Willauer as the business head thereof and offer Willauer an opportunity to regain control on certain terms and conditions. The option was exercised effective 30 June, with final transfer of properties and payment therefor to be accomplished as rapidly as possible. The transaction involves the sale of all physical assets, franchises and goodwill of C.A.T., Inc. (WTC) to a new operating company without assumption of any liabilities accrued prior to 1 July 1950. For reasons of continuity of operations and ready transferance of goodwill, the new operating company was to be named CAT, Incorporated, and the name of C.A.T., Inc. was changed to Willauer Trading Company.

9. A second new corporation, [redacted] was to be substituted for Dunn and his undisclosed principals to act as a holding company of the stock of CAT, Incorporated, and to supply to the latter corporation both the initial capital to purchase the operating assets of C.A.T., Inc. (WTC), and subsequently the necessary working funds during the initial period of anticipated operating deficits.

Current Action - Holding Company

1. [redacted] has been properly formed and registered. This corporation will have two stockholders to whom the entire capital stock will be issued in return for [redacted] and assignment or conveyance to the corporation of the promissory note of C.A.T., Inc. (WTC), for [redacted], issued to R. P. Dunn, agent, and a release of indebtedness owed by C.A.T., Inc. (WTC) to R. P. Dunn in the amount of [redacted], and the executory contract held by Dunn to acquire the

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the assets of C.A.T., Inc. (WTC) as exercised by him. The value of these considerations totals [redacted] which is [redacted] in excess of the purchase price in order to provide the corporation with adequate funds for banking and credit purposes.

2. As a result of the proceedings will be an initial capitalization of [redacted] at [redacted] which [redacted] (100 shares) at stated value of [redacted] will be capital stock, and [redacted] will be paid-in surplus.

3. Termination of the Agency of R. P. Dunn, has been accomplished together with assignment of all of Dunn's rights as Agent for OPC to [redacted]

4. The assets required by the sale of [redacted] stock will in turn be sold, conveyed and assigned to CAT, Incorporated, the new operating company, in return for the issuance of its entire capital stock. Thus, by this procedure, the means has been provided to CAT, Incorporated to acquire the working assets of C.A.T., Inc. (WTC), and [redacted] becomes the holding company of CAT, Incorporated stock.

5. [redacted]

6. Three Directors have been elected by the above mentioned stockholders. In addition to themselves, a third Director was provided in order to ensure a quorum of Directors for any necessary corporate action. These Directors in turn have appointed themselves in the various corporate officer positions.

[redacted] This was done for several reasons.

7. An option has been granted by [redacted] to Whiting Willauer and James Brennan jointly, and with survivorship rights to purchase the entire capital stock of CAT, Incorporated, between the periods of 1 July 1952 through 1 July 1955, for the original purchase price to [redacted], plus any sums advanced or loaned to CAT, Incorporated [redacted] Mirdale. In effect, this option will enable the original owners

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of the CAT facilities (in the persons of Willauer and Brennan) to re-acquire the corporation at the total cost to the Government if it should become profitable to do so. This option is the result of negotiations between the Government and the principals of C.A.T., Inc. (WTC), and is based in part on the theory that the assets are actually worth more than [redacted] and that the Government is in effect taking "custodial control" for administrative policy and operational purposes. The existence of the purchase option will be made a matter of corporate records without disclosure of the basis or consideration involved.

Current Action - Operating Company

1. CAT, Incorporated, a new operating company, has also been organized in the State of Delaware. Its entire capital stock will be issued to Airdale Corporation in return for the considerations set forth in Paragraph 3, of the preceding section. The face value of these considerations will be capitalized as Capital Stock [redacted] (2,000 shares at [redacted] stated value) and Paid-in-Surplus of [redacted]

2. The Directors of CAT, Incorporated, as elected by [redacted] include the three Directors of [redacted] together with four other Directors in the field who occupy the positions of President, Executive Vice-President, Vice-President, and Treasurer. The first two of these field Directors, Whiting Willauer and James Brennan, are former employees of C.A.T., Inc. (WTC), and represent the experienced air-line operators.

[redacted] Provision has been made whereby three Directors constitute a quorum in order that such expeditious action as may be necessary can be accomplished either in the United States or in the field.

3. C.A.T., Inc. (WTC) has been informed of the assignment of the purchase option by Dunn [redacted] and hence to CAT, Incorporated, and of the intention of the latter corporation to exercise the option to purchase the operating assets of C.A.T., Inc. (WTC). The assignment has been concurred in by C.A.T., Inc. (WTC) and the purchase is to be consummated on 22 August 1952.

4. In order to ensure competent management, a management contract between CAT, Incorporated and Mr. Whiting Willauer has been consummated. The contract in so far as possible assures the managerial services of Mr. Willauer for a minimum period of two years with annual renewal options for a total period of 5 years. Mr. Willauer's compensation is set at [redacted] per year with provision for adjustment by reason of changes in the cost of living as indicated in the statistics of the Department of Labor

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labor. Provisions are also made for termination of the contract prior to completion of the first two year period upon payment of 75% of the compensation for the balance of the two years. Further, a death benefit of 3 months salary and a total disability benefit of 6 months salary has been provided.

5. It is anticipated that CAT, Incorporated will require substantial amounts of operating capital during an indefinite period of negligible or inadequate revenues. These funds will be provided by CIA up to a total which may be allocated by OPC for this purpose. They will be introduced into the holding company, Airdale, as loans from the two principal stockholders. Airdale in turn will advance or loan these funds to its wholly owned subsidiary, CAT, Incorporated. At the present time it is anticipated that these requirements will approximate [redacted] per month.

6. [redacted]

[redacted] By appropriate corporate action, all funds come under his control and the Treasurer or Assistant Treasurer or Chief Accountant must countersign all checks drawn by the other officers. In addition, the Treasurer has been specifically charged with the responsibility to establish an appropriate double entry bookkeeping system, and other accounting and administrative procedures to ensure full control of all assets, properties, and revenues. [redacted]

[redacted]
Secretary & Recorder

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