

The Jones Act:  
An Economic and Political Evaluation

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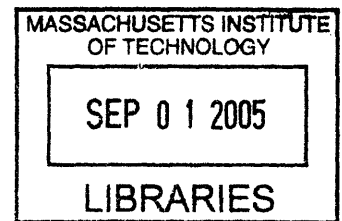
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# **The Jones Act: An Economic and Political Evaluation**

**By**

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**Submitted to the Department of Ocean Engineering  
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Requirements for the Degree of Master of Science in  
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## **Abstract:**

**On June 5, 1920, the Merchant Marine Act of 1920, also known as the Jones Act, became law. The Jones Act, a cabotage law, restricts American waterborne domestic trade to vessels flagged in the United States, owned by citizens of the United States, operated by citizens of the United States, and built in the United States. This highly restrictive law has become an integral part of American maritime policy. A brief history of the maritime policies of the United States and the Merchant Marine Act of 1920 is followed by an evaluation of the effects of the act on the maritime and shipbuilding industries, an evaluation of the effects on the American economy, and an evaluation of the political debate surrounding the act. Conclusions are made regarding the effects of the act and recommendations are made for the future of the act.**

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## **NOMENCLATURE**

<b>AFIA -</b>	<b>American Feed Industry Association</b>
<b>CDS -</b>	<b>Construction Differential Subsidy</b>
<b>CSCA -</b>	<b>Coastal Shipping Competition Act</b>
<b>DOT -</b>	<b>Department of Transportation</b>
<b>GAO -</b>	<b>General Accounting Office</b>
<b>GNP -</b>	<b>Gross National Product</b>
<b>ITC -</b>	<b>International Trade Commission</b>
<b>JARC -</b>	<b>Jones Act Reform Coalition</b>
<b>LASH -</b>	<b>Lighter Aboard Ship</b>
<b>LCA -</b>	<b>Lake Carriers' Association</b>
<b>LNG -</b>	<b>Liquefied Natural Gas</b>
<b>MARAD -</b>	<b>Maritime Administration</b>
<b>MCTF -</b>	<b>Maritime Cabotage Task Force</b>
<b>MSP -</b>	<b>Maritime Security Program</b>
<b>NDRF -</b>	<b>National Defense Reserve Fleet</b>
<b>NPV -</b>	<b>Net Present Value</b>
<b>ODS -</b>	<b>Operating Differential Subsidy</b>
<b>RO/RO -</b>	<b>Roll On/Roll Off</b>
<b>SNAME -</b>	<b>Society of Naval Architects and Marine Engineers</b>

## **Introduction**

Cabotage is a term that has become synonymous with the protection of a nation's internal maritime trade. In the United States that protection has been secured with the Merchant Marine Act of 1920, also known as the Jones Act. The Jones Act has never been without controversy. Proponents argue that the protections granted by the act secure a place for our national merchant marine for national defense and support our national maritime interests. Opponents argue that the act fails to sustain the goals of national defense and promotes and supports an inefficient industry leading to higher costs to the American economy. This paper seeks to delineate the arguments on both sides of the issue, to determine and understand what impact the Jones Act has on the maritime industry and the national economy, and to understand the politics surrounding the issue.

The term cabotage, derived either from the Spanish word *cabo*, which literally translated means "cape or promontory", or from the French word *caboter*, which literally translated means "to sail along a coast",<sup>1</sup> once meant navigation along a protected section of coastline or between two capes. The term grew over time to signify coastal voyages of greater distance, possibly requiring travel on the open sea.<sup>2</sup> In its modern and legal context, cabotage has come to denote the reservation of trade along a nation's coast to ships belonging to that nation's fleet.

The geographical makeup of the United States has made coastal trades a vital part of the nation's economy and culture. Due to this geographical distinction, the designation of coastal trade is not reserved merely to trade along a single coast, but has

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<sup>1</sup> "Definition of the word *Cabotage*," Available: <http://dictionary.reference.com/search?q=cabotage>

<sup>2</sup> Jantscher, Gerald R., *Bread upon the Waters: Federal Aids to the Maritime Industries*, The Brookings Institution, Washington D.C., 1975, pg. 45

come to represent national inter-coastal trade as well as trade between the mainland United States and Alaska, Hawaii, Puerto Rico and other territories and national possessions.<sup>3</sup>

These trades have been vital to the United States throughout its history and growth. Throughout that history and growth, the United States has enacted many measures of protectionism for the maritime industry and internal maritime trades. To fully understand the implications of the Jones Act and modern cabotage and protectionist laws it is important to understand the history which led to their enactment.

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<sup>3</sup> Jantscher, Gerald R., pg. 45

## **A Brief History of American Maritime Legislation**

International law has, for several centuries, recognized the right of nations to reserve internal and coastal maritime trade for their national fleets.<sup>4</sup> The United States, like many other nations throughout the world, has chosen to exercise this right and has enacted legislation to this end. Cabotage has remained one of the most important, and the most prevalent, forms of aid given to the maritime industry.

Cabotage, in the United States, can be traced back to the very beginning of the republic. During the colonial period of American history, mercantilism was the primary philosophy governing the economic growth of European nations and the acquisition of colonial possessions. Mercantilism focused on the importance of a nation's manufacturing capabilities with that nation's colonies serving as the source of the raw materials for production and the market for the sale of the finished products.<sup>5</sup> Nations garnered wealth under this system by sustaining a larger number of exports than imports. A key element to this strategy was to restrict trade to and from colonies to the mother nation.

In accordance with this strategy, England enacted various navigation acts designed to control trade with the colonies and to promote and foster the English merchant marine. These acts provided that goods imported into England could only be transported on English vessels, the product of any English colony could only be shipped to England or another English colony, and goods capable of being manufactured in

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<sup>4</sup> Jantscher, Gerald R., pg. 45

<sup>5</sup> Leback, Warren G. and McConnell, John W. Jr., "The Jones Act: Foreign Built Vessels and the Domestic Shipping Industry," SNAME Transactions, Vol. 91, 1983, pg. 170



England were not permitted to be manufactured in the colonies.<sup>6</sup> With these acts, we see the beginnings of a cabotage influence on the colonies.

Shipping and shipbuilding thrived in the colonies. The coastal location of the colonies, skilled colonists with strong maritime heritage, an ample supply of timber, and the relatively low wages led to a robust and economical industry.<sup>7</sup> A high quality American built ship, during colonial times, could be constructed for approximately £3-4 per ton, while a similar ship would cost £5-7 per ton in England. Due to these factors approximately one third of the English merchant fleet was built in the American colonies.<sup>8</sup>

However, after the colonies gained independence, the fledgling nation found itself in a position where its newly formed national merchant fleet had to contend with the British navigation acts that served to protect the English shipping industry. Many routes were now suddenly off limits to American ships as they were no longer part of the English empire.<sup>9</sup> It was seen that similar protections would be necessary for the new nation to protect the American maritime fleet and to pressure Great Britain and other European maritime powers into modifying or rescinding laws that excluded American ships from their trades.<sup>10</sup> Thomas Jefferson argued “that shipping and sea commerce is essential to American industry and economic balance and that the merchant vessel in times of war is the very core of successful naval and expeditionary operations.”<sup>11</sup>

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<sup>6</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 170

<sup>7</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 170

<sup>8</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, American Enterprise Institute for Public Policy Research, Washington D.C., 1985, pg. 4

<sup>9</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 4

<sup>10</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, Naval Institute Press, Annapolis, MD, 1983, pg. 2

<sup>11</sup> Cuneo, Joseph J., “U.S. Maritime Policy-A Perspective and a Plan for the Future,” *SNAME Transactions*, Vol.101, 1993, pg. 63

Thus, one of the first actions taken by the newly formed Congress was the passage of the Act of July 4, 1789. This act placed a tariff on all goods imported into the United States. However, in the spirit of protectionism, the act also discounted the tariff on the goods by ten percent if they were carried on American vessels.<sup>12</sup> Further restrictions were added sixteen days later with the Act of July 20, 1789. This act established standard tonnage duties that would be levied on any merchant ship entering an American port. Ships built and registered in the United States paid a duty of six cents per ton. Ships built in the United States but registered under a foreign flag paid a duty of thirty cents per ton. Ships built in a foreign nation and registered under a foreign flag were subject to a duty of fifty cents per ton.<sup>13</sup> Ships built in the United States and owned by United States citizens engaging in the coasting trade paid the tonnage duty only once a year while all other vessels paid the duty each time they entered a U.S. port.<sup>14</sup>

To be considered an American vessel and be eligible for preferential treatment under these regulations the Act of September 1, 1789 established that only vessels built in the United States and owned by United States citizens could registered for the coasting trade or fisheries under the United States flag and be considered an United States vessel.<sup>15</sup> However, foreign built vessels owned by citizens of the United States were eligible for registry under the United States flag if they were registered before May 29, 1789. Any ship built in a foreign nation after that date, regardless of ownership, was ineligible for registration in the United States.<sup>16</sup>

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<sup>12</sup> Labaree, Benjamin W., et al., *America and the Sea: A Maritime History*, Mystic Seaport Museum Inc., Mystic, CT, 1998, pg. 167

<sup>13</sup> Labaree, Benjamin W., et al., pg. 167

<sup>14</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 171

<sup>15</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 171

<sup>16</sup> Labaree, Benjamin W., et al., pg. 167

These early laws set the stage for protectionist legislation and for the future of cabotage laws. Some at that time demanded complete cabotage enactment by the Congress. Instead of completely excluding foreign shipping from the coastwise trade, however, Congress chose to enact the above tariffs. These effectively eliminated foreign vessels from the coastwise trade, the purpose of cabotage, by making it cost ineffective for foreign vessels to operate in the trade.<sup>17</sup>

Registration standards were further restricted by the Act of June 27, 1797. This was the first law to restrict registration among ships built in the United States. Under the terms of the act, no vessel registered under the United States flag which was thereafter seized, captured, or condemned by a foreign power, or was sold to a foreigner, was entitled to a new register, notwithstanding such ship shall afterwards be owned by United States citizens.<sup>18</sup> The law was further modified by the Act of March 27, 1804 which stipulated that a vessel could not maintain a United States registration if the owner was a naturalized United States citizen and resided for more than one year in his country of origin or for more than two years in any other foreign nation unless the owner was a public agent of the United States.<sup>19</sup>

None of these acts, however, established a legal prohibition against foreign ships operating in the United States coastal trades. This may have been due to an inadequate number of United States ships to support the domestic trade of the nation. Prohibiting foreign vessels would have been detrimental to the economic growth of the young nation, so the Congress opted instead for the duties, tariffs and registration restrictions.<sup>20</sup>

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<sup>17</sup> Labaree, Benjamin W., et al., pg. 168

<sup>18</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 171

<sup>19</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 171

<sup>20</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 171

The need to include foreign vessels in domestic trade did not persist. In 1817, economic and fleet conditions had changed, and Congress responded with the Act of March 1, 1817. The act excluded vessels owned by a foreign citizen from transporting merchandise from one port within the United States to another port within the United States. The act also encouraged transport upon vessels crewed by citizens of the United States by imposing a duty of fifty cents per ton on a United States registered vessel unless, in the case of trade originating in a foreign port, the officers and two thirds of the crew were United States citizens, for which no duty would be paid, or in the case of trade operating coastally, the officers and three fourths of the crew were United States citizens, for which the duty would be reduced to six cents per ton.<sup>21</sup> This law didn't restrict all coastal voyages to ships registered in the United States. An exception in the law permitted foreign vessels to move between United States domestic ports if it were to unload goods from abroad in one port and to load goods for a foreign destination in another domestic port.<sup>22</sup> This was the first example of a true cabotage law in the history of the United States.

This first cabotage law was considered by some to be a monumental success, largely responsible for the rapid and massive growth of the United States merchant fleet in the early part of the nineteenth century.

“With the protective umbrella provided by the 1817 Act, America’s coastal trade thus flourished during the decades preceding the Civil War. The ease of entry for American sailing vessels, coupled with the enforced absence of low-cost foreign competition in this trade, continued to attract new entrants to coastal shipping, so that by 1820 the coastwise fleet exceeded in size America’s large and expanding foreign trade fleet. With no government

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<sup>21</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 171

<sup>22</sup> Jantscher, Gerald R., pg. 46

restrictions or controls on their activity, shipowners enjoyed great flexibility in being able to shift their vessels freely from one branch of shipping enterprise to another, in order to take advantage of the constantly changing supply and demand for America's large variety of commodities."<sup>23</sup>

The United States foreign trade also flourished during this time, leading to a large and robust merchant fleet. The value of foreign trade cargo carried by ships registered in the United States increased from \$100 million in 1789 to \$687 million in 1860. This mirrored an increase in the percentage (by weight) of foreign trade carried by United States flagged ships from 23.6 percent in 1789 to 66.5 percent in 1860 with a high of 92.5 percent in 1826. The tonnage of the national merchant fleet grew from 667,000 tons in 1800 to 2,380,000 tons in 1860.<sup>24</sup> However, two technological developments, the use of steam in lieu of sails and the use of iron in lieu of wood, would threaten this prosperity.

The United States was slow to adopt these new technologies. American shipbuilders and shipowners had become complacent in their superiority with low timber and labor costs and better construction techniques allowing them to build higher quality-less expensive wooden sailing ships. As the 1860's began, American shipping involved in foreign trade began to see significant competition from British ships of iron construction and steam propulsion. The competition of these more advanced and more efficient ships forced American shipowners to seek other methods of cost reduction and improved productivity.<sup>25</sup>

Crew sizes and accommodations aboard American vessels were reduced. Working conditions deteriorated and many American seafarers left the industry, replaced by lower paid non-citizen workers. In response to the competition of lower cost foreign

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<sup>23</sup> Labaree, Benjamin W., et al., pg. 245

<sup>24</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 172

<sup>25</sup> Cuneo, Joseph J., pg. 65

vessels Congress passed an act in 1864 that removed all citizenship requirements for crews on American flagged vessels. This trend of men and capital moving away from the American merchant fleet reached an apex around the end of the 19<sup>th</sup> century with approximately ten percent of crewmembers aboard American vessels being of foreign citizenship.<sup>26</sup>

The United States was slowly becoming a high cost nation with respect to building and operating ships. Timber was becoming more expensive and less ideal. The shipping industry started to move away from wooden ships, leaving the United States behind. Further exacerbating the problem were statutes protecting the national iron and steel industries, which placed the higher quality and cheaper British products off-limits to American shipbuilders.<sup>27</sup> Ironical that a protectionist statute would in turn create a detrimental effect on the maritime industry.

On December 20, 1860, South Carolina seceded from the United States. The rest of the states comprising the Deep South followed on February 7, 1861.<sup>28</sup> Two months later, on April 12, 1861 the army of the confederate states opened fire on Fort Sumter in Charleston, South Carolina.<sup>29</sup> War had begun, and the United States merchant marine, as well as the nation as a whole, would succumb to dramatic change.

The once large and prolific American merchant fleet saw a dramatic decrease in size during the Civil War. Many ships were lost through war, but many others were lost through the effects of legislation. Due to the war and attacks on shipping by confederate forces, a large number of American vessels abandoned the American flag, easily done

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<sup>26</sup> Cuneo, Joseph J., pg. 65

<sup>27</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 2

<sup>28</sup> Davidson, James West, et al, *Nation of Nations: A Narrative History of the American Republic*, McGraw-Hill, New York, NY, 2001, pg. 480

<sup>29</sup> Davidson, James West, et al., pg. 482

due to the large percentage of crews that were of foreign citizenship. During the course of the war, nearly 1000 vessels left the American registry.<sup>30</sup>

The Act of June 27, 1797 prevented any of these ships from being repatriated back into the American fleet. The Act of February 10, 1866 reaffirmed this law and specifically prohibited any ship that transferred to a foreign flag during the war from being reregistered under an American flag. This resulted in the postwar fleet being approximately two thirds the size of the prewar fleet.<sup>31</sup>

Also passed by the same Congress was the Act of July 18, 1866, which required that any equipment purchased for, or the expense of repairs made in a foreign country upon, a U.S. vessel engaged in the foreign and coasting trade on the northern frontier of the United States be subject to an ad valorem duty of 50 percent on the cost.<sup>32</sup>

Following the depletion of the American merchant fleet and the growing dominance of British ships in the North Atlantic foreign trade, Congress reacted by enacting another form of aid to the maritime industry. The Act of March 3, 1845 encouraged involvement of the American fleet in the Atlantic packet trade by offering mail subsidies. More comprehensive mail subsidies were created with the Act of May 28, 1864 and the Act of March 3, 1891.<sup>33</sup>

“The theory was that guaranteed mail payments, in almost every case higher than actual cost of providing the service, would induce American operators to establish steamship service on certain designated routes. These early subsidy laws were, in part, justified by national defense considerations. The 1845 act, for example, stated that preference would be given bidders for mail contracts who promised to deliver their vessels to the U.S. government in

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<sup>30</sup> Cuneo, Joseph J., pg. 65

<sup>31</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 172

<sup>32</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 172

<sup>33</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 23

time of emergency. And the 1891 act stated that a mail-subsidized ship had to be convertible to a naval auxiliary and specified the type of the ship.”<sup>34</sup>

The national defense context of these laws is vitally important. Virtually all protectionist laws pertaining to the merchant marine, including cabotage laws, are presented and vigorously defended in a national defense context. Unfortunately, in this case the mail subsidies failed to halt the decline of the American foreign trade fleet. In 1910 only about nine percent of the nation’s foreign trade was carried on American flagged vessels.<sup>35</sup> This decline may have been associated with the inability of these subsidies to fully dissolve the prohibitive financial risk of ship ownership in the United States.<sup>36</sup>

Following the decline of the merchant fleet during the Civil War period there were many attempts at revitalization. These attempts were made using primarily three methods. First was the admission of foreign built vessels to the American registry. These ships were also known as “free ships.” Second was manipulation of the tax structure. Finally, subsidies were provided for American merchant vessels.<sup>37</sup>

Free ships remained a controversial issue.

“Those who argued for “free ships” advocated repeal of the nation’s basic Navigation Act of 1798. This allowed only wholly American-owned and American-built vessels to be registered in the American foreign trade. Free-ship advocates claimed that American shipbuilders could not build iron steamers in competition with the British. To attain their avowed goal, equipping the American commercial fleet with competitive vessels, the free-ship advocates demanded the admission of cheap-necessarily

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<sup>34</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 23

<sup>35</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 23

<sup>36</sup> Frankel, Ernst G., *Regulation and Policies of American Shipping*, Auburn House Publishing Company, Boston, MA, 1982, pg. 45

<sup>37</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 172



British-vessels to American registry. They claimed this would reverse a temporary trend and encourage American shipbuilders to meet the competition.”<sup>38</sup>

Thus the admission of free ships would run contrary to the spirit of virtually all of the legislation that had been enacted to this point in the nation’s history.

With regard to tax structure, the act of June 6, 1872 allowed materials to be used for the construction of wooden ships to be entered in bond and withdrawn without duties being paid. Unfortunately, the law did not foster competition with iron ships leading American industry away from the new technology by only supporting the construction of wooden ships.<sup>39</sup>

Many of the subsidy attempts resulted in scandal. One such example can be seen with the Pacific Mail Company. In 1874 it was discovered that the Pacific Mail Company spent millions of dollars in 1872 in efforts to renew its mail subsidy contract and that a portion of that money was spent on bribes. The Pacific Mail Company was able to remain in business, but its subsidy was immediately abrogated and resulted in the abandonment of subsidy legislation for several years.<sup>40</sup> In general, most of the revitalization efforts of the period failed.

There was also an important change in the cabotage laws of the period. In 1892, a change in the Act of March 1, 1817, arose from the court decision *United States v. 250 Kegs of Nails*. The case involved a ship transporting merchandise from New York to Antwerp on a Belgian vessel. The cargo was then discharged and reloaded on a British vessel and carried to San Francisco. The government brought a libel against the cargo.

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<sup>38</sup> Kilmarx, Robert A., et al., *America’s Maritime Legacy: A History of the U.S. Merchant Marine and Shipbuilding Industry Since Colonial Times*, Westview Press, Inc., Boulder, CO, 1979, pg. 69

<sup>39</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 172

<sup>40</sup> Kilmarx, Robert A., et al., pg. 71-72

The court stated that the Act of March 1, 1817 was “manifestly passed in the interest of American shipping, and to prevent foreign vessels from engaging in domestic commerce.” However, the court further stated that the Act of July 18, 1866 clearly indicated that Congress was aware of transshipments and only prohibited them to specific ports named, which did not include the ports involved in this case. The libel was dismissed.<sup>41</sup> To prevent this occurrence in the future, Congress passed the Act of February 15, 1893 which amended the prior cabotage laws. The law now specified that the transportation of merchandise in any foreign vessel from one port to another port of the United States “via any foreign port” shall be deemed a violation of the provision. A further amendment with the Act of February 17, 1898 prohibited transportation “either directly, or via a foreign port, or for any part of the voyage. Congress clearly stated its intent when it wrote, “the object of said bill is simply to carry out the intent of the Acts of 1792 and 1817 and the policy of the nation which has prevailed since the foundation of the Government, to restrict the coastwise trade of the United States to American vessels... and to remedy this difficulty [pointed out in the Kegs and Nails case]...and to maintain the policy of the nation.”<sup>42</sup>

During the 1890’s the Wrecked Vessel Act of 1852 was amended so that vessels wrecked anywhere, not just in the coastal waters of the United States, could be registered under an U.S. flag if repaired in a U.S. shipyard. The act was opposed, however, by U.S. shipyards and some U.S. operators because it lifted some of the protections granted to U.S. ships, even though the act required that repairs of at least three times of the value of

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<sup>41</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 172

<sup>42</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 172

the ship be made in a U.S. shipyard.<sup>43</sup> Despite the objections of industry, 350 vessels were registered in the United States under the revised act from 1894 to 1904. The provision allowing wrecked vessels to be repaired and registered in the United States was repealed in 1906. The law of 1852 was then reenacted and revised in 1915.<sup>44</sup>

The Act of March 3, 1897 repealed the rule that a U.S. flag vessel sold to a foreigner cannot be registered under the U.S. flag if it later becomes American property. It was stipulated, however, that the ship could not have undergone any change in build outside the United States. This act also repealed the law that a vessel would lose its register in the United States if the owner was a naturalized citizen residing in a foreign country.<sup>45</sup>

Then, on April 20, 1898, Congress insisted on the withdrawal of Spanish forces from Cuba and authorized President McKinley to use military force if necessary.<sup>46</sup> The United States was once again at war. Though the war was short, it was global in scale, with battles fought in Cuba and the Philippines. Due to the global nature of the conflict, it was necessary to transport large numbers of men and supplies with ships. However, the United States didn't have the merchant fleet needed to meet this sudden demand.

“...The Spanish American War of 1898 which, although very short in duration, necessitated that the United States charter a substantial number of foreign vessels to transport American soldiers and material to Cuba and the Philippines. One direct effect of the war was to revitalize interest in an American merchant marine as an essential link to protect American economic interests...”<sup>47</sup>

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<sup>43</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 172

<sup>44</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 172

<sup>45</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 172

<sup>46</sup> Davidson, James West, et al., pg. 695

<sup>47</sup> Cuneo, Joseph J., pg. 65

The necessity to charter foreign vessels to serve American military interests also signified the need for a national merchant marine for national defense. In recognition of this need, the first cargo preference law was passed in 1904. The act stated that “...transportation of coal, provisions, fodder, or supplies of any description...for use of the Army and Navy” was reserved for vessels of the United States granted that such vessels were available unless the President determined the freight rates were excessive.<sup>48</sup>

The Act of August 24, 1912, also known as the Panama Canal Act, extended the privilege of American registry to ships built in a foreign shipyard with the stipulation that the ship could not participate in the coastwise trades.<sup>49</sup> The law further stipulated that the ship could be no more than five years old to receive an American flag. This statute also provided rules regarding the ownership of a vessel by a corporation. The corporation “must be organized and chartered under the laws of the United States or of any State thereof and the president and managing director of which must be citizens of the United States.”<sup>50</sup>

The 1912 act was modified in 1914 eliminating the provision that required a ship to be more than five years old to receive an American registry if it was foreign built. Thus, so called “free ships” could be entered into the foreign trades under the American flag.<sup>51</sup> The coastal trade in the United States was temporarily opened to foreign-built vessels during World War I. In 1917 Congress passed a law allowing the United States

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<sup>48</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 23

<sup>49</sup> Jantscher, Gerald R., pg. 47

<sup>50</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 173

<sup>51</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 173

Shipping Board to suspend the prohibition against foreign-built vessels for the duration of the war and for a period of up to 120 days following the end of the war.<sup>52</sup>

At the outbreak of World War I, the American merchant fleet had dwindled to a point that it no longer had sufficient capacity to meet the needs of the nation for military transportation or trade. This led to the passage of the Shipping Act of 1916, which permitted the creation of the Emergency Fleet Corporation to carry out a shipbuilding and ownership program in support of the nation's war effort.<sup>53</sup>

The Shipping Act of 1916 also created the United States Shipping Board with five commissioners, authorized liner or conference agreements with the requirement that rates had to be published and made available to shippers and that unfair practices were prohibited, and prohibited ships from being purchased from a nation at war. This strong support for the merchant marine led to the production of 1,409 merchant vessels.<sup>54</sup>

Though the discriminating duties of 1789 were repealed in 1815, they were reenacted in 1913 as part of a general tariff reduction. However, a five percent additional reduction was permitted on goods imported on vessels flagged in the United States. This preferential reduction for American flagged ships was later nullified due to reciprocity provisions in various treaties. The discriminating duties were repealed in 1915.<sup>55</sup>

The end of World War I brought a large surplus in government-owned merchant vessels. The disposal of the surplus ships presented a serious problem to the United States Shipping Board. Congress' response to the slow disposal of ships under the provisions of the Shipping Act of 1916 was the Merchant Marine Act of 1920, also

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<sup>52</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 173

<sup>53</sup> Frankel, Ernst G., pg. 45

<sup>54</sup> Heine, Irwin M., *The U.S. Maritime Industry: In the National Interest*, National Maritime Council, Washington D.C., 1980, pg. 5

<sup>55</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 173

known as the Jones Act.<sup>56</sup> This act is also of great importance because it is the source for the nation's cabotage laws today. The Merchant Marine Act of 1920 is the primary focus of this thesis and will be discussed in much greater detail in the following section, "The Merchant Marine Act of 1920."

Disappointed with the pace at which a private American merchant fleet was developing, Congress passed the Merchant Marine Act of 1928. The act gave the United States Shipping Board the authority to repair vessels with the stipulations that the vessels be documented under U.S. laws for a minimum of five years following repair and that they could not operate on exclusively coastwise voyages.<sup>57</sup> The construction loan fund created under the 1920 act was increased to \$250 million.<sup>58</sup> The Ocean Mail Act of 1891 was repealed, mail contracts were made conditional on replacement of old tonnage, and all officers and two thirds of the crew serving on vessels contracted for mail service were required to be citizens of the United States.<sup>59</sup> The act also required that government officials travel on American flagged ships.<sup>60</sup> However, many of the act's loosely worded provisions led to scandal and a Senate Select Committee report of the early 1930's suggested an end to all assistance provided to ship operators.<sup>61</sup>

In a message to Congress in 1935, President Franklin Roosevelt proposed that cost difference between American and foreign construction, repairs, wages, insurance, and subsistence, be paid by the federal government. Eligibility for these subsidies was restricted to liner vessels engaged in foreign trade. In return, ship operators were

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<sup>56</sup> Heine, Irvin M., pg. 5

<sup>57</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 177

<sup>58</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 177

<sup>59</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 26

<sup>60</sup> Heine, Irwin M., pg. 7

<sup>61</sup> Cuneo, Joseph J., pg. 66

obligated to build and repair their vessels in the United States, offer a specific number of sailings of designated trade routes designated as “essential” to national interest, adhere to minimum manning and wage scales and working conditions, and submit plans for subsidized construction to the Department of the Navy for review.<sup>62</sup> President Roosevelt’s proposals were considered by Congress and incorporated into the Merchant Marine Act of 1936.

The act required a subsidized operator to deposit a sum equal to the annual depreciation charge on his vessels and insurance indemnities into a capital reserve fund. Subsidized operators were also to deposit earnings in excess of ten percent and earnings in excess of the percentage allocated to the capital reserve fund in a special reserve fund. The first fund was to provide insurance for vessel replacement and to insure the long-term viability of a national subsidized merchant fleet. The second fund was to partially repay the government for subsidies during periods when the ship operator was making above average returns on investment. Both of these funds were exempt from federal taxes.<sup>63</sup>

The act also provided for construction subsidies of up to 33 1/3 percent but allowed the United States Maritime Commission to approve subsidies as great as 50 percent.<sup>64</sup> In 1938 the act was amended to include Title XI which created a fund to insure the payment of the interest on and the unpaid balance of the principle of any obligation for financing construction, reconstruction or reconditioning of a vessel owned by American citizens designed for domestic or foreign trade.<sup>65</sup>

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<sup>62</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 26-27

<sup>63</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 27

<sup>64</sup> Cuneo, Joseph J., pg. 67

<sup>65</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 177

After the passage of the Merchant Marine Act of 1936, the newly formed Maritime Commission set on a construction campaign that envisioned the construction of 50 new ships in American shipyards each year for a period of ten years. With Europe on the brink of war, and a strong possibility that the United States would be drawn into conflict, the program quickly modernized existing shipyards, built new yards, and produced 4,976 ships between 1939 and 1946.<sup>66</sup>

When World War II ended it was estimated that there would be approximately 58,000,000 deadweight tons of government owned merchant vessels suitable for commercial operation. Approximately 19,000,000 deadweight tons were considered to be “preferable” vessels and approximately 39,000,000 deadweight tons were considered less-desirable but still suitable. It was also estimated that the postwar foreign and domestic commerce of the United States would support an American merchant marine of approximately 15,000,000 deadweight tons.<sup>67</sup> To dispose of this massive buildup of ships, Congress passed the Merchant Ship Sales Act of 1946.

One of the important considerations addressed by the bill was the price at which the ships should be sold. There were three primary factors that were applied to determine the appropriate “statutory sales price.” First, a comparison was made between wartime construction costs and prewar construction costs. Second, account was taken of the fact that construction differential subsidies were available for vessels constructed in the United States for foreign service. Finally, the price should be set to place the largest number of ships that could be efficiently operated with private operators without setting

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<sup>66</sup> Heine, Irwin M., pg. 10

<sup>67</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 177



the price so low that it would adversely affect the future stability of the United States merchant marine.<sup>68</sup>

A problem arose during the war with regard to domestic shipping, which the act attempted to address.

“The question of sales of such vessels to operators engaged in the domestic trades indicated the tremendous obstacles faced by these operators in restoring the prewar domestic operations. During the war the movement of goods by water in domestic commerce had completely stopped and traffic which in the prewar years had moved by water was then moving for the most part by rail. Due to the uncertainty of the future in domestic water commerce, operators formerly engaged in that trade were hesitant to make large capital investments in ships.”<sup>69</sup>

To address this problem a price equal to 50 percent of the prewar domestic construction cost was set as the “statutory sales price” so that it would be competitive with the construction cost in foreign yards. The only exceptions to this were the statutory sales price of tankers which was set at 87 ½ percent and that the price of each ship was subject to certain changes to fit the particular vessel sold. A floor price was also established below which no sale could be made after adjustments. Older vessels could be traded in for the newer war-built vessels. Adjustments were to be made in the sale price of any vessel sold prior to the enactment of the act; and any vessel sold or chartered to a citizen of the United States would not be prohibited from participating in the domestic coastwise trade because of foreign registry if it was otherwise qualified for the coastwise trade. Under these terms, 1,956 vessels were sold, 843 of them to American citizens.<sup>70</sup>

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<sup>68</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 178

<sup>69</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 178

<sup>70</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 178

The remainders of the 1,956 ships sold were sold to allies to aide in the replenishment of their national shipping fleets.

The act also provided for a National Defense Reserve Fleet to be composed of ships that were not sold or scrapped for use in national emergencies and further emphasized the need for a national merchant fleet to maintain national security.<sup>71</sup>

In 1951, Congress appropriated \$350 million for the construction of the Mariner class dry cargo vessel. The money was to be used to build 35 vessels in seven different American shipyards. U.S. operators bought 29 of these vessels for use in the foreign trades at a price generated on the basis that the ships had been built with construction differential subsidies. However, none of these ships was purchased for use in the domestic trades because of a stipulation that any ship purchased for the domestic trades would be sold at full construction price.<sup>72</sup>

The Merchant Marine Act of 1936 was amended in 1952 to permit vessels in the domestic, as well as foreign, trade to be traded in to the government as a trade-in payment on the construction cost of a replacement vessel. The amendment also allowed a domestic operator to create a construction reserve fund for the construction, reconditioning, and purchase of new vessels.<sup>73</sup>

In 1954 Congress passed a law that required 50 percent of the gross tonnage of equipment, materials or commodities procured, furnished or financed by the United States to be transported on privately owned U.S. commercial vessels if available at reasonable rates. The law could, however, be temporarily waived by Congress, the President, or the Secretary of Defense in case of national of emergency. The law was

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<sup>71</sup> Heine, Irwin M., pg. 11

<sup>72</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 178

<sup>73</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 178

later amended in 1961 to specify “privately owned United States-flag commercial vessels” to exclude any vessel built or rebuilt outside the United States or registered under a foreign flag until the vessel had been registered under the laws of the United States for a minimum of three years.<sup>74</sup>

The Merchant Marine Act of 1970 was another attempt to revitalize the national merchant fleet. In 1969, the average age of a ship in the national merchant fleet was 20 years. It was seen that many of the ships were nearing the end of their service life and would need to be scrapped. To encourage the construction of new vessels Congress passed the Merchant Marine Act of 1970 and President Richard Nixon signed the law on October 21, 1970.<sup>75</sup>

The act consolidated reserve funds and special reserve funds into a single capital construction fund.<sup>76</sup> Earnings placed in this fund by American companies in foreign, Great Lakes, and noncontiguous trades were eligible for tax deferment, a privilege previously reserved only for subsidized operators.<sup>77</sup> Bulk carriers and reconstructed vessels were made eligible for differential subsidies and tankers and liquefied natural gas (LNG) carriers were made eligible for construction subsidies.<sup>78</sup> The act set a subsidy ceiling of 35 percent to be reached by 1976. This measure of the act failed with the exception of LNG vessels which had an initial subsidy of 15 to 25 percent, and was eventually eliminated for later built vessels due to the ability of the LNG vessels to compete in the international market.<sup>79</sup>

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<sup>74</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 178

<sup>75</sup> Heine, Irwin M., pg. 14

<sup>76</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 27

<sup>77</sup> Heine, Irwin M., pg. 14

<sup>78</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 27

<sup>79</sup> Cuneo, Joseph J., pg. 68

Another substantial goal of the act was to further the development of the American shipbuilding industry by authorizing the construction of 300 vessels over a period of ten years. However, only 89 vessels were constructed and fewer still were either tankers or bulk carriers.<sup>80</sup>

The act also tried to control the high costs associated with supporting the American merchant marine. Crew size was determined during the design and construction phases instead of once the ship was in operation. Negotiated contracts were allowed. An upper limit was set on subsidy payments. Wages were indexed.<sup>81</sup>

Further provisions of the act increased the allowable amount of Federal Ship Mortgage Insurance on ships to \$3 billion from \$1 billion, created a seven-member Commission of American Shipbuilding to make recommendations for improving the productivity and competitiveness of American shipyards, and attempted to phase out foreign flag operations of American shipowners who participated in the shipbuilding program.<sup>82</sup>

Congress passed a law in 1981 which permitted operators receiving operating differential subsidies to construct, reconstruct, or acquire vessels built abroad until September 30, 1983, if there were no construction differential subsidies available. These vessels, if registered under the American flag, would be eligible for operating differential subsidies and to carry preference cargoes. The provision would only be effective after September 30, 1982 if construction differential subsidy funds were requested for 1983. No such requests were made, but twelve American operators requested, and were

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<sup>80</sup> Cuneo, Joseph J., pg. 68

<sup>81</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 27

<sup>82</sup> Heine, Irwin M., pg. 14-15

approved, to reconstruct, convert, or retrofit 50 ships in foreign shipyards under the terms of this law.<sup>83</sup>

On September 24, 1996, Congress passed the Maritime Security Act and President Clinton signed the bill into law on October 8, 1996. Under the terms of this legislation the Maritime Security Program was established with the goal of providing sustained sealift capabilities at a minimal cost for times of national emergency.<sup>84</sup>

“Under the Maritime Security Program (MSP), the government contracts with the owners of U.S. flag commercial ships for service when needed for national emergencies or war. This approach avoids the need to spend billions of dollars to acquire additional cargo ships dedicated solely to carrying military cargoes, and the millions of additional dollars required to maintain more standby vessels.

“The MSP maintains a modern U.S. flag fleet providing military access to vessels and vessel capacity, as well as a total global intermodal transportation network. This network includes not only vessels, but logistics management services, infrastructure, terminals and equipment, *communications and cargo-tracking networks*, 20,000 well trained, professional U.S. citizen seafarers, and 22,000 shoreside employees located throughout the world.”<sup>85</sup>

A total of 47 vessels participate in the Maritime Security Program including: eighteen large containerships, eighteen medium containerships, three LASH (Lighter Aboard Ship), and eight car/truck carriers. These ships provide the military with a total cargo capacity of 118,000 TEU (twenty foot equivalent unit) or 10.4 million square

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<sup>83</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 178

<sup>84</sup> MARAD, “Maritime Security Act: Meeting National Sealift Needs,” Maritime Security Program Brochure, April 2000. Available: <http://marad.dot.gov/Programs/msp/Brochure%20-%20Traditional.pdf>

<sup>85</sup> MARAD, Maritime Security Program Brochure

feet.<sup>86</sup> The funding for these ships provided by the act is approximately \$100 million, representing approximately thirteen percent of the cost of operating U.S. flag vessels.<sup>87</sup>

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<sup>86</sup> MARAD, Maritime Security Program Brochure

<sup>87</sup> MARAD, Maritime Security Program Website, Available: <http://marad.dot.gov/Programs/MSP.html>

## Protectionism at Home and Abroad

It is important to recognize that protectionism is not unique to the United States and that cabotage and other similar laws exist in other nations throughout the world. The following table displays other nations in the world with cabotage or protectionist laws for their domestic fleets and what type of laws they have in effect.

<b>NATION</b>	<b>Cabotage</b>	<b>Fleet Subsidies</b>	<b>Crewing Requirements</b>	<b>Ownership Requirements</b>	<b>Domestic Construction Provisions</b>	<b>Reflagging Restrictions</b>
U.S.	Y		Y	Y	Y	Y
Algeria	Y	1	Y	Y		1
Argentina	Y	4	Y	Y		5
Australia	Y	4	Y			
Bahamas	Y	Y	Y	Y		1
Belgium		Y	Y			
Brazil	Y	Y	Y	Y	Y	Y
Bulgaria	Y	4	Y	Y		
Canada	Y		Y	3		5
Chile	Y	4	Y	Y		Y
China	Y	4	Y	Y		Y
Colombia	Y		Y	Y		5
Cyprus						1
Denmark	2	4	Y	Y		5
Ecuador	Y	4	Y	Y		1
Egypt	Y		Y	Y	3	5
Finland	Y		Y	Y		1
France	Y	Y	Y	3		1
Germany	Y	Y	3			5
Greece	Y		Y	Y		1
Honduras	Y		Y	Y		1
Hungary	Y	Y	Y	Y		5
India	Y		Y	Y		1
Indonesia	Y	4	Y	Y	Y	Y
Israel						1
Italy	Y	4	3			5
Ivory Coast	2	4	Y	Y		
Japan	Y	Y	Y	Y		5
Kenya						1
Malaysia	Y	4	Y	Y		1
Malta	Y		3			5
Mexico	Y	Y	Y	Y		1
Netherlands	2	Y	3	Y		1

New Zealand	Y		Y	Y		
Nigeria	2	Y	Y	Y		1
Norway	2	Y			Y	1
Panama	2					
Peru	Y	Y	Y	Y	Y	5
Philippines	Y		Y	Y		1
Poland	Y			Y		5
Romania	Y	Y	Y	Y		5
Saudi Arabia	Y			Y		1
Singapore						1
South Africa						1
South Korea	Y	Y		Y		Y
Spain	Y	4	Y	1	Y	1
Sweden	Y		3	Y		
Taiwan	Y	1	Y	1	1	1
Thailand	Y		Y	Y		5
United Kingdom	2	4	Y			
Uruguay	Y		Y			1
USSR	Y	Y	Y	Y	1	1
Venezuela	Y	Y	Y	Y		5
Yugoslavia	Y	Y	Y			5

Y = Yes      Blank = No  
 1 = No information provided  
 2 = Countries that do not exclude foreign vessels but do have certain restrictions  
 3 = No formal requirement, but some minor restrictions  
 4 = Indirect benefits provided  
 5 = Reflagging allowable, but controlled

**Table 1: National Flag Preferences in Domestic Trade Around the World<sup>88</sup>**

So the United States is certainly not unique in having protectionist laws for its domestic merchant fleet. All of the nations included on this list met at least one of the following criteria: 1) An oceangoing fleet of at least 50 national flag vessels of 1,000 deadweight tons or more, 2) Coastal shores connecting to international waters, 3) An established government without major armed conflict which maintains diplomatic relations with the United States and, 4) MARAD had some political or commercial interest in the nation. When the nations included in this list were asked what policy their maritime policies served, they responded with some of the following statements: “to

<sup>88</sup> MARAD, “By the Capes Around the World: A Summary of World Cabotage Practices,” pg. 4, Available: <https://marad.dot.gov/publications/PDF/By%20the%20Capes.pdf>



develop a merchant marine,” “to give preference to Australian labor and industry,” “to generate employment for Bahamian nationals,” “to support national security,” and “to protect the domestic economy.”<sup>89</sup> Many of these nations support policy objectives similar to those of the United States’ cabotage and protectionist laws.

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<sup>89</sup> MARAD, “By the Capes Around the World: A Summary of World Cabotage Practices,” pg. 3

## **The Merchant Marine Act of 1920**

Wesley Livsey Jones, a Republican from the state of Washington, served five terms in the United States House of Representatives from March 4, 1899 to March 3, 1909. Refusing to accept a sixth nomination for his seat in the House, he ran for and was elected to the United States Senate in 1909. He was reelected in 1914, 1920, and 1926, serving until his death on November 19, 1932. He held various positions within the Senate, including Republican whip from 1924 to 1929, Chairman of the Committee on Industrial Expositions, the Committee of Fisheries, and various other committees throughout his tenure.<sup>90</sup> In 1920, Senator Jones sponsored the Merchant Marine Act of 1920. It became law on June 5, 1920 and has since shared the Senator's name, being commonly referred to as the "Jones" Act.

The Shipping Act of 1916 was a response to the sudden need for ships to support American efforts in World War I. Under the terms of the act, 1,409 merchant vessels were constructed.<sup>91</sup> When the war concluded Congress was presented with the problem of disposing of the suddenly large government-owned merchant marine. In 1919, the 66<sup>th</sup> Congress decided that the conditions justifying continued federal construction and control of merchant vessels no longer existed. The Shipping Act of 1916 stipulated that the government was to relinquish this control within five years following the conclusion of the war. In November 1919, the House of Representatives voted 240 to 8 to annul the

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<sup>90</sup> Biographical Directory of the United States Congress, "Jones, Wesley Livsey," Available: <http://bioguide.congress.gov/scripts/biodisplay.pl?index=J000257>

<sup>91</sup> Heine, Irwin M., pg. 5

emergency provisions provided by the 1916 act thus preventing the Shipping Board from granting additional building contracts.<sup>92</sup>

The measure then went to the Senate Commerce Committee where the House's attitudes on reorganization of the merchant marine to promote private ownership were reflected. However, the recent war experience spurred a continual program of strong governmental support. With the fear of British competition a bill was developed that supported protectionism and retaliatory policies.<sup>93</sup>

President Wilson appointed Admiral William Benson to the chairmanship of the Shipping Board to pursue his agenda. Benson pushed for a very tough measure with strong discrimination and subsidies and complete American involvement in all shipping affairs. Newton D. Baker, the Secretary of War, noted that Benson viewed the problem as "one fierce and final competition between the British mercantile marine and the American mercantile marine." President Wilson met with his cabinet on June 1, 1920 and sided with Benson and the Shipping Board. Wilson admitted a concern with British commercial practices and expressed a desire for a strong American merchant marine. On June 5, 1920 President Wilson signed the Merchant Marine Act of 1920.<sup>94</sup>

The preface to the act states that the act is "An act to provide for the promotion and maintenance of the American merchant marine, to repeal certain emergency legislation, and provide for disposition, regulation, and use of property acquired thereunder, and for other purposes."<sup>95</sup> The first section of the act then went on to set a clear agenda for the regulations the act set forth.

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<sup>92</sup> Kilmarx, Robert A., et al., pg. 135-136

<sup>93</sup> Kilmarx, Robert A., et al., pg. 136

<sup>94</sup> Kilmarx, Robert A., et al., pg. 136

<sup>95</sup> Act of June 5, 1920

**“Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That it is necessary for the national defense and for the proper growth of its foreign and domestic commerce that the United States shall have a merchant marine of the best equipped and most suitable types of vessels sufficient to carry the greater portion of its commerce and serve as a naval or military auxiliary in time of war or national emergency, ultimately to be owned and operated privately by citizens of the United States; and it is hereby declared to be the policy of the United States to do whatever may be necessary to develop and encourage the maintenance of such a merchant marine, and, in so far as may not be inconsistent with the express provisions of this Act, the United States Shipping Board shall, in the disposition of vessels and shipping property as hereinafter provided, in the making of rules and regulations, and in the administration of the shipping laws keep always in view this purpose and object as the primary end to be attained.”<sup>96</sup>**

Thus, the goals of the act were very clearly laid out. The war had made clear the necessity for improvements in transportation and this act allowed for the federal government to enact these improvements through some form of nationalization. However, the act made it clear that public operation was not the desired method. Congress chose instead to pursue this goal through increased governmental regulation and encouragement. The act provided the Shipping Board with a method to turn its fleet over to private ownership, through sales at extremely low rates, while maintaining a regulatory role. The Shipping Board could also provide some funds to American shipping companies for new vessels. Through an “essential trade routes plan” the act also encouraged the growth of foreign trade on American vessels.<sup>97</sup>

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<sup>96</sup> Act of June 5, 1920

<sup>97</sup> Kilmarx, Robert A., et al., pg. 137

The Act addressed these issues and several others, but the section of the act that is of great concern today, and the focus of this thesis, is Section 27 which established the nation's current cabotage laws. Section 27 reads:

**“That no merchandise shall be transported by water, or by land and water, on penalty of forfeiture thereof, between points in the United States, including Districts, Territories, and possessions thereof embraced within the coastwise laws, either directly or via a foreign port, or for any part of the transportation, in any other vessel than a vessel built in and documented under the laws of the United States and owned by persons who are citizens of the United States, or vessels to which the privilege of engaging in the coastwise trade is extended by sections 18 or 22 of this Act: Provided, That this section shall not apply to merchandise transported between points within the continental United States, excluding Alaska, over through routes heretofore or hereafter recognized by the Interstate Commerce Commission for which routes rate tariffs have been or shall hereafter be filed with said commission when such routes are in part over Canadian rail lines and their own or other connecting water facilities: Provided further, That this section shall not become effective upon the Yukon river until the Alaska Railroad shall be completed and the Shipping Board shall find that proper facilities will be furnished for transportation by persons citizens of the United States for properly handling the traffic.”<sup>98</sup>**

It is the first half of this section that is of primary interest (the latter half delineates two specific exceptions), because it establishes the primary cabotage law of the United States as it exists today. Under this provision, goods are not permitted to be transported from one U.S. port to another on any ship other than a ship that was built in the United States, is owned by U.S. citizens, is crewed by U.S. citizens and is registered under an American flag.

This proviso is simply a reinstatement of cabotage laws that had been established by the Act of March 1, 1817 as amended in 1893 and 1898, but were lifted during World

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<sup>98</sup> Act of June 5, 1920

War I. There were, however, a few changes made with the reenactment. The language prohibiting movement in vessels owned by foreigners was changed to require movement on vessels “owned by persons who are citizens of the United States.” The phrase “by land and water” was added. U.S. ports were extended to include ports within “Districts, Territories, and possessions thereof embraced within the coastwise laws.” “Vessels to which the privilege of engaging in the coastwise trade is extended by sections 18 or 22 of this Act” was added. Finally, the two provisos at the end of the section setting aside two specific exceptions were added.<sup>99</sup>

Section 18 amended section 9 of the Shipping Act of 1916 to establish rules governing the registry of ships purchased from the government. Section 22 repealed the act entitled “An Act giving the United States Shipping Board power to suspend present provisions of law and permit vessels of foreign registry and foreign-built vessels admitted to American registry under the Act of August 18, 1914, to engage in the coastwise trade during the present war and for a period of one hundred and twenty days thereafter, except the coastwise trade with Alaska.” Section 22 also allowed the shipping board to issue special permits for foreign ships to carry passengers from the Pacific Coast to Hawaii through February 1, 1922.<sup>100</sup>

Section 21 of the act extended the coastwise laws of the United States to all island territories and possessions not already covered by the coastwise laws. It also provided an exception for the Philippine Islands until Congress recognized ships registered in the Philippines as registered in the United States.<sup>101</sup>

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<sup>99</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 173

<sup>100</sup> Act of June 5, 1920

<sup>101</sup> Act of June 5, 1920

Section 38 amended the Shipping Act of 1916 so as to define citizenship of a corporation, partnership or association. “No corporation, partnership, or association shall be deemed a citizen of the United States unless the controlling interest therein is owned by citizens of the United States, and, in the case of a corporation, unless its president and managing directors are citizens of the United States and the corporation itself is organized under the laws of the United States or of a State, Territory, District, or possession thereof, but in the case of a corporation, association, or partnership operating any vessel in the coastwise trade the amount of interest required to be owned by citizens of the United States shall be 75 per centum.”<sup>102</sup>

Section 27 has been amended over time so that it now contains eight provisos, including the two stated in the original statute. The first proviso restored some of the prohibitions of the 1797 Act that were repealed by the 1897 Act. Under this proviso, no vessel having at any time acquired the lawful right to engage in the coastwise trade, either by virtue of having been built in or documented under the laws of the United States, and later sold foreign, or placed under foreign registry, shall thereafter acquire the right to engage in the coastwise trade.<sup>103</sup> The intent of the law was to prevent the repatriation of American-built vessels under foreign flags to engage in the coastwise trade.

The second proviso resulted from two amendments, one in 1956 and the other in 1960. The 1956 amendment prohibited any ship that had the right to participate in the coastwise trade and then was rebuilt outside the United States, its territories, or possessions, from reengaging in the coastwise trade. In 1960 the proviso was amended to read “unless the entire rebuilding, including the construction of any major components of

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<sup>102</sup> Act of June 5, 1920

<sup>103</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 173-174

the hull or superstructure of the vessel, is effected within the United States, its Territories or its possessions.”<sup>104</sup>

The third and fourth provisos are those included in the original statute. The remainder of the provisos contain exceptions concerning transportation of merchandise loaded on railroad cars transported in a railroad car ferry operated on the Great Lakes, carriage of empty vans, tanks, barges and equipment for use with vans, cargo transported after consolidation on lighter-aboard-ship barges, and merchandise transported in vans in U.S.-flag vessels, when transferred from one such vessel to another owned by the same owner and having either a foreign destination or origin.<sup>105</sup>

In 1936, Section 21 was amended to include an exemption for the Virgin Islands. Cabotage laws were lifted and foreign-flag shipping service would be permitted to service the Virgin Islands to ensure adequate service until the President declared otherwise.<sup>106</sup> This Jones Act exemption remains in place today.<sup>107</sup>

Another exemption to the Jones Act is provided in Section 506 of the Merchant Marine Act of 1936. Usually, vessels receiving construction differential subsidies or operating differential subsidies are not permitted to operate in the coastwise trade so they do not compete with Jones Act ships that do not receive subsidies. However, under Section 506, ships can receive a six month waiver to participate in the protected trades if the Maritime Administration determines that there are no Jones Act ships available for a particular service.<sup>108</sup>

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<sup>104</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 174

<sup>105</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 174

<sup>106</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 21

<sup>107</sup> Virgin Islands Port Authority Website, Available: <http://www.viport.com/marine-services.html>

<sup>108</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 22



In 1984, Congress passed an exception that would allow foreign vessels to transport passengers between the mainland United States and Puerto Rico if no Jones Act ship is available. Waivers have also been periodically granted for Canadian vessels serving the Great Lakes or Alaskan trades if no Jones Act ship is available. In 1950, Public Law 891 authorized waiver of the navigation and inspection laws of the United States “upon the request of the Secretary of Defense to the extent deemed necessary in the interest of national defense by the Secretary of Defense.” However, waivers are granted to foreign-flag vessels usually only after the Maritime Administration seeks to arrange alternative U.S. flag shipping.<sup>109</sup>

However, throughout the summer of 1920 the attention focused on the bill was not focused on Section 27. Instead, controversies arose surrounding three other highly discriminatory clauses. The first extended coastal protections to the Philippines and other distant American possessions. The second, Section 28, granted preferential inland railroad rates to American cargoes shipped in American vessels if there was a surplus of American tonnage to handle the foreign trade. The third, Section 34, ordered the President to repeal all treaties that conflicted with the United States’ ability to employ discriminatory policies.<sup>110</sup>

Debate on the bill focused primarily on Section 28. The preferential rates system enacted by this section violated no less than thirty-two international treaties. Due to the large volume of complaints from injured foreign interests and irritated domestic interests who feared foreign retaliation the Shipping Board declared a ninety-day moratorium on

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<sup>109</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 22

<sup>110</sup> Kilmarx, Robert A., et al., pg. 138

the execution of this section of the act four days after the act was passed. The moratorium was later extended until January 21, 1921.<sup>111</sup>

Protest against extending coastal laws to the Philippines was also very intense. When the Philippine administration complained that foreign shippers would retaliate by boycotting the port of Manila, the Shipping Board shelved the clause.<sup>112</sup>

President Wilson was also faced with a major challenge, regarding Section 34, from foreign nations who protested that a treaty was “not a scrap of paper” and could not be abrogated without mutual consent. Wilson also insisted that Congress had overstepped its legislative authority when it inserted abrogation rights into the bill, because Congress could not appropriate executive functions. However, his cabinet pointed out that he forfeited those executive functions by signing the bill.<sup>113</sup>

President Wilson announced on September 24, 1920 that an endorsement of Section 34 would have been incompatible with the respect that America had given, and would give, to international accords. He had signed the bill under the rationale that his disavowal of the congressionally mandated discriminations would not negatively affect the “sound and enlightening provisions” also set forth by the bill. President Wilson’s announcement was an attempt to relieve international tensions created by the bill.<sup>114</sup>

President Wilson’s decision to strike down these three discriminatory features of the act represented a distinct shift in his attitude toward foreign shipping. In 1919 and early 1920, Wilson was upset with the diplomatic and commercial maneuvering of Allies following the war and with debate at home over the League of Nations. However,

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<sup>111</sup> Kilmarx, Robert A., et al., pg. 138

<sup>112</sup> Kilmarx, Robert A., et al., pg. 138

<sup>113</sup> Kilmarx, Robert A., et al., pg. 138

<sup>114</sup> Kilmarx, Robert A., et al., pg. 138-139

believing that the Merchant Marine Act of 1920 reflected a sort of bitterness over these issues and thus had gone a little too far, President Wilson tempered debate over these discriminations and moved back toward a platform of generosity and constructive policy. The President put the issue in perspective in the fall of 1920. There were two ways in which the nation could assist the world in creating a pure and spiritual democracy-by applying equality of treatment in domestic matters, and by “standing for right and justice as towards individual nations.”<sup>115</sup>

It is interesting that the debate over the bill focused on these issues and not Section 27. The Merchant Marine Act of 1920 was a 59-page bill with 149 amendments. The conference report for the bill was 36 pages long and the final reconciliation between the House and Senate versions of the bill did not mention Section 27. “The Sense of Congress was clear: a protected U.S. domestic-trade merchant fleet would be the cornerstone of any future American maritime policy.”<sup>116</sup>

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<sup>115</sup> Kilmarx, Robert A., et al., pg. 139

<sup>116</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 13

## **Impacts on the American Maritime Industry**

As discussed in prior sections, the United States has consistently acted to protect the national merchant marine with various legislations. These laws have had various effects on an industry that has changed throughout the history of the nation. It is important to understand the impacts of these laws, primarily the Jones Act (as it constitutes the nation's cabotage policy today), on the maritime industry. Thus an observation should be made of the state of the industry at the time of the law's conception, the state of the industry today, and what influence the law has on the national maritime industry.

Shortly after independence, to contend with the British navigation acts, the United States Congress passed an agenda of protectionist laws to aide the newly formed national merchant fleet. The merchant fleet of the United States flourished in the later part of the 18<sup>th</sup> century and reached a peak in the percentage of American commerce it carried in 1810 with 91.5% being carried on American ships.<sup>117</sup> However, some attribute this to the low cost and high quality of American shipbuilding at the time. During the colonial period an American ship could be constructed for approximately £3-4 per ton, while a similar ship would cost £5-7 per ton in England.<sup>118</sup>

“It can hardly be argued, however, that the competitive edge held by American maritime industries suffered greatly because of the English navigation laws. In fact, one authority has pointed out the adverse effect of a government-sponsored monopoly: ‘Protection from foreign competition resulted in British ship design of 1845 differing little from the style to be found in 1815...’

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<sup>117</sup> Cuneo, Joseph J., pg. 64

<sup>118</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 4

Statistics confirm the overall stagnant nature of the British shipbuilding industry in the 35 years before 1850.”<sup>119</sup>

By 1850, the American registered tonnage had tripled from what it was in 1830, to 3.5 million tons. Meanwhile, the British registered tonnage increased by less than half. In 1849, Great Britain repealed the last of its navigation acts, but the American protectionist laws remained in place.<sup>120</sup> It is statistics such as these that would suggest that protectionist laws may harm the maritime industry, rather than help it, and that it is the ability to compete that strengthens the industry.

Table 2 shows the percentage of American commerce carried on American ships from 1789 through 1991. It can be seen that the percentage carried by American ships peaked in the early 19<sup>th</sup> century, fell during the period following the civil war, rose again following World War I and then fell to its current levels following World War II. Table 3 shows the tonnage of the American fleet from 1800 through 1991 engaged in foreign trade. It can be seen that the tonnage consistently increases until the period following the Civil War then begins to recede. Then, during World War I, there is a massive build up of American tonnage followed by another massive construction of American tonnage during World War II. Following World War II, the tonnage under American registry falls to a rather steady plateau. As of July 1, 2002 the tonnage of American flagged ships engaged in foreign trade was 5,319,000 metric tons, lower than it was ten years prior.<sup>121</sup>

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<sup>119</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 4

<sup>120</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 6

<sup>121</sup> MARAD, U.S. flag statistics , Available: [http://www.marad.dot.gov/Marad\\_Statistics/USCCF\\_7-02.htm](http://www.marad.dot.gov/Marad_Statistics/USCCF_7-02.htm)

<u>Year</u>	<u>Percentage</u>
1789	23.6
1790	40.5
1800	89.0
1810	91.5
1820	89.5
1830	89.8
1840	82.9
1850	72.5
1860	66.5
1870	35.6
1880	17.6
1890	12.8
1900	9.8
1910	11.0
1920	48.7
1930	37.8
1940	N/A
1950	42.6
1960	11.1
1970	5.3
1980	3.7
1985	4.3
1986	4.2
1987	4.0
1988	3.9
1989	4.4
1990	4.1
1991	4.0

**Table 2: Percentage of American Commerce Carried on U.S. Flagged Ships<sup>122</sup>**

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<sup>122</sup> Cuneo, Joseph J., pg. 64

<u>Year</u>	<u>Size of Fleet</u>
1800	667,107
1810	981,019
1820	583,657
1830	537,563
1840	762,838
1850	1,439,694
1860	2,379,396
1870	1,448,846
1880	1,314,402
1890	928,062
1900	816,795
1910	782,517
1920	9,924,694
1930	6,295,935
1940	24,000,000
1950	8,353,000
1960	6,812,000
1965	6,759,000
1970	4,261,000
1975	6,204,000
1980	6,619,000
1982	5,141,000
1984	5,487,000
1986	5,475,000
1988	7,356,000
1990	7,283,000
1991	7,246,000

**Table 3: Size of the U.S. Flag Fleet in Tons Engaged in Foreign Trade<sup>123</sup>**

The depletion of the fleet following the Civil War can be attributed to two main factors. During the war nearly 1000 vessels left the American registry and the Act of June 27, 1797 prevented these ships to reenter the American registry after the war. The law was originally intended to protect the American fleet, but instead impacted the industry in the adverse by preventing reentry of these vessels, thus depleting the fleet.<sup>124</sup>

The second factor was the development of British iron steam vessels which were more productive than there American wooden counterparts. The competition offered by

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<sup>123</sup> Cuneo, Joseph J., pg. 65

<sup>124</sup> Cuneo, Joseph J., pg. 65

these vessels forced American shippers to seek other methods of cost reduction and the American fleet began to suffer.<sup>125</sup>

The last competitively priced American built ship was the wooden sailing schooner. During the period from 1880 to World War I they rivaled the tonnage of moderate sized steam-propelled vessels while offering low construction costs and small crew sizes. However, they only offered a short reprieve and were eventually overtaken by steel and steam vessels.<sup>126</sup> By the time the Merchant Marine Act of 1920 passed the United States had become a high cost producer of ships, with a cost of approximately \$130 per ton compared to \$70 per ton in Great Britain for steel steamship.<sup>127</sup>

As discussed in the prior section of this thesis, the Shipping Act of 1916 was a response to the need for ships to support American efforts during World War I. 1409 ships were constructed under the terms of the act and, as can be seen in the above tables, American shipping grew substantially during this period.<sup>128</sup> When Congress declared that conditions justifying continued federal construction and control of merchant vessels no longer existed, a means of relinquishing the ships under government control was needed. The response was the Merchant Marine Act of 1920.

By 1922, the United States had developed world's largest merchant fleet. At 13.5 million tons, the American fleet constituted 22% of the world's total shipping. However, due to the large number of vessels of which the Shipping Board had to dispose and the low rates at which these vessels were being sold, vessel prices (on the open market as

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<sup>125</sup> Cuneo, Joseph J., pg. 65

<sup>126</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 12

<sup>127</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 13

<sup>128</sup> Heine, Irwin M., pg.5



well as those being sold by the Shipping Board) declined severely. Owners who had previously purchased ship in the United States faced bankruptcy. Prospectors indulged in rate wars and other detrimental practices. The wages and working conditions of crews suffered.<sup>129</sup> Due to the overwhelming surplus of ships, the shipbuilding industry saw no significant new construction.<sup>130</sup>

This was the nature of the industry when the act was passed. The act has now been law for over eighty years and the industry has undergone many changes, including the rapid build up of World War II. At the end of the war the United States had the largest merchant fleet in the world, composed of more than 5000 vessels totaling over 32 million tons. The ships were once again sold at bargain prices, to both national and foreign interests.<sup>131</sup> European and Japanese shipyards undertook massive rebuilding and modernization efforts with their shipyards. However, American shipyards and shipowners looked primarily to protective legislation as the basis for survival and growth.<sup>132</sup> The tables above show a steady decline in the United States Merchant Marine. Only during times of war did the nation reassert its maritime dominance when the government undertook massive construction campaigns.

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<sup>129</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 177

<sup>130</sup> Cuneo, Joseph J., pg. 66

<sup>131</sup> Cuneo, Joseph J., pg. 67

<sup>132</sup> Cuneo, Joseph J., pg. 67

The following table shows the Jones Act qualified fleet as of July 1, 2003.

Vessel Type	Ships	Gross Tons	Deadweight Tons
Tanker	83	3,082	5,295
Full Container	22	520	552
Dry Bulk	9	148	315
Roll-On/Roll-Off	13	426	240
Freighter	2	32	45
Cruise/Passenger	1	20	7
<b>Total</b>	<b>130</b>	<b>4,228</b>	<b>6,454</b>

**Table 4: Privately-Owned Self-Propelled Merchant Vessels with Unrestricted Domestic Trading Privileges (Jones Act); Vessels of 1,000 GRT and above. Tonnage in Thousands of Tons.**<sup>133</sup>

Though the United States merchant fleet has decreased in size substantially from the size of the fleet following World War II, as seen in Tables 2 and 3, it continues to decrease in size even today. In 1982, the active Jones Act fleet consisted of 198 active merchant vessels: 2 passenger ships, 1 general cargo ship, 24 intermodal vessels, 10 bulk carriers, and 161 tankers, tank barges and LNG carriers.<sup>134</sup>

The size of the fleet is not the only important measure of the Jones Act's influence and importance. The extent to which the vessels that comprise the fleet are useful is also an important barometer. "The 1982 Falkland Islands war demonstrated the usefulness of passenger ships in limited conflicts far from homeland bases. Intermodal vessels, particularly roll-on/roll-off (RO/RO) vessels, are highly valued by the navy as defense assets, and smaller tankers, of 80,000 deadweight tons or less, are considered militarily useful."<sup>135</sup> Thus, though there are few ships in the current Jones Act fleet, many of them may be useful in a military context.

<sup>133</sup> MARAD, Jones Act Fleet Statistics, Available: [http://www.marad.dot.gov/Marad\\_Statistics/ja-7-03.htm](http://www.marad.dot.gov/Marad_Statistics/ja-7-03.htm)

<sup>134</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 16

<sup>135</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 16

Another measurement that can be used to evaluate the Jones Act is the number of shipyards in the country capable of undertaking major construction projects, such as combatants, naval supply vessels, or merchant vessels. In 1950, the Maritime Administration recognized 80 shipyards in the United States.<sup>136</sup> In 1984 there were 23 large shipyards.<sup>137</sup> That number fell to 15 in 1992.<sup>138</sup> In the 2002 annual report, the Maritime Administration stated the number of large shipyards to be six.<sup>139</sup> By this measure, the Jones Act would seem to be failing.

Many of these shipyards rely on naval contracts to survive. In 1984 the largest source of revenue for private shipyards was the Department of Defense. Then Secretary of the Navy John Lehman stated that navy work by itself could not support an adequate shipbuilding base.<sup>140</sup> Table 5 shows the number of new merchant ships delivered by U.S. shipyards from 1977 to 2002. The table shows a general downward trend in new merchant ship production by American shipyards. In 1984 it was estimated that 21,000 more production workers were needed to meet the shipyard mobilization requirements. To support this work force it was estimated that between twenty and thirty new merchant ships would need to be constructed each year.<sup>141</sup> Table 5 clearly shows that this level of production has not been met.

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<sup>136</sup> Cuneo, Joseph J., pg. 70

<sup>137</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 16

<sup>138</sup> Cuneo, Joseph J., pg. 70

<sup>139</sup> MARAD Annual Report 2002, pg. 22, Available: <http://www.marad.dot.gov/publications/genref.htm>

<sup>140</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 16-17

<sup>141</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 17

<b>Year</b>	<b>Merchant Ships (#)</b>	<b>Merchant Ships (x1000GT)</b>
1977	25	1036
1978	19	1027
1979	21	1298
1980	23	788
1981	22	347
1982	17	326
1983	15	283
1984	5	125
1985	3	60
1986	1	95
1987	7	166
1988	0	0
1989	0	0
1990	0	0
1991	0	0
1992	3	45
1993	0	0
1994	1	17
1995	1	2
1996	1	28
1997	4	107
1998	2	24
1999	6	161
2000	1	7
2001	2	90
2002	2	90

**Table 5: New Merchant Ships Over 1000 GT Delivered by U.S. Shipyards Since 1977<sup>142</sup>**

On July 12, 2003, Matson Navigation Company christened its newest containership, the M/V Manukai. The M/V Manukai is the first of a two-vessel, \$220 million, contract between Matson and Kvaerner Philadelphia Shipyard. It is the first new ship built by Matson since the M/V R.J. Pfeiffer, built in 1992.<sup>143</sup> The Manukai is also

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<sup>142</sup> Maritime Business Strategies, LLC, "Deliveries from U.S. Shipyards, 1977 to Present," Available: <http://www.coltoncompany.com/shipbldg/statistics/deliver1.htm>

<sup>143</sup> Matson Navigation Company, "New Matson Containership MV Manukai Christened in Philadelphia," Available: [http://www.matson.com/bos/pr\\_071203a.shtml](http://www.matson.com/bos/pr_071203a.shtml)

the first new containership built by an American shipyard since the construction of the Pfeiffer.<sup>144</sup>

In his 1999 thesis for an SM degree in Ocean Systems Management at the Massachusetts Institute of Technology, Joseph A. Hubbard performed a net present value (NPV) analysis to determine the feasibility of constructing a new container ship versus purchasing an older container ship for use in the Jones Act trade. The first part of his analysis required the designation of an older ship and the costs associated with acquiring it for use in the Jones Act fleet. Pace Setters, CDS ships built in 1973, were chosen as candidates for the analysis. Hubbard determined that one of the ships could be purchased for \$500,000, would require \$1,000,000 in reconditioning, and a fee of \$40,000 would need to be paid to MARAD for approval to enter the Jones Act trade.<sup>145</sup>

Hubbard used the M/V R.J. Pfeiffer as the candidate for the new ship. At the time of the thesis, the Pfeiffer was the newest containership in the Jones Act fleet and had similar characteristics to the Pace Setter. Using a new construction cost of \$129,000,000 and a Title XI mortgage that required a 12.5% down payment (\$16,125,000), Hubbard determined the annual payment over 25 years with an 8% interest rate to be \$10,573,992.<sup>146</sup>

When determining daily operating costs, Hubbard accounted for such factors as: crew costs, maintenance costs, hull and machinery insurance, and the new ship's superior efficiency (protection and indemnity insurance and port charges were excluded since they would be the same for both ships). The daily operating cost for the new ship was

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<sup>144</sup> Maritime Business Strategies, LLC, "Containerships Built in U.S. Shipyards," Available: <http://www.coltoncompany.com/shipbldg/ussbldrs/postwwii/merchant/containerships.htm>

<sup>145</sup> Hubbard, Joseph A., "The Jones Act Liner Trade," S.M. Thesis, Department of Ocean Engineering, Massachusetts Institute of Technology, 1999, pg. 36

<sup>146</sup> Hubbard, Joseph A., pg. 37

calculated to be \$19,625 and the daily operating cost of the old ship was determined to be \$32,917.<sup>147</sup>

Using these values, Hubbard performed a NPV analysis using discount rates varying from 5-15%. Then using the values obtained with the NPV analysis he calculated an equivalent annuity payment to determine the mortgage payments. In each case analyzed the old ship was cheaper, with an average difference in annuity payments of \$7.7 million.<sup>148</sup>

Acknowledging the fact that the life of the old ship could not be twenty years, Hubbard performed another analysis with the life of the old ship being five years. Using a ten percent discount rate, Hubbard tested acquisition costs from \$1,540,000 to \$30,000,000, with steps of \$5,000,000 (except from the original acquisition cost to the \$5,000,000 level). Only at the \$30,000,000 acquisition cost did the old ship yield similar equivalent annuity payments to that of the new ship. Hubbard concluded that this difference in cost represented a substantial burden for domestic carriers imposed by the Jones Act.<sup>149</sup>

Hubbard argued that, though the Jones Act had an effect on the state of the industry, it did not have a direct effect and that much of the decline could be associated with the behavior of the industry.

“The decline can be largely attributed to the focus of shipyards on higher priced government contracts. Prior to World War II, ship contracts, both Navy and commercial, were generally of a simple fixed price nature. Generally contract plans and specifications were developed, but in some cases where integrity and mutual respect existed on both sides, the contract consisted only of performance

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<sup>147</sup> Hubbard, Joseph A., pg. 38

<sup>148</sup> Hubbard, Joseph A., pg. 38-42

<sup>149</sup> Hubbard, Joseph A., pg. 42

requirements, a handshake of understanding and a confirming letter contract. The best practice with respect to contract changes identified by either party was to “scope” each perceived change and estimate the cost and negotiate a price therefore before commencing work thereon. After World War II the general Navy practice was to contract for prototypes on a cost plus fee basis, and for follow on ships on a firm fixed price basis. The first constructive claims suit, by Todd Shipbuilding Corporation, in connection with overruns of approximately \$100 million in 1967. This claim was settled favorably to Todd. This concept spread throughout the Navy shipbuilding industry like wildfire. The industry total for asserted but unsettled claims was to grow to \$300 million in 1971 and explode to \$2.7 billion by 1977. Contractor’s bid prices were often deliberately set below the yard’s best historical performance to come within the Navy’s budget and/or wipe out the competition, the exception being that, the yard could make up the difference in the course of negotiating change orders and by constructive claims. To this day Navy contracts continue to nurse the few remaining shipyards along.”<sup>150</sup>

Hubbard also places some of the blame on the behavior of the government with regard to maritime policies.

“The shipbuilding industry has suffered greatly over the years. Although the Jones Act is not wholly responsible for its demise, it is nevertheless a factor. When our military buys foreign ships, as they have for the current Sealift program, it is a strong statement as to the failure of the Jones Act. It is extremely hypocritical for the government to require private companies to build U.S. and not follow the doctrine it created.”<sup>151</sup>

“The Sealift program itself is contradictory to the Jones Act. Its mission is to provide sea transportation needed to deploy and sustain U.S. forces worldwide. In peacetime this command contracts with private shipping companies to meet its requirements. The Navy has deemed it necessary to create its own fleet of supply ships, thus taking away the need for vessels from the private sector.”<sup>152</sup>

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<sup>150</sup> Hubbard, Joseph A., pg. 45-46

<sup>151</sup> Hubbard, Joseph A., pg. 46

<sup>152</sup> Hubbard, Joseph A., pg. 46-47

**“To add insult to injury the formation of the Maritime Security Program, which currently serves as an auxiliary when needed for national defense needs, only requires vessels to be U.S. flag. Only four ships in this program are U.S. built and they are over twenty years old. If this does not admit the failure of the Jones Act, I don’t know what does. The government has mandated the construction of Jones Act vessels in the U.S. so that they can have a Naval auxiliary.”<sup>153</sup>**

Suffice it to say, the Jones Act is not the only contributing factor to the current state of the national maritime industry. The industry has been in decline since the end of World War II, and only for the periods during and immediately following the two World Wars has the United States had a dominant national merchant marine. The number of ships, as well as the number of major shipyards, in the national maritime industry has declined to extreme lows.

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<sup>153</sup> Hubbard, Joseph A., pg. 47



## **The Economic Effect of the Jones Act**

The primary justification of the Jones Act is the necessity of a viable national merchant marine for national defense; an important benefit to society. However, restrictions in free trade will result in an efficiency loss for the allocation of economic resources. Thus, there are also significant economic effects that result from cabotage restrictions. The following section attempts to quantify many of the costs associated with domestic shipping restrictions.

### **Early Estimates**

In 1975, Gerald R. Jantscher performed estimates of the costs associated with cabotage for his book *Bread Upon the Waters: Federal Aids to the Maritime Industries*. He stated that the full costs associated with cabotage could never be established. This was due to indirect costs that shippers must bear as additional costs by using alternative methods of transportation due to the high costs associated with domestic shipping. The costs are often passed on to the consumer through higher prices for goods. This can result in the consumer substituting cheaper goods. In the extreme, it may result in entire markets being lost. These costs result in a welfare loss for consumers.<sup>154</sup>

Jantscher emphasized that these indirect costs may not be small and should not be assumed to be so. Because he was unable to quantify these costs, however, they were ignored in the analysis. Jantscher chose to focus on the direct costs of cabotage. He defined the direct costs to be additional costs attributable to the cabotage laws of operating vessels in the domestic trade. He further defined direct costs by breaking the costs into two distinct groups: the costs associated with the requirement that only vessels

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<sup>154</sup> Jantscher, Gerald R., pg. 49

built in the U.S. could operate in the domestic trade, or building restriction costs; and the costs associated with the reservation of domestic commerce to U.S. flag vessels, or the operating restriction.<sup>155</sup>

Between 1950 and 1970, customers of American shipyards paid an estimated \$900 million to \$1 billion more, for constructing new vessels and converting old vessels, over the amount that would have been paid to perform the same work in foreign yards. This represents a substantial added cost to the American domestic operator. This is a number comparable to the \$1.13 billion given as construction subsidies to offset the costs of domestic building for American ships participating in the foreign trades.<sup>156</sup>

To arrive at these estimates, Jantscher assumed that no American shipowner would build a vessel or perform conversions in the United States after July 1956 without a construction subsidy if the building restriction did not require the owner to do so. Once the value of unsubsidized new construction and conversions was determined, an estimate was made of the cost of this work abroad using the published rates of construction differential subsidies. Jantscher adjusted his estimates by one third for ships built in 1958 and 1959 since the closing of the Suez Canal resulted in several ships being ordered from American yards for foreign flag service. These orders were not due to the building restriction and thus some ships may be built under certain circumstances in American shipyards without the need for the build restriction. This method resulted in a cost of nearly \$1 billion dollars due to the building restriction.<sup>157</sup>

To determine the cost of the operating restriction, Jantscher estimated that the freight rates would fall to approximately the lower rates of foreign operators. The key is

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<sup>155</sup> Jantscher, Gerald R., pg. 49

<sup>156</sup> Jantscher, Gerald R., pg. 50

<sup>157</sup> Jantscher, Gerald R., pg. 50-51

to determine how much lower costs would be for foreign operators if they entered the American domestic trade. The estimated cost of the operating restriction under this approach was estimated to be between \$100 million and \$150 million per year. This would represent a cost substantially exceeding \$2 billion dollars between 1950 and 1975. Since the U.S. domestic oceangoing fleet shrank between 1950 and 1975 and the costs associated with the operating restriction have risen, the gap has widened between domestic and foreign rates.<sup>158</sup>

However, Jantscher acknowledged that his estimate was not 100 percent reliable. The costs of operating American ships in the domestic trade were derived from data collected by the Maritime Administration. This data was for foreign operators, since the Maritime Administration did not collect data for domestic operators, and were therefore adjusted. To determine foreign freight rates, Jantscher based his estimates on the principal competitors to U.S. operators in the North Atlantic trade routes. The estimate also relies solely on operating costs, neglecting other possible sources of costs. The estimate does demonstrate, however, that there is a substantial cost to the operating restriction.<sup>159</sup> Combined, the building and operating restrictions represented an additional cost of over \$3 billion from 1950 to 1975.

Another brief glimpse of what economic influence the Jones Act has can be captured by comparing the shipbuilding industry to the national economy. In 1983, the total employment in private U.S. shipyards was 160,000, of which only 10,000 could be attributed to the Jones Act. In contrast, national employment in 1983 was 103 million people. The total value of work done in U.S. private shipyards in 1983 was \$9.7 billion.

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<sup>158</sup> Jantscher, Gerald R., pg. 52

<sup>159</sup> Jantscher, Gerald R., pg. 53

The Gross National Product for 1983 was \$3,304.8 billion.<sup>160</sup> Though this is not a definitive portrayal of the maritime industry, it certainly provides a context for the contribution of the shipbuilding industry to the national economy.

In 1984, the Congressional Budget Office published a report that concluded that “U.S. crew costs have reached levels that typically are 2.5 times those of European crews and over six times those of Third World crews.” The study also estimated that the cost to build a ship in the United States was approximately three times the cost to build a comparable ship in a Japanese or Korean shipyard.<sup>161</sup>

Basic economic theory would suggest that the resulting higher cost of American ships would result in higher prices to consumers. The Congressional Budget Office study noted:

“It is estimated that the cost to the economy from cabotage in fiscal 1983 was about \$1.3 billion. This is the cost to shippers for U.S. flag services above the cost of the same services from foreign flag ships. The major portion of this amount (about \$1 billion) is attributable to the carriage of Alaskan North Slope crude oil to the continental United States.”<sup>162</sup>

In 1980, the General Accounting Office estimated the additional cost to the federal government of moving 2.3 million tons of foreign trade cargo on American ships due to cargo preference laws to be between \$71.4 million and \$78.6 million. This cargo represented 6.2 percent of all U.S. flag cargo. In 1982, a study performed for the Alaskan Statehood Commission estimated that “differentials for U.S. flag vs. foreign flag total

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<sup>160</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 26-27

<sup>161</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 27

<sup>162</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 27

shipping costs would range from about ten percent (in the liner trade with the west coast) to 40 percent in oil product shipments from west coast refineries.”<sup>163</sup>

These numbers led Clinton Whitehurst, in his publication *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, to conclude that relaxing Jones Act prohibitions would result in some decrease of consumer prices. The effect on the consumer price index would be minimal, however, due to the relatively small share of total domestic transportation expenses held by ocean shipping. Unemployment would increase in the short term but would not significantly impact national unemployment percentages. There would be no discernible effect on Gross National Product.<sup>164</sup>

### **1998 General Accounting Office Report**

In 1991, 1993 and 1995, the United States International Trade Commission (ITC) issued reports entitled The Economic Effects of Significant U.S. Import Restraints. These reports concluded that the Jones Act substantially increased the cost of domestic waterborne commerce. These three reports estimated the annual economic impact in terms of gains from repealing the act to range from a high of \$9.8 billion in the 1991 study to a low of \$2.8 billion in the 1995 study.<sup>165</sup>

In March of 1998, at the request of Senator John McCain, Chairman of the Senate Committee on Commerce, Science, and Transportation, the United States General Accounting Office published a report evaluating the validity of the 1995 report issued by

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<sup>163</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 27

<sup>164</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 28

<sup>165</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, United States General Accounting Office, Washington D.C., March 1998, pg. 1-2

the U.S. International Trade Commission. The GAO report focused on four key questions: 1) Was the ITC's estimate of the impact of reduced transportation costs on Alaska's North Slope oil production unreasonably high? 2) How reasonable was ITC's estimate of the impact that repealing the Jones Act would have on the number of U.S. workers in the domestic maritime industry? 3) How reasonable was ITC's methodology for calculating the differential between the shipping rates of domestic and foreign vessels, and were the data ITC used accurate and complete? 4) To what extent did ITC include in its analysis the additional costs to foreign vessel operators of complying with relevant U.S. laws if they were allowed to engage in domestic trade?<sup>166</sup>

To answer these questions, the GAO interviewed ITC staff, officials of the Maritime Administration, and groups representing various opinions on the Jones Act such as the Jones Act Reform Coalition and the Maritime Cabotage Task Force. The GAO also examined studies related to the Jones Act economic impact by GAO, ITC, the Department of Energy, the Office of Technology Assessment, the Congressional Budget Office, and private consultants. Finally, the GAO conducted a review to assess which U.S. laws might result in significant compliance costs for foreign vessel operators if the Jones Act was repealed. The GAO report was not an attempt to quantitatively determine the economic impact of the Jones Act.<sup>167</sup>

With regard to the first question, the GAO found that the ITC estimate for the impact of reduced transportation costs on Alaska's North Slope oil production was not

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<sup>166</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 2-3

<sup>167</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 3

excessive. ITC actually estimated a small increase in domestic oil production that represented less than three percent of Alaska's oil production.<sup>168</sup>

Answering the second question, the GAO found that the ITC's assumption about the number of jobs that might be affected by the repeal of the Jones Act appeared reasonable. In the 1995 analysis, ITC estimated that repealing the Jones Act would cause the loss of approximately 2,450 American maritime jobs due to foreign flagged vessels replacing American flagged vessels. This estimate was based solely on the 11,000 workers employed in the coastwise trade. ITC argued that there would be little impact on the inland and lakewise segments of domestic trade because the segments of the industry are sufficiently competitive and efficient. However, critics charged that repeal could result in up to 124,000 workers losing their jobs. This would represent the total number working in all aspects of the domestic trade.<sup>169</sup>

However, the GAO report noted that it would be difficult to determine the percentage of workers that could lose their jobs in the coastwise maritime sector because the ITC's estimates relied on an assumption about how cargo would be divided between American and foreign flagged ships and there are currently no foreign flagged ships in the trade to give verification to this assumption. It would also be difficult to predict how relevant laws would apply to foreign ships if they were allowed to enter the trade.<sup>170</sup>

The GAO determined that the methodology used by the ITC for calculating the differential between the shipping rates of domestic and foreign vessels appeared

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<sup>168</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 4

<sup>169</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 4-6

<sup>170</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 4

reasonable. The 1995 study estimated that the average shipping cost to transport goods on American flagged vessels was 89 percent higher than that for comparable foreign flagged vessels.<sup>171</sup>

However, the GAO report stated that the accuracy of this estimate can be questioned for two key reasons. First, there are no data for foreign vessels operating in the domestic trade, since they are not permitted to operate in this trade, therefore the actual freight rates that would be charged cannot be determined and the freight rates used were based on assumptions that in turn can't be verified for this reason. Second, oil shipments from Alaska accounted for 90 percent of the domestic cargo carried in the ITC calculations. Since the issue of the report, shipments from Alaska to the Gulf Coast had effectively been eliminated due to increased demand on the West Coast and declining oil production of the Alaskan North Slope oil field. Since this trade represented the largest cost differential between foreign and domestic shipping, this elimination would result in a lower cost differential.<sup>172</sup>

On the final aspect of the analysis, the GAO determined that the ITC did not fully consider the costs of foreign vessel operators complying with U.S. laws if they were allowed to engage in the domestic trade. The GAO assessment found that if foreign vessel operators incurred additional costs because they had to comply with some or all of the laws applicable to American flagged vessel operators, the additional costs would probably be incurred in three main areas: taxes, labor, and employee protection.<sup>173</sup> ITC

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<sup>171</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 4,8

<sup>172</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 8-9

<sup>173</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 4



staff contended the costs of compliance with these laws were not as high as critics state. ITC argued that lower ship construction costs accounted for the largest share of the rate differential and that compliance with U.S. minimum wage laws would have little impact because foreign crews are already paid at least that level. MARAD said that foreign crews are paid substantially less than American crews, some less than the U.S. minimum wage. GAO concluded that determining the cost of complying with these laws would be difficult, and that their applicability to foreign vessels would be up to the governing agencies if the laws were not amended by Congress.<sup>174</sup>

The 1991 report was generated due to a request by the Senate Finance Committee for the ITC to review a number of significant import restraints, including the Jones Act. The U.S. Trade Representative asked ITC to update the 1991 study biennially, which resulted in the 1993 and 1995 studies. At the request of the U.S. Trade Representative, ITC did not publish a report in 1997 so that more current economic data could be obtained.<sup>175</sup> In 1999 and 2002, ITC published updated reports.

### **1999 International Trade Commission Report**

The 1999 ITC report estimated that in 1996 Jones Act waterborne commerce amounted to 1,101 million short tons of traffic and \$7.7 billion in revenues. Seventy-nine percent of this cargo was liquid bulk shipments and 21 percent was dry cargo.<sup>176</sup> The report estimated shipboard employment in the domestic cargo sector to be 24,246 jobs. Of those jobs, 8,800 were listed as oceanborne, 1,736 were listed as lakewise, and 13,710

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<sup>174</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 11

<sup>175</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 2

<sup>176</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, Investigation No. 332-325, United States International Trade Commission, Washington D.C., May 1999, pg. 88

were listed as inland waterway jobs. Since vessels on longer voyages may employ more than one seaman for a billet in a calendar year, a conversion ratio of 2.3 was used resulting in 3,850 billets being equivalent to 8,800 jobs.<sup>177</sup>

Once the nature of the industry was determined, ITC created a general equilibrium model that divided the U.S. economy into ten sectors that, in addition to the nine aggregate sectors, accounted for the rest of the U.S. economy. Highlighted sectors in the model included the cabotage and water transportation sectors, which are directly affected by the Jones Act, and those sectors with significant upstream or downstream linkages to cabotage services. Using this model, the ITC then analyzed two scenarios. The first scenario analyzed complete removal of the Jones Act (complete liberalization) and the second analyzed partial removal of the Jones Act, namely the U.S. build requirement. The models dealt only with domestic oceanborne cargo.<sup>178</sup>

The effects of the Jones Act on oceanborne cabotage services were estimated by introducing the possibility of importing cabotage services at the world price. This figure was calculated as the output-weighted average difference between U.S. and world prices for shipping for the various main types of cargo. A tariff equivalent was estimated at 64.6 percent for the analysis. The tariff equivalent estimate was a weighted average of the average price gap between the U.S. price for shipping Alaskan North Slope crude petroleum to all destinations and the average world price for a comparable tanker shipment transported an equal distance and the average price gap between domestic and foreign dry cargo shipments.<sup>179</sup>

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<sup>177</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 89

<sup>178</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 97

<sup>179</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 98

The ITC analysis concluded that complete liberalization of the Jones Act trade would result in a total welfare gain of \$1.32 billion. Stated another way, the real national income is reduced by approximately \$1.32 billion due to the restrictions imposed by the Jones Act. ITC stated the primary reason for this cost to the national economy to be a 22 percent decline in the cost of shipping services in the domestic trade if the Jones Act were repealed.<sup>180</sup>

The ITC estimated further that imports would rise by approximately \$2.4 billion, domestic output would fall by \$1.5 billion (or 51 percent), and employment in the cabotage trades would decline by 4500 full-time jobs. Furthermore, upstream sectors (such as management/consulting services and shipbuilding) would lose approximately 2,450 jobs. Downstream sectors and the rest of the U.S. economy showed an increase in employment of approximately 7,850 jobs, representing an employment increase of approximately 0.1 percent or less per sector.<sup>181</sup>

The second scenario analyzed the cost if foreign built ships were allowed to enter the domestic trade, but maintained the American crew, American owned, and American flagged requirements. This is important because ITC estimated the price gap to be between 50 and 150 percent for foreign and domestically built ships. Capital costs were estimated to account for approximately 26 percent of the daily cost breakout for American liner operators. Thus, daily costs are 13 to 39 percent higher than they would be if domestic carriers were permitted to purchase foreign-built ships.<sup>182</sup>

With the partial liberalization scenario, ITC estimated that domestic prices for cabotage services would be reduced between five and twelve percent and demand for

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<sup>180</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 98

<sup>181</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 98-100

<sup>182</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 102

these services would increase. Domestic revenues would increase by \$69.5 million to \$188.9 million, or by 2.5 to 6.8 percent, respectively. Employment in the deepwater domestic sector would increase by 670 to 1,920 full-time jobs, or by 8 to 22 percent, respectively. The total benefit to consumers would be a welfare increase ranging from \$138 million to \$380 million.<sup>183</sup>

The primary differences between domestic and foreign shipping costs are due to higher operating costs and capital costs for domestic operators. Manning costs for a comparable vessel are twice as high in the United States when compared to the international trades. Since older vessels generally pay higher insurance, and American vessels tend to be substantially older than those of international fleets, there is a significant increase in insurance costs. However, ships of comparable age would pay comparable insurance. Capital costs are significantly higher for American built ships, with the lowest differential in cost between an American built ship and a foreign built ship estimated at 50 percent.<sup>184</sup>

### **2002 International Trade Commission Report**

The 2002 report estimated that in 1999 the American oceanborne domestic shipping industry carried 229 million short tons of cargo in U.S. waters and generated \$1.8 billion in revenues. The domestic shipping industry as a whole generated \$6.8 billion, with \$549 million attributed to lakewise trade, and \$4.4 billion attributed to inland waterway commerce. Of the oceanborne cargo, 70.8 percent was petroleum-based products, 7.4 percent was crude materials, manufactured goods and manufacturing equipment accounted for 6.8 percent, chemicals and related products accounted for 6.2

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<sup>183</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 103

<sup>184</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 94

percent, coal accounted for 5.7 percent, and food and farm products accounted for 3.1 percent.<sup>185</sup>

The 2002 report estimated shipboard employment in the year 1999 to be 10,380 jobs. However, this number does not include employment in the inland waterways segment of the industry and consists of 9,036 in the oceanborne fleet and 1,344 in the lakewise fleet. The number of self-propelled, American flagged vessels decreased by seven percent from 1995 to 1999 and the volume of cargo fell by fourteen percent over the same period. Employment also declined, but the decline was not proportional as more activity had been transferred to barges and other lower-cost vessels. Employment declined approximately four percent.<sup>186</sup>

The 2002 report also found the cost differentials between operating an American ship and a foreign ship to be substantial. ITC estimated the daily operating expense for a U.S. flagged tanker to be \$26,050 while a foreign flagged would have operating costs of approximately \$12,400. The daily operating expense for a U.S. flagged containership was estimated to be \$110,800 while a foreign flagged tanker would have operating costs of approximately \$96,450. The majority of this cost differential was accounted for in crew costs and maintenance and repair costs.<sup>187</sup>

Once again, ITC created a general equilibrium model. The cost advantage held by foreign suppliers was estimated to be 59 percent based on the weighted average of cost differentials for the different types of cargos. Using this model, the 2002 reports estimated that complete liberalization would result in a welfare change of \$656 million.

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<sup>185</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, Investigation No. 332-325, United States International Trade Commission, Washington D.C., June 2002, pg. 118-119

<sup>186</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 118-119

<sup>187</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 121

Relaxing only the U.S. build requirement would result in a welfare change of \$261 million. Taking the analysis a step further this time, ITC analyzed complete liberalization again if the foreign cost differential was only 80 percent (foreign operators operated at a cost 80 percent of the U.S. cost) and if the cost differential was only 90 percent. The 80 percent level resulted in a welfare gain of \$262 million and the 90 percent level resulted in a \$119 million welfare gain. ITC performed the additional cost differentials of 80 percent and 90 percent because of the varying set of beliefs about what the differential would be.<sup>188</sup> Thus the report concluded that the Jones Act still costs the American economy, but not as much as they had stated in the 1999 report.

With respect to job loss, the 2002 report estimated that complete liberalization would result in 8,340 lost full-time jobs in water transportation and 3,140 lost full-time jobs in shipbuilding. However, downstream sectors and the rest of the U.S. economy would see an increase in employment of 7,230 full-time jobs.<sup>189</sup>

In the partial liberalization scenario, where only the requirement that ships operating in the domestic trade be built in the U.S. was lifted, ITC estimated that coastwise water transportation would lose 810 full-time jobs, but other water transportation sectors would gain 710 full-time jobs. Shipbuilding was estimated to lose 4,000 full-time jobs, but downstream sectors and the rest of the American economy was estimated to gain 2,450 full-time jobs.<sup>190</sup>

In monetary terms, removal of U.S. build requirement was estimated to cost the American shipbuilding industry \$503 million. However, water transportation (including coastwise and other sectors) were estimated to gain \$253 million. Downstream sectors

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<sup>188</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 123-125

<sup>189</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 126

<sup>190</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 128

and the rest of the U.S. economy were estimated to gain \$321 million. Imports in the shipbuilding industry were predicted to rise by \$271 million.<sup>191</sup>

Thus, the largest impact of removing the domestic build requirement was on the U.S. shipbuilding industry. Investments in new domestic built ships were eliminated, replaced by cheaper foreign built ships. Output of the U.S. shipbuilding industry fell by four percent while shipbuilding imports increased by 133 percent. Output of coastwise shipments increased six percent and the cost savings were passed on in an eleven percent rate reduction. Over time, removal of the U.S. build requirement would result in decreased capital costs leading to decreased operating costs.<sup>192</sup>

It is apparent that there is a general consensus among the ITC reports that the Jones Act does indeed place an added cost on the American economy. The level of that cost varies greatly between the reports, from a high of \$9.8 billion in the 1991 report to a low of \$656 million in the 2002 report. ITC attributes this change to two factors. First, ITC cites a change in the modeling system used, including a “comprehensive revision of the treatment of coastwise water transportation.”<sup>193</sup> Second, ITC cites a large decline in the gross output of Jones Act transport, which fell by approximately 34 percent from 1996 to 1999. The contraction of the industry correlates to smaller benefits from liberalization in the model since the industry is smaller.<sup>194</sup>

In every ITC report the Jones Act represented an added burden. Though the ITC’s estimate of the economic burden imposed by the Jones Act decreased substantially from the 1991 report to the 2002 report, it is clear that there is still a substantial cost

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<sup>191</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 128

<sup>192</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 129

<sup>193</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 125

<sup>194</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 125

associated with cabotage. ITC also noted prior work by Hufbauer and Elliott, *Measuring the Costs of Protection in the United States*, which estimated the cost of the Jones Act to be \$1.1 billion.<sup>195</sup>

ITC also points out that the purpose of these reports was “to provide information on the costs and effects of only the Jones Act. The analysis does not seek to draw conclusions regarding the desirability of cabotage laws, nor does this report attempt to quantify or assess other costs or benefits, such as those associated with national defense issues, that are linked with the support of a domestic fleet.”<sup>196</sup>

Thus, there are two important difficulties regarding any attempt to quantify and analyze the costs of cabotage. First, as pointed out in the GAO report, the true costs of cabotage cannot be determined because there is no way to measure what the rates and operating costs of foreign operators in the American domestic trade would be. In turn, many argue that any estimate is faulty and doesn’t supply adequate evidence. An interesting paradox is thus developed where the only way to determine the cost of cabotage is to let foreign ships enter the trade, but foreign ships would most likely not be permitted to enter the trade without sufficient evidence of the significant benefits. This argument seems on some level illogical. To dismiss the potential benefits of eliminating cabotage, simply because the benefits cannot be completely quantified, would seem overly prohibitive. It seems particularly illogical when the uncertainty is generated by perpetuating the status quo. If this principle were applied to every situation, nothing would ever change, since all decisions contain some uncertainty.

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<sup>195</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 122

<sup>196</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 86



The second difficulty in the analysis comes from the value of the contribution to national defense made by the Jones Act. Any attempt to determine the economic costs should be weighed against these benefits. Do the ships sailing under the auspice of the Jones Act offer a significant contribution to national defense? If so, does this benefit sufficiently offset the loss in economic efficiency created by the restriction of free trade? An exact estimate of the contribution to national defense (such as the value of the ships that represent defense assets versus the cost of maintaining a separate military reserve fleet) is beyond the scope of this thesis. However, if the ships do not provide a significant benefit, due perhaps to the size of the fleet or the type of ships, then the act would seem to be an undue burden on trade.

### **Niche Markets**

The economic effects of cabotage do not need to be viewed in national terms. Cabotage can also have a significant impact on smaller segments of society, or niches. These niches may possess some characteristic (i.e. geography, industry) that makes them more susceptible to the impacts of the Jones Act.

One such niche is the oil trade. The movement of oil in tankers grew substantially during the period of 1930 through 1950. However, during World War II this trade was significantly curtailed by the use of pipelines when shipping was in short demand. Today, more oil and gas products move by pipeline than by either rail or water.<sup>197</sup>

The discovery of oil in Alaska, and the construction of the Trans-Alaskan pipeline in the 1970's, created a large market for the transportation of oil for domestic carriers.<sup>198</sup>

GAO noted in its evaluation of the ITC reports of 1991, 1993, and 1995, that ITC

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<sup>197</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 176

<sup>198</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 176

predicted a small increase (less than three percent) in domestic oil production in the 1991 report associated with removal of the Jones Act, and a small reduction in oil production associated with removal of the act in the 1995 report.<sup>199</sup>

The rate differential between American flagged and foreign flagged shipping for Alaskan oil transport was determined to be higher than that for other segments of the Jones Act trade. With 90 percent of the domestic cargo consisting of oil carried from Alaska, this is rather significant. Of this oil, 85 percent was transported to the West Coast and 15 percent was transported to the Gulf of Mexico. Transport to the Gulf of Mexico had an even larger rate differential between American flagged and foreign flagged shipping than shipping to the West Coast.<sup>200</sup> These rate disparities could represent an increased burden on this niche market due to the Jones Act. However, GAO pointed out that increased demand on the West Coast and decreased production of Alaska's North Slope oil field eliminated the demand for shipping to the Gulf of Mexico, thus relieving the effect of that segment of the rate differential.<sup>201</sup>

The Great Lakes and their connecting waterways are the largest inland fresh water transportation complex. The St. Lawrence Seaway enables ocean vessels to sail from mid-continent U.S. ports to the rest of the world.<sup>202</sup> Trade on the Great Lakes represents another important niche market under the veil of the Jones Act.

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<sup>199</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 4-5

<sup>200</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 7-8

<sup>201</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 8-9

<sup>202</sup> Heine, Irvin M., pg. 109

As of July 1, 1998, the Great Lakes fleet consisted of 65 large vessels and tug/barge units.<sup>203</sup> This is a significant decline from the 159 U.S. flag vessels, including 136 bulk carriers, thirteen tankers, and nine rail car vessels and ferries, which comprised the Great Lakes fleet as of December 31, 1979.<sup>204</sup> In 1996, the annual revenue of the lakewise trade was \$580 million.<sup>205</sup> That number rose to \$615 million in 1997, fell to \$612 million in 1998, and fell again to \$549 million in 1999.<sup>206</sup> In 1994, shipboard employment in the lakewise trade was 2,045 jobs.<sup>207</sup> By 1999, that number had fallen to 1,344 jobs.<sup>208</sup> So there has been a decline in recent years, despite the existence of the Jones Act.

However, ITC's primary consideration was oceangoing shipping when performing its analysis because it deemed inland and lakewise shipping to be sufficiently competitive to withstand any new competition introduced with the removal of the Jones Act.<sup>209</sup> This was also true in the 1991, 1993, and 1995 reports. In those reports ITC concluded that repeal of the Jones Act would not result in the loss of jobs in the lakewise or inland waterways trades.<sup>210</sup>

ITC did take into account water transportation other than coastwise trade (i.e. Great Lakes and inland waterways) as a secondary consideration when estimating the effects of liberalization. In 1999, ITC estimated that other water transportation sectors

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<sup>203</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 88

<sup>204</sup> Heine, Irvin M., pg. 109

<sup>205</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 89

<sup>206</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 118

<sup>207</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 89

<sup>208</sup> Effects of Significant U.S. Import Restraints: Third Update 2002, pg. 118

<sup>209</sup> Effects of Significant U.S. Import Restraints: Second Update 1999, pg. 97

<sup>210</sup> Maritime Issues: Assessment of the International Trade Commission's 1995 Analysis of the Economic Impact of the Jones Act, pg. 6

would gain 510 full-time jobs and would increase output by \$104 million.<sup>211</sup> In 2002, ITC estimated that other water transportation sectors would lose 650 full-time jobs and output would fall by \$131 million.<sup>212</sup>

Finally, one of the largest niches in the Jones Act trade is the State of Hawaii. America's fiftieth state is infamous for its extremely high cost of living; the cost of paradise. As an island chain, Hawaii relies heavily on goods imported from the contiguous United States.

Citing independent consultants, Hawaiian State Representative Gene Ward estimated that Hawaiian residents pay an additional \$1 billion per year in higher prices due to the Jones Act. That number would correspond to approximately \$3,000 per Hawaiian household.<sup>213</sup>

In response to Rep. Ward's claim, R.J. Pfeiffer, chairman emeritus of Matson Navigation Co., cited a report by the University of Hawaii that concluded that repeal of the Jones Act would result in an annual loss per Hawaii household of between \$611 and \$3,563 and the loss of up to 17,025 jobs.<sup>214</sup> In a statement issued April 7, 1997, Congressman Neil Abercrombie, a democrat from Hawaii, cited a study by Mercer Management Consulting, Inc., that determined the added cost of consumer goods in Hawaii due to shipping to be approximately four percent.<sup>215</sup> Testifying on September 15, 1998, before the Senate Committee on Commerce, Science and Transportation, Donald T. Bollinger, Chairman and CEO of Bollinger Shipyards, Inc. and Chairman of the National

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<sup>211</sup> *Effects of Significant U.S. Import Restraints: Second Update 1999*, pg. 100

<sup>212</sup> *Effects of Significant U.S. Import Restraints: Third Update 2002*, pg. 126

<sup>213</sup> Ward, Gene, "To Fix Economy, Junk the Jones Act," *Honolulu Star-Bulletin*, December 5, 1997

<sup>214</sup> Pfeiffer, R.J., "Jones Act Serves Hawaii and the Nation Very Well," *Honolulu Star-Bulletin*, December 26, 1997

<sup>215</sup> Abercrombie, Neil, "Statement of Congressman Neil Abercrombie: The Jones Act and Hawaii," April 7, 1997, Available: <http://www.house.gov/abercrombie/jones.htm>

Shipyards Association, also cited Mercer Management Consulting, Inc., as placing the additional cost of consumer goods due to vessel construction in the United States to be only 0.29 percent.<sup>216</sup>

A study performed by Matson Navigation Company estimated that if its Hawaiian fleet had been built in foreign yards, the overall level of freight rates could be reduced by approximately 9.7 percent. Supporters of the Jones Act argue that if Matson's freight rates represented between seven and eight percent of retail prices in Hawaii, that when this percentage is multiplied by the 9.7 percent that the resulting change is less than one percent.<sup>217</sup> R.J. Pfeiffer used this same report to argue that if foreign-built ships entered the Hawaiian trade the reduction in consumer prices would be minimal.<sup>218</sup>

It is important to note that virtually all of the people who made arguments for or against the Jones Act as it relates to Hawaii have some political or professional affiliation that may result in bias. This does, however, demonstrate that there is a large debate surrounding the issue with varying points of view. This debate and the politics surrounding the Jones Act is the focus of the next section of this thesis. It is also important to note that, regardless of what numbers you use, Hawaii is still an island state that depends heavily on shipping and any increased cost in shipping rates is going to lead to higher consumer prices. The restrictive policies of the Jones Act definitely impose an added cost on both Hawaii and the nation as a whole. Estimates of this added cost vary

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<sup>216</sup> Bollinger, Donald T., "Testimony of Mr. Donald T. Bollinger, Chairman & CEO, Bollinger Shipyards, Inc. on the Freedom to Transport Act of 1998 (S.2390) Before the Senate Committee on Commerce, Science and Transportation," September 15, 1998, Available: <http://commerce.senate.gov/hearings/0915bol.pdf>

<sup>217</sup> Haskell, Arthur J., "Discussion-The Jones Act: Foreign-Built Vessels and the Domestic Shipping Industry," SNAME Transactions, Vol. 91, 1983, pg. 184-185

<sup>218</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 27

greatly, but it exists none the less and must be weighed against the benefit of national defense.

STUDY	BUILD RESTRICTION	COSTS		INDUSTRY	JOBS		OTHER SECTORS	Liberalization)
		(1950 - 1970)	TOTAL COST		(For Complete)			
Jantscher (1975)	\$1 Billion	(1950 - 1970)	\$3 Billion	(1950 - 1970)	N/A		N/A	
General Accounting Office (1980)	Just Cost to Government		\$71.4-\$78.6 Million	(for 1980)	N/A		N/A	
Congressional Budget Office (1984)	N/A		\$1.3 Billion	(for 1983)	N/A		N/A	
International Trade Commission (1991)	N/A		\$9.8 Billion	(annually)	N/A		N/A	
International Trade Commission (1995)	N/A		\$2.8 Billion	(annually)	2450	Lost	N/A	
International Trade Commission (1999)	\$138-\$380 Million	(annually)	\$1.32 Billion	(annually)	6950	Lost	7850	Gained
International Trade Commission (2002)	\$261 Million	(annually)	\$656 Million	(annually)	11480	Lost	7230	Gained

**Table 6: A Summary of the Costs of Cabotage**

## **A Political Evaluation of the Jones Act**

The debate surrounding cabotage laws in the United States has existed nearly as long as the laws themselves. Political groups, politicians, and citizens have aligned themselves with various viewpoints concerning cabotage. Initial protectionist legislation was passed in response to similar laws enacted by Great Britain and other European powers that prohibited American ships from their trades.<sup>219</sup> As mentioned earlier, Thomas Jefferson argued “that shipping and sea commerce is essential to American industry and economic balance and that the merchant vessel in times of war is the very core of successful naval and expeditionary operations.”<sup>220</sup> So, political support can be traced back to the nation’s beginning.

Great Britain repealed its Navigation Acts in 1849, yet American exclusionary laws remained in place unchanged.<sup>221</sup> Following the Civil War, the attempt to admit foreign built ships (also known as “free ships”) was made, unsuccessfully, to revitalize the merchant marine. Free ships remained an issue through out the latter half of the 19<sup>th</sup> century.<sup>222</sup> Those who supported free ships advocated repeal of the basic cabotage principles of the Navigation Act of 1798.<sup>223</sup>

In 1920, the Jones Act was passed and the nation’s cabotage laws, as they exist today were enacted. President Wilson appointed Admiral William Benson to the chairmanship of the Shipping Board to pursue his agenda. Benson supported and pushed for very tough discriminatory measures with American involvement in all shipping

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<sup>219</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 2

<sup>220</sup> Cuneo, Joseph J., pg. 63

<sup>221</sup> Whitehurst, Clinton H., *The U.S. Merchant Marine*, pg. 2

<sup>222</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 172

<sup>223</sup> Kilmarx, Robert A., et al., pg. 69

affairs. President Wilson signed the Merchant Marine Act of 1920 on June 5, 1920.<sup>224</sup> Senator Jones commented on the act, “They say it will drive foreign shipping from our ports. Granted; I want it to do it.”<sup>225</sup> Interestingly, the majority of the debate did not focus on section 27, but rather on three sections which extended coastal protection to the Philippines, granted preferential inland railroad rates to American cargoes shipped in American vessels, and that ordered the president to repeal any treaties that conflicted with American ability to employ discriminatory policies.<sup>226</sup> Clearly, Senator Jones supported the exclusion of foreign shipping and the lack of debate may suggest others did as well. The lack of debate may also suggest merely that the other sections were more inflammatory and that other political forces were at work.

“Working with Senator Wesley Jones of the Commerce Committee, Benson rushed through Congress the Jones or Merchant Marine Act of 1920, virtually without congressional debate and with no recorded vote. A not fully recovered President Wilson signed the bill on 5 June 1920 after the most cursory discussion in the cabinet.”<sup>227</sup>

In fact, Wilson’s attitude began to shift back to benevolence toward foreign nations when he struck down section 34 and a moratorium was issued on the Philippines provision.<sup>228</sup>

“Wilson’s action to strike down the discriminatory features of the Jones Act clarified an important shift in his attitude toward foreign affairs. In 1919 and early 1920, Wilson’s reactions to Allied diplomatic and commercial maneuverings and to the debate over the League of Nations at home had left him a bitter man. The Merchant Marine Act of 1920 had reflected that bitterness; in fact, it had

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<sup>224</sup> Kilmarx, Robert A., et al., pg. 136

<sup>225</sup> De La Pedraja, René, *The Rise and Decline of U.S. Merchant Shipping in the Twentieth Century*, Twayne Publishers, New York, NY, 1992, pg. 62

<sup>226</sup> Kilmarx, Robert A., et al., pg. 138

<sup>227</sup> De La Pedraja, René, pg. 62

<sup>228</sup> Kilmarx, Robert A., et al., pg. 138-139



taken the issue a step too far. Recognizing this, Wilson tempered debate over discriminations during the summer and struck out in an old direction-by applying equality of treatment in domestic matters, and by ‘standing for right and justice as towards individual nations’”<sup>229</sup>

This change in attitude signified a softening in Wilson’s attitude toward protectionism, but Section 27 remained intact.

Today, the debate surrounding the Merchant Marine Act of 1920 and its protectionist clauses remains as intact as Section 27. Various politicians have voiced support for the act, for revision of the act, or for repeal of the act. Lobbying groups have formed to support the act and to support modification or repeal of the act. Other groups and citizens have voiced opinions on the act and many suggestions have been made as to what direction the act and national maritime policy should take.

In 1983, Warren G. Leback, then Deputy Administrator of the Maritime Administration, and attorney John W. McConnell Jr., published a paper with the Society of Naval Architects and Marine Engineers entitled “The Jones Act: Foreign-Built Vessels and the Domestic Shipping Industry.” They concluded that the objectives of the national maritime policy, as set out by the Merchant Marine Acts of 1916, 1920, and 1936, to have a merchant marine “sufficient to carry domestic waterborne commerce and a substantial portion of the waterborne export and import foreign commerce of the United States” and “capable of serving as a naval and military auxiliary in times of war or national emergency” are not always complementary and at times contradictory.<sup>230</sup>

They argued that the needs of a merchant fleet during a time of war are often not the same as the needs of a merchant fleet to meet the demands of commerce during peace

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<sup>229</sup> Kilmarx, Robert A., et al., pg. 139

<sup>230</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 179

time. Often different types and quantities of vessels are needed. Thus they believed that the ability of the shipyard base to expand and construct the necessary vessels during periods of national emergency was most important. They also pointed out that during peace time, ship construction must be competitive to maintain an efficient fleet and to maintain the shipyard base.<sup>231</sup>

“However, during normal periods if the vessels to transport domestic ocean-borne commerce must be built in the United States, then these vessels must be not only of the type and have the characteristics necessary to transport such cargo in the most efficient manner and on the most reasonable terms but also competitive in terms of their capital cost. If such vessels are not competitive in cost, there will be no need for, and thus no construction of, the vessels, resulting in an inadequate domestic merchant marine and a lesser number of qualified U.S. operators, officers, and seamen (and a reduced shipbuilding base.) However, if vessels that are competitive in types, efficiency and cost are constructed in foreign shipyards and allowed to be registered under U.S. laws for use in the domestic trades, then there will be vessels available to meet the needs of the domestic ocean commerce (and emergency and war needs) and operated and manned by a greater number of U.S. citizens (with no change in the shipyard base since such vessels otherwise would not be constructed in U.S. shipyards).”<sup>232</sup>

They then suggested ten changes to the maritime policy of the United States that they believed would allow the stated objectives to be achieved and would revitalize the anemic industry. They were as follows: 1) Any American built vessel which subsequently is transferred to foreign ownership, or registry, may be re-transferred to American ownership and enrollment to transport merchandise in the coastwise trades. 2) Any vessel constructed in and documented under the laws of the United States, but subsequently rebuilt, regardless of the location or extent of rebuilding, may be permitted

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<sup>231</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 179

<sup>232</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 179

to operate in the domestic trades. 3) Allow American citizens to acquire and enroll vessels built abroad under American laws for use in the domestic trades after the effective date of the law amending. The purpose of the effective date requirement was to prevent speculation in foreign vessels and to prevent the transfer of older vessels to American registry for the domestic trade. 4) Allow vessels built abroad and registered under foreign or American laws and which is and has been owned by U.S. citizens for a minimum of three years to have the lawful right to engage in domestic trade, provided such vessel is not less than three years and not more than ten years of age. 5) Repeal the ad valorem import duty on equipment, or any parts thereof, purchased for, or the expense of repairs made abroad upon, an American vessel engaged in the domestic trade. 6) Repeal the penalty on foreign built American flagged vessels carrying passengers in the domestic trade. 7) An ad valorem duty would be levied on any foreign built or foreign rebuilt vessel enrolled under American law to engage in the domestic trade and on spare parts purchased for, and the expense of repairs made in a foreign country upon, any such vessel. 8) Allow vessels built in the United States with the aid of CDS to engage in the domestic trade without any repayment of the subsidy. 9) Present owners of American built and enrolled vessels engaged in the domestic trade would be compensated under certain circumstances to equalize the capital costs of their vessels with those vessels built foreign or in the United States with CDS when in direct competition with such vessels. 10) To maintain the shipyard mobilization base to meet the requirements of national emergencies, a shipbuilding program would be implemented promptly to meet national defense needs. 200 national defense break bulk vessels would be constructed over a ten year period for the National Defense Reserve Fleet with the current fleet being scrapped

as new vessels are delivered. This program would support four major shipyards in addition to the five major shipyards engaged in naval construction.<sup>233</sup>

Supporting their plan, Leback and McConnell concluded the following:

“Although the Jones Act is sacrosanct to all elements of the merchant marine and its supporters and any inroads, regardless of extent or merit, are vehemently opposed, the state of the domestic merchant fleet and trades requires immediate and necessary adjustment. The allowance of foreign-built vessels to be enrolled and used in the domestic trade appears to be a disadvantage to the shipbuilding industry. However, when it is noted that the amount of shipbuilding in the United States for such purpose is minimal and that a program for construction of bulk vessels for the NDRF will more than compensate for the vessels that would otherwise be constructed for the Jones Act trade, the shipbuilding base should be preserved. If the lack of domestic shipping is due to the high capital costs of the vessels, then with the ability to use lower-cost foreign-built vessels, the number of vessels, crew members and operators in that trade and the amount of cargo carried should materially increase. If such foreign-built vessels are not competitive in that trade, then no such vessels will be acquired and enrolled under U.S. laws and there will be no loss to the shipbuilding industry. If as a result there is a larger domestic fleet, this will be a distinct advantage to the shipping public and particularly those in the noncontiguous trades where ocean transportation is the only mode of transportation available. To not make such changes in an effort to revive the Jones Act fleet and trade will be an acceptance of the demise of that fleet and trade. Public interest requires this effort before making such acceptance.”<sup>234</sup>

Leback and McConnell’s plan for modification of the Jones Act received eighteen responses. Of the eighteen respondents, only four supported the proposal (or any major

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<sup>233</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 180-181

<sup>234</sup> Leback, Warren G. and McConnell, John W. Jr., pg. 181

modification of the Jones Act). The other fourteen attacked the proposal on some level and expressed support for the Jones Act.<sup>235</sup> Some of the responses are as follows:

“As a result of current adverse trends, a shortfall of about 40,000 skilled shipyard workers in any major mobilization effort is now foreseen. This critical deficiency will not be corrected by exporting domestic shipbuilding opportunities or by foreclosing domestic ship repair opportunities through repeal of the 50 percent ad valorem duty on other than emergency repairs to U.S.-flag vessels in foreign shipyards. The authors seem wholly oblivious to the long-standing relationship between the Jones Act and national security. Their fanciful proposals would undermine this historic affinity, and, in the process, decimate an essential component of the U.S. shipyard industry.”<sup>236</sup>

“Our shipyards do not compete in a fair marketplace. Most foreign shipyards are heavily subsidized by their governments as national policy. I take great issue with the authors’ basic assumption that U.S. shipyards are noncompetitive. U.S. shipyards are technologically up to date and productive but it is impossible for a commercial concern to compete against such odds.

“The need today, before we completely lose our shipbuilding base, is to not only preserve the Jones Act intact, but, more importantly, to reassess our overall national maritime policy. The administration and Congress must address this problem before it is too late.

“If the shipyard problem is solved, the revival of the Jones Act fleet will automatically follow.”<sup>237</sup>

“I strongly oppose this proposition that would destroy the existing Jones Act structure, unnecessarily cost the taxpayer several billion dollars, and further decrease the shipyard and suppliers mobilization base for defense.”<sup>238</sup>

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<sup>235</sup> Leback, Warren G. and McConnell, John W. Jr., (Discussion), pg. 182-191

<sup>236</sup> Rice, M. Lee, “Discussion-The Jones Act: Foreign-Built Vessels and the Domestic Shipping Industry,” SNAME Transactions, Vol. 91, 1983, pg. 182

<sup>237</sup> Renshaw, Edward, “Discussion-The Jones Act: Foreign-Built Vessels and the Domestic Shipping Industry,” SNAME Transactions, Vol. 91, 1983, pg. 183

<sup>238</sup> Turner, James E., “Discussion-The Jones Act: Foreign-Built Vessels and the Domestic Shipping Industry,” SNAME Transactions, Vol. 91, 1983, pg. 184

As discussed in earlier sections, there is some debate over what effect removal or modification of the Jones Act would have on the industry. Leback and McConnell obviously feel that the changes they suggest are needed to arrest the decline of the industry. However, some of the respondents felt that removal or modification would simply end up hurting the industry, not help it.

“DOT was successful in 1982 in obtaining a waiver of the requirement that U.S.-flag foreign-trading vessels be built or rebuilt in domestic shipyards. Orders for 49 ships were placed, and resulted in the export of 30,000 shipyard jobs.”<sup>239</sup>

“In conclusion, the authors are asking the country to sacrifice permanently about 10,000 Jones Act jobs in exchange for a very vulnerable NDRF upgrading program. I fail to see any incentive. I can only hope that this important paper, prepared by Administration insiders, will prod into action those of us who believe that the Administration’s ‘build foreign’ policy is detrimental to U.S. interests.”<sup>240</sup>

Some of the responses supported the proposal, or supported modification of the Jones Act, in some way.

“Anyone who understands the long-term benefits of free-market economics should applaud what the authors propose. Their recommendations might well lead to a revival of our once-thriving coastwise trade-leading, in turn, to important economic benefits to those who pay to have goods shipped. The general public, of course, stands to gain the most-through reduced prices for consumer goods”<sup>241</sup>

“Vessel owners have been forced to rehabilitate existing tonnage rather than construct new or modern ships because of the high cost of new production. As a result, the current policy is producing the precise reverse of its objectives.

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<sup>239</sup> Turner, James E., pg. 184

<sup>240</sup> Lowry, Robert, “Discussion-The Jones Act: Foreign-Built Vessels and the Domestic Shipping Industry,” SNAME Transactions, Vol. 91, 1983, pg. 189

<sup>241</sup> Benford, Harry, “Discussion-The Jones Act: Foreign-Built Vessels and the Domestic Shipping Industry,” SNAME Transactions, Vol. 91, 1983, pg. 188

Instead of an expanding, modern fleet, we have produced a declining, antiquated domestic fleet.

The United States must adopt policies that produce a modern waterborne offshore transportation system. A country with our coastline should have passenger and car ferries bustling up and down the coasts. It should have a system of waterborne dry cargo transportation off the coasts that would make efficient use of our great harbors and ports. Such a fleet would be available for military contingencies as well.”<sup>242</sup>

Some of the responses did not even address the problem of the declining shipbuilding industry.

“If you, Mr. Leback, feel you are following the ‘Code of Ethics’ adopted by the Society in 1923, I challenge you to tell us how the fall of the shipbuilding industry will meet the charges of ‘loyalty to his country’ or ‘cooperate in upbuilding the professions of naval architecture and marine engineering.’ This is not the forum for politics. Go back to Washington and politic. Please don’t insult naval architects and marine engineers.”<sup>243</sup>

While this last passage does not directly comment on the merits of the proposal or the state of the shipbuilding industry and Jones Act fleet, it does clearly show the emotional context of the issue. The debate surrounding the Jones Act can be very heated and is very personal to many of the participants.

Other analyses have been performed on the Jones Act and other suggestions have been made on how to modify the act and remedy the decline of the industry. In his 1985 analysis, *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, Clinton H. Whitehurst Jr. made several suggestions for “making the Jones Act as economically efficient as possible and maintaining a merchant marine and shipyard

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<sup>242</sup> Bowman, Roy G., “Discussion-The Jones Act: Foreign-Built Vessels and the Domestic Shipping Industry,” SNAME Transactions, Vol. 91, 1983, pg. 190

<sup>243</sup> Zankich, L. Paul, “Discussion-The Jones Act: Foreign-Built Vessels and the Domestic Shipping Industry,” SNAME Transactions, Vol. 91, 1983, pg. 185

mobilization base.”<sup>244</sup> His suggestions were as follows: 1) Foreign built ships would be allowed in the noncontiguous domestic trades, but the requirement that they be American-flagged and American-crewed would be maintained. The Virgin Islands would be included under this stipulation. 2) Foreign-flagged, Foreign-crewed vessels would be permitted in the coastal and intercoastal trades given that the vessels were American owned and controlled as outlined by the Department of Defense. A condition for entry by an American firm would be that it build under a CDS program, and operate under the American flag, a tanker or bulk carrier in the U.S. foreign trade on a one-for-one basis. 3) To maintain the desired shipyard mobilization base the federal government would fund CDS on a long term basis to maintain a fleet of approximately 150 tankers and bulk carriers. 4) The ad valorem tax on American-flagged ship repairs in foreign yards would be reduced from 50 to 25 percent.<sup>245</sup>

Whitehurst concluded that there were two important considerations for judging modification of the Jones Act. First is the competitiveness of American crews (specifically with regard to wages) with foreign crews. If the size of crews continues to decrease, and wages remain moderate, then American crews may become competitive with their foreign counterparts. However, the second consideration is the cost of domestic vessel construction, which Whitehurst believed could never compete with foreign shipyards. Since shipyards are crucial to national defense, the government should

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<sup>244</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 37

<sup>245</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 37-39



support them directly when needed. With these two considerations accounted for, American shipping could become competitive.<sup>246</sup>

The debate of proposed changes and their opposition was discussed here for two reasons. First, these proposed changes point out what some believe to be the weaknesses of the Jones Act and the industry it serves and some of the remedies suggested. These weaknesses and remedies are not uniformly recognized. Second, it also demonstrates how politically charged this issue is simply through the debate for and against these proposals. The Jones Act has attained many staunch supporters and opponents.

In the late 1990's this debate became the focus of two special interest groups that were diametrically opposed. The Jones Act Reform Coalition formed to seek change in the Jones Act. The Maritime Cabotage Task Force formed to support the Jones Act.<sup>247</sup>

The Jones Act Reform Coalition (JARC) claimed the Jones Act resulted in a significant loss to the American economy and resulted in a substantial loss of revenue for the government. On top of this, JARC believed that act actually resulted in the loss of a large number of jobs, while only protecting a relatively small number of jobs. JARC believed that the Jones Act permitted a monopoly for the few domestic carriers it protects while smaller businesses suffer. They also believed that the Act has failed with regard to its objective of supporting a strong national merchant marine and has left ships, shipyards, terminals, and others vulnerable to open ended liability claims.<sup>248</sup>

JARC cited the 1991 ITC study and predicted that U.S. Treasury would lose \$21 billion dollars in lost revenue over seven years. Furthermore, JARC claimed that more

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<sup>246</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 39

<sup>247</sup> Hubbard, Joseph A., pg. 24,27

<sup>248</sup> Hubbard, Joseph A., pg. 27-28

than 40,000 maritime jobs had been lost since 1950 under the Jones Act. JARC was denied access to employment information from Jones Act carriers, but JARC estimated, based on government data, that approximately 173,500 jobs were associated with the maritime industry. Of those, only 3,000 were related to deepwater, coastwise and intercoastal Jones Act vessels. The remaining 170,500 jobs were on inland waterway barges, dredges, and tugs or associated with marine cargo handling and are effectively protected by U.S. labor and immigration laws. JARC claimed that the Coastal Shipping Competition Act would not affect these jobs.<sup>249</sup>

JARC argued that the Jones Act had a substantial impact on American business. Again citing the 1991 ITC study, JARC claimed that large American carriers received approximately \$635 million in “benefits” from Jones Act protection while the overall cost to the national economy was \$10.4 billion. JARC also claimed that the Jones Act hurts small businesses by making entry into the domestic trade nearly impossible. Raised capital costs and labor costs, as well as increased legal exposure, associated with the Jones Act is more than small business can surmount.<sup>250</sup>

JARC also cited the decline of the shipbuilding industry as incentive for the act. They claim while shipbuilding accounts for nearly 50,000 jobs in the United States, commercial building only supports approximately 1,700 jobs. They cite the failed attempt of Newport News Shipbuilding to profitably build the Double Eagle class tankers, with a loss in excess of \$315 million dollars on the project. JARC also cites the extremely high cost of building in the United States, with the cost of the M/V R.J. Pfeiffer estimated at over \$150 million, or 2.5 times world price and the high cost of

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<sup>249</sup> Hubbard, Joseph A., pg. 28-29

<sup>250</sup> Hubbard, Joseph A., pg. 29

tankers ordered by ARCO, placed at \$165 million each, where the world market price would be approximately \$65 million.<sup>251</sup>

JARC blamed increased exposure to liability (over alternative forms of transport) for further increasing operating costs in the United States. They also claimed that the Jones Act represented an increased burden on the environment by forcing the use of alternative forms of transportation that result in higher emissions. Further, they argued that U.S. environmental laws would still apply to foreign vessels entering American ports. They also believed that non-contiguous routes would benefit from the entry of lower cost foreign shipping.<sup>252</sup>

The Coastal Shipping Competition Act represented an attempt to remedy the perceived problems of the Jones Act. JARC believed the Coastal Shipping Competition Act would create more jobs, create a more competitive domestic waterborne transportation industry, and eliminate the costs associated with the Jones Act. The Provisions of the bill were as follows: 1) American domestic coastal trade would be redefined to include trade on all waters accessible by ocean-going vessels, including the Great Lakes, St. Lawrence Seaway, and inland “mixed waters.” Inland waterborne trade is narrowed in definition to include inland waters not accessible by ocean-going vessels. 2) American-flag requirements would be modified to eliminate American-ownership and build requirements in coastal, intercoastal, and noncontiguous trades. 3) American-labor and build requirements would be retained for inland barge, tow and tug trades. American citizenship ownership requirements in these trades would be dropped. 4) Regularly scheduled liners in the coastal trades must be documented under the new requirements in

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<sup>251</sup> Hubbard, Joseph A., pg. 30

<sup>252</sup> Hubbard, Joseph A., pg. 32-33

the U.S. No documentation requirements would apply to tramps or charters in U.S. trades, or in domestic coastal or intercoastal trades that are part of international shipping movements, up to six voyages per year. 5) "Bowater's" restrictions would be eliminated. This would allow foreign companies in the United States to ship cargoes on their own vessels, allowing an exception where foreign companies could own domestic shipping. 6) Domestic maritime employers would be able to choose workman's injury coverage under the Longshore and Harbor Worker's Compensation Act or an authorized state workman's compensation program as an alternative to Jones Act (FELA) tort remedies. 7) Coast Guard rules for all vessels (American and foreign) in the coastal trades as newly defined would be harmonized with recognized international safety, manning, and marine construction standards. Other currently applicable environmental standards and tax provisions under American law would continue to apply to all vessels operating on a regular basis in American domestic trades.<sup>253</sup>

Senator Jesse Helms of North Carolina introduced the Senate version of the Coastal Shipping Competition Act, S.1813, on May 23, 1996. The bill was cosponsored by two Senators, Conrad R. Burns of Montana and Charles E. Grassley of Iowa. The bill was read twice in the Senate then referred to the Senate Committee on Commerce, Science and Transportation. The bill remained in committee.<sup>254</sup>

On August 2, 1996, Congressman Nick Smith of Michigan introduced H.R. 4006, the House version of the Coastal Shipping Competition Act. The resolution was cosponsored by six other Congressmen; Christopher Cox of California, Thomas W.

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<sup>253</sup> Hubbard, Joseph A., pg. 33-35

<sup>254</sup> "Bill Summary & Status for the 104<sup>th</sup> Congress-S.1813," Available: <http://thomas.loc.gov/cgi-bin/bdquery/z?d104:SN01813:@@L&summ2=m&>

Ewing of Illinois, David Funderburk of North Carolina, Frank D. Lucas of Oklahoma, David M. McIntosh of Indiana, and Thomas E. Petri of Wisconsin.<sup>255</sup>

The bill was originally referred to the House Committee on Transportation and Infrastructure and the House Committee on National Security. The House Transportation and Infrastructure committee then referred the bill to the Subcommittee on Coast Guard and Maritime Transportation on August 15, 1996. The House Committee on National Security requested executive comment from the Department of Defense on August 29, 1996. No further action was taken on the bill during the 104<sup>th</sup> Congress.<sup>256</sup>

The bill was introduced again by Congressman Nick Smith to the 105<sup>th</sup> Congress on June 19, 1997 as H.R.1991. This time the bill had 15 cosponsors; Doug Bereuter of Nebraska, Merrill Cook of Utah, Christopher Cox of California, Jay Dickey of Arkansas, Scott L. Klug of Wisconsin, Tom Latham of Iowa, David M. McIntosh of Indiana, Jerry Moran of Kansas, Charlie Norwood of Georgia, Thomas E. Petri of Wisconsin, Bob Schaffer of Colorado, Joe Skeen of New Mexico, Charles W. Stenholm of Texas, Mac Thornberry of Texas, and Robert A. Underwood of Guam. Congresswoman Jennifer Dunn of Washington initially cosponsored the bill but withdrew her name as a cosponsor on September 23, 1998.<sup>257</sup>

The bill was initially referred to the House Committee on Transportation and Infrastructure and to the House Committee on Armed Services. The House Committee on Transportation and Infrastructure referred the bill to the Subcommittee on Coast

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<sup>255</sup> “Bill Summary & Status for the 104<sup>th</sup> Congress-H.R. 4006,” Available: <http://thomas.loc.gov/cgi-bin/bdquery/z?d104:HR04006:@@L&summ2=m&>

<sup>256</sup> “Bill Summary & Status for the 104<sup>th</sup> Congress-H.R. 4006”

<sup>257</sup> “Bill Summary & Status for the 105<sup>th</sup> Congress-H.R. 1991,” Available: <http://thomas.loc.gov/cgi-bin/bdquery/D?d105:1./temp/~bdMoXg:@@L&summ2=m&/bss/d105query.html>

Guard and Maritime Transportation on July 3, 1997. The bill again remained in committee.<sup>258</sup>

The most recent attempt to pass the Coastal Shipping Competition Act took place during the 107<sup>th</sup> Congress. Congressman Nick Smith introduced the bill again on May 26, 2001 without cosponsors. The bill was again referred to the House Committee on Transportation and Infrastructure and the House Armed Services Committee. The Committee on Transportation and Infrastructure referred the bill to the Subcommittee on Coast Guard and Maritime Transportation. The House Armed Services Committee requested executive comment from the Department of Defense. No further action was taken on the bill.<sup>259</sup>

The Coastal Shipping Competition Act is not the only bill to be introduced during this time period. On July 30, 1998, Senator Sam Brownback of Kansas introduced the Freedom to Transport Act, S.2390, during the 105<sup>th</sup> Congress. Five Senators cosponsored the bill; Conrad R. Burns of Montana, Chuck Hagel of Nebraska, Jesse Helms of North Carolina, Richard G. Lugar of Indiana, and Pat Roberts of Kansas.<sup>260</sup>

The bill was intended to “exempt from the prohibition against transportation of merchandise in the coastwise trade in any vessel other than one built and documented under U.S. law certain foreign built vessels issued a certificate of documentation for the coastwise trade that are used to transport forest products, bulk cargo (including agricultural products carried in bulk), or livestock.”<sup>261</sup>

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<sup>258</sup> “Bill Summary & Status for the 105<sup>th</sup> Congress-H.R. 1991”

<sup>259</sup> “Bill Summary & Status for the 107<sup>th</sup> Congress-H.R. 2046,” Available: <http://thomas.loc.gov/cgi-bin/bdquery/D?d107:1:./temp/~bdqzLf:@@L&summ2=m&/bss/d107query.html>

<sup>260</sup> “Bill Summary & Status for the 105<sup>th</sup> Congress-S.2390,” Available: <http://thomas.loc.gov/cgi-bin/bdquery/D?d105:1:./temp/~bdim1J:@@L&summ2=m&/bss/d105query.html>

<sup>261</sup> “Bill Summary & Status for the 105<sup>th</sup> Congress-S.2390”

The bill was read twice and then referred to the Senate Committee on Commerce, Science and Transportation. The Committee on Commerce, Science and Transportation held hearings on the legislation, but the bill never left committee.<sup>262</sup>

The Freedom to Transport Act was introduced again by Senator Sam Brownback, during the 106<sup>th</sup> Congress, on May 13, 1999 as Senate resolution S.1032. The act was again cosponsored by Senators Burns, Helms, Lugar and Roberts with the addition of Senator Peter Fitzgerald of Illinois. The act was again read twice and referred to the Senate Committee on Commerce, Science and Transportation. The act remained in committee.<sup>263</sup>

On July 24, 2003, Congressman Ed Case of Hawaii introduced three bills to amend the Jones Act without cosponsors. The first, H.R. 2845, the United States Noncontiguous Shipping Open Market Act of 2003, would amend the Jones Act to due the following:

**“Amends the Merchant Marine Act, 1920, to make the requirement that all cargo shipping between U.S. ports occur exclusively on U.S. flagged vessels inapplicable with respect to transportation in noncontiguous trade of merchandise on a foreign qualified freight vessel for which the Secretary of Transportation has issued a certificate of documentation.**

**“Amends the Shipping Act, 1916, to repeal certain requirements regarding: (1) the percentage of ownership of a corporation operating in coastwise trade owned by U.S. citizens; and (2) seizure and forfeiture of documented vessels.**

**“Requires jurisdiction for an action brought for recovery for injury to or death of a seaman against a defendant employer that does not reside or maintain an office in the**

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<sup>262</sup> “Bill Summary & Status for the 105<sup>th</sup> Congress-S.2390”

<sup>263</sup> “Bill Summary & Status for the 106<sup>th</sup> Congress-S.1032,” Available: <http://thomas.loc.gov/cgi-bin/bdquery/D?d106:1:./temp/~bd6Axj:@@L&summ2=m&/bss/d106query.html>

United States and that engages in any enterprise that makes use of one or more ports in the United States to be under the district court most proximate to the place of the occurrence of the personal injury or death that is the subject of the action. Authorizes the employer of a master or member of the crew of a vessel, at the employer's election, to participate in an authorized compensation plan under the Longshore and Harbor Workers' Compensation Act.

“Subjects all vessels operating in the U.S. coastwise trade to minimum international labor and environmental standards. Sets requirements for non-citizens irregularly engaging in the U.S. domestic coastwise trade.”<sup>264</sup>

The United States Noncontiguous Shipping Open Market Act of 2003 was referred to the House Committee on Transportation and Infrastructure and the House Armed Services Committee. The Committee on Transportation and Infrastructure referred the bill to the Subcommittee on Coast Guard and Marine Transportation on July 25, 2003. That same day, introductory remarks were given on the measure and there has been no further activity regarding the bill.<sup>265</sup>

The second bill introduced by Congressman Case was the Hawaii Shipping Open Market Act of 2003, H.R. 2846. This bill would stipulate the same changes as the first act introduced by Case but would apply to only Hawaii, rather than all of the noncontiguous trades. The bill was referred to the House Committee on Transportation and Infrastructure and the House Armed Services Committee. The Committee on Transportation and Infrastructure referred the bill to the Subcommittee on Coast Guard

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<sup>264</sup> “Bill Summary & Status for the 108<sup>th</sup> Congress-H.R.2845,” Available: <http://thomas.loc.gov/cgi-bin/bdquery/D?d108:1:./temp/~bdah0M:@@@L&summ2=m&/bss/d108query.html>

<sup>265</sup> “Bill Summary & Status for the 108<sup>th</sup> Congress-H.R.2845”



and Marine Transportation on July 25, 2003 and introductory remarks were made for the bill the same day. No further action has been taken.<sup>266</sup>

The third and final bill introduced by Congressman Case was the Hawaii Agriculture/Livestock Shipping Open Market Act of 2003, H.R. 2847. This act would stipulate the same changes as the prior two acts, except that it would apply only to the transportation of forest products, agricultural products, or livestock in the Hawaiian trade. The bill was referred to House Committee on Transportation and Infrastructure and the House Armed Services Committee. It was in turn referred to the Subcommittee on Coast Guard and Maritime Transportation on July 25, 2003. Introductory remarks were read on July 25, 2003 as well and no further action has been taken on the bill.<sup>267</sup>

After failing to pass any legislation through Congress to reform the Jones Act, the Jones Act Reform Coalition dissolved in 2000.<sup>268</sup> During the same time period that JARC was trying to change the nation's cabotage laws, the Maritime Cabotage Task Force (MCTF) formed to support the Jones Act and fight against the attempts to modify or repeal the law.<sup>269</sup>

The Maritime Cabotage Task Force argued that the Jones Act has been very successful in maintaining a strong American domestic fleet. They claimed that large productivity gains were made over the last thirty years resulting in a larger, faster, more productive fleet. One of the largest measures of enhanced productivity was the increased

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<sup>266</sup> "Bill Summary & Status for the 108<sup>th</sup> Congress-H.R.2846," Available: <http://thomas.loc.gov/cgi-bin/bdquery/D?d108:1:./temp/~bd9xfa:@@L&summ2=m&/bss/d108query.html>

<sup>267</sup> "Bill Summary & Status for the 108<sup>th</sup> Congress-H.R.2847," Available: <http://thomas.loc.gov/cgi-bin/bdquery/D?d108:1:./temp/~bdCQK7:@@L&summ2=m&/bss/d108query.html>

<sup>268</sup> "Jones Act Updates," Lake Carriers' Association website, Available: <http://www.lcaships.com/JANEWS.HTM>

<sup>269</sup> Hubbard, Joseph A., pg. 23

use of barges which they claim the opposition neglects to recognize the use of in analyzing productivity.<sup>270</sup>

MCTF claimed the Jones Act contributed \$15 billion to the U.S. economy annually, including \$4 billion in direct wages to American citizens. In turn, that \$4 billion in wages generated \$1.4 billion in federal and state taxes each year. MCTF stated the value of Jones Act cargo transported annually amounted to \$222 billion, or 3.3 percent of GNP. Meanwhile, Jones Act freight charges totaled less than \$12 billion annually, or less than 0.2 percent of GNP.<sup>271</sup>

MCTF claimed that the decline in the number of ships in the fleet is due to the replacement of older, smaller ships with newer, larger, more reliable, and more efficient vessels and that the liner trades have actually grown. They also claimed that there are approximately 124,000 jobs that fall under the Jones Act, 80,000 of which are on-board positions.<sup>272</sup>

Acknowledging that the U.S. shipping industry is highly competitive, MCTF claimed the barriers to entry were not a result of high capital cost for domestic ships, but rather due to the low margins provided by current freight rates.

MCTF credited the Jones Act in driving maritime innovations, through competition with other modes of transportation, such as the containership, the double-hulled tank barge, the Great Lakes self-unloader, and the chemical parcel tanker. They also credited the Jones Act with protecting nearly 44,000 vessels comprising the total Jones Act fleet, including containerships, coastal tankers, inland grain tows, dredges,

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<sup>270</sup> Hubbard, Joseph A., pg. 23

<sup>271</sup> Hubbard, Joseph A., pg. 23

<sup>272</sup> Hubbard, Joseph A., pg. 24

Great Lakes self-unloaders, and passenger ferries, which carry one billion tons of cargo and 80 million passengers annually.<sup>273</sup>

MCTF associated the lack of freighters operating on the East Coast with market-driven factors and not the Jones Act. Shipping costs and capabilities along the East Coast resulted in transporting by water often being a less economical choice. Costs associated with moving goods from port facilities to facilities inland, and vice versa, can be avoided through direct overland transportation. The small sizes that these shipments often comprise also make shipping by rail or truck more practical and efficient.<sup>274</sup>

MCTF pointed out that there were more than 120 vessels serving the U.S. noncontiguous trades. Ten self-propelled vessels and nineteen tug-barge units moved more than fifteen million tons of cargo to Puerto Rico annually. More than 67 vessels, including sixteen tug-barge units, served the Alaskan trade, moving more than 105 million tons of cargo annually worth approximately \$21 billion. Twenty vessels served the Hawaiian trade, moving 21 million tons of cargo worth \$46 billion annually. MCTF argued this represents a healthy market. MCTF also credits the use of barges with revolutionizing the domestic trades.<sup>275</sup>

With these arguments, MCTF claimed that the Jones Act has been very successful and abandoning or modifying the act would be detrimental to the domestic shipping industry and the national defense service it provides. However, it is important to note whom MCTF represents. MCTF's constituents are mostly operators, shipbuilders, designers, intermodal carriers, and marine suppliers. All have made large investments in the current domestic shipping industry. They set up a system of operation under the

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<sup>273</sup> Hubbard, Joseph A., pg. 25

<sup>274</sup> Hubbard, Joseph A., pg. 25

<sup>275</sup> Hubbard, Joseph A., pg. 25-26

current rules, which have been around for a long time, and they want to protect that investment from what they see as unfair competition.<sup>276</sup>

The representation of special interests is not restricted to only the Jones Act Reform Coalition and the Maritime Cabotage Task Force. Other organizations have voiced support for the Jones Act or for Jones Act repeal or reform.

The Lake Carriers' Association is an organization representing U.S.-flag vessel operators on the Great Lakes. The Lake Carriers' Association strongly supports the Jones Act. When Congressman Nick Smith introduced the Coastal Shipping Competition Act, they wrote him several open letters outlining their position, their support for the Jones Act, and what they feel are the strengths of the Jones Act and the trade it supports.<sup>277</sup>

Another organization that strongly supports the Jones Act is the Gulf Coast Mariners Association. They tout the importance of the Jones Act in securing the maritime industry, the benefit they believe it provides the economy, and the important role the act plays in national security. They support the act and urge mariners to do the same.<sup>278</sup>

Many special interests have also taken a stance supporting repeal or modification of the Jones Act. The American Feed Industry Association, which represents the animal feed and pet food industries and their suppliers, opposes the Jones Act. The following is a statement of their position:

“AFIA supports free trade and market access, as well as the most efficient, competitive and cost-effective methods of moving U.S. goods to foreign buyers to take advantage of new and potential markets. AFIA supports reforms of cargo

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<sup>276</sup> Hubbard, Joseph A., pg. 43

<sup>277</sup> “Jones Act Updates,” *Lake Carriers' Association website*

<sup>278</sup> “The Jones Act: It’s Your Fight! It’s Your Right,” Gulf Coast Mariners Association, Available: <http://www.gulfcoastmariners.org/issuesjonesact.htm>

preference laws to bolster export promotion efforts and maintain U.S. competitiveness.”<sup>279</sup>

Thus, they clearly are against the Jones Act, preferring instead free market access so as to reduce transportation costs.

The salt industry is another industry that voiced its support of Jones Act reform clearly when the president of the Salt Institute, Richard L. Hanneman, sent a letter, dated May 20, 1999, to Senator John McCain, Chairman of the Senate Committee on Commerce, Science and Transportation, urging support for the Freedom to Transport Act. Citing costs to the economy, the Salt Institute urged Senator McCain to take a leadership role in reforming the Jones Act to create and maintain American economic competitiveness.<sup>280</sup>

These are just a few of the organizations that voiced an opinion on the Jones Act. It is interesting to note that, while the variety of industries represented is quite diverse, it is primarily those involved in the domestic shipping and shipbuilding industries that support the Jones Act. Meanwhile, it is primarily those who must ship goods in the domestic trades that oppose the Jones Act. It is clear that both sides have something substantial to gain or preserve through the positions they take.

Since this issue is so political, politicians have an obvious role. Politicians at various levels of government have aligned themselves with one side or the other of the debate, expressing their opinions publicly.

Due to the fact that Hawaii is an island state and it depends heavily on domestic shipping, the Jones Act has become an important topic there. In an article written for the

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<sup>279</sup> “Jones Act Reform,” American Feed Industry Association, Available:

[http://www.afia.org/Government\\_Affairs/Issue\\_Summaries/Jones\\_Act\\_Reform.html](http://www.afia.org/Government_Affairs/Issue_Summaries/Jones_Act_Reform.html)

<sup>280</sup> Hanneman, Richard L., “Hanneman to McCain on Jones Act Reform, May 20, 1999,” Salt Institute, Available: <http://www.saltinstitute.org/pubstat/mccain5-20.html>

Honolulu Star-Bulletin on December 5, 1997, Republican State Representative Gene Ward vehemently opposed the Jones Act. Representative Ward expressed support for the Coastal Shipping Competition Act and concluded by saying, “If Hawaii is serious about tackling the economic and cost-of-living problems currently facing Hawaii’s families and businesses, the reform of the Jones Act must be near the top of its list.”<sup>281</sup> During the week of January 30, 2004, the Hawaiian State Legislature introduced four bills that called on the United States Congress to either totally exempt or partially waive elements of the Jones Act for vessels operating in the noncontiguous trades.<sup>282</sup>

Hawaii’s representatives to the United States Congress have also weighed in on the debate. As mentioned before, Democratic Congressman Ed Case introduced three bills in July of 2003 to repeal portions of the Jones Act. These bills were an attempt to alleviate the shipping costs in the noncontiguous trades, particularly in the Hawaiian trade.

However, Hawaii’s other member of the United States House of Representatives, Democrat Neil Abercrombie, announced his support for the Jones Act in a statement released April 7, 1997. Congressman Abercrombie cited the dependability of shipping to Hawaii as a necessity that would vanish with the removal of the Jones Act. He believed the economic impact removal of the Jones Act would be severe and that removal would compromise defense capabilities. Concluding, he wrote, “Hawaii and the country need a strong maritime industry, and our maritime industry needs the Jones Act. That’s why we have a strong bipartisan Jones Act coalition in Congress. It is defended by Democrats

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<sup>281</sup> Ward, Gene

<sup>282</sup> “Maritime Update,” *Transportation Institute Website*, Available: [http://www.transinst.org/updates\\_January\\_23\\_\\_04.htm](http://www.transinst.org/updates_January_23__04.htm)

and Republicans alike because it stands as a bulwark of our national security and economic independence.”<sup>283</sup>

Hawaii’s senior United States Senator, Daniel K. Inouye, has also voiced his opinion on the Jones Act. In 1996, Senator Inouye stated, “...Opponents of cabotage would allow foreign operators to compete for all U.S. cargo without the responsibility of complying with all U.S. laws and requirements. That is fundamentally unfair. No other U.S. industry is expected to-or could-compete under these circumstances in our domestic economy... The battle to maintain the integrity of the Jones Act is a battle about national security and about economic security...”<sup>284</sup>

However, in 2002, Inouye reconsidered his position on the Jones Act, stating that he would be willing to allow foreign built ships to enter the American domestic trade if they adhered to American laws. “If there is an American company that has foreign-bottom ship made on foreign soil but is willing to have American crew, operate under American law, pay federal and state taxes and maintain labor management laws as we have here, then I’m for it,” said Inouye to Pacific Business News. Inouye continued to say, “Why do you think they don’t want to do it? They want cheap labor.”<sup>285</sup>

Considering a foreign build amendment represents a deviation from the complete support for the Jones Act that Inouye had shown.

Other members of the Senate have also voiced their opinion on the Jones Act. The Senate version of the Coastal Shipping Competition Act was introduced by Senator Jesse Helms of North Carolina with two cosponsors, Senator Conrad R. Burns of

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<sup>283</sup> Abercrombie, Neil

<sup>284</sup> “Support for Jones Act and Merchant Marine Spans the Political Spectrum,” *Lake Carriers’ Association website*, Available: <http://www.lcaships.com/hpquotes.html>

<sup>285</sup> DiPietro, Ben, “Inouye Would Consider Jones Act Amendments,” *Pacific Business News website*, January 10, 2002, Available: <http://www.bizjournals.com/pacific/stories/2002/01/07/daily62.html>

Montana and Senator Charles E. Grassley of Iowa.<sup>286</sup> Affiliating themselves with this bill is an obvious statement of support for amending the Jones Act.

Senator Sam Brownback of Kansas introduced the Freedom to Transport Act in 1998 and again in 1999. Each time it had five cosponsors, with a total of six Senators cosponsoring either one or both introductions of the bill. They were Senator Conrad R. Burns of Montana, Senator Peter Fitzgerald of Illinois, Senator Chuck Hagel of Nebraska, Senator Jesse Helms of North Carolina, Senator Richard G. Lugar of Indiana, and Senator Pat Roberts of Kansas. Again, by affiliating themselves with this legislation these Senators made obvious statements of support for amending the Jones Act.<sup>287288</sup>

Other prominent members of the Senate have also voiced strong opinions on the Jones Act. Chairman of the Committee on Commerce, Science, and Transportation, Senator John McCain of Arizona strongly opposes the Jones Act as he made clear in remarks he made during a hearing on the Freedom to Transport Act on September 15, 1998.<sup>289</sup>

“As many of you may know, I am a proponent of eliminating barriers to free trade as well as a strong national defense. I understand the Jones Act involves elements of both of these issues.

“I am very concerned about the impact on trade of any barrier. I believe U.S. trade barriers invite other countries to put up or retain their own barriers. I believe the U.S. can compete in any arena it chooses. The philosophy that we need to protect our industries troubles me. Additionally, U.S. trade barriers have real costs for U.S. consumers. While the witnesses today could argue about the magnitude

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<sup>286</sup> “Bill Summary & Status for the 104<sup>th</sup> Congress-S.1813”

<sup>287</sup> “Bill Summary & Status for the 105<sup>th</sup> Congress-S.2390”

<sup>288</sup> “Bill Summary & Status for the 106<sup>th</sup> Congress-S.1032”

<sup>289</sup> McCain, John, “Statement of Senator John McCain, Chairman, Senate Committee on Commerce, Science and Transportation, Full Committee Hearing on S.2390, The Freedom to Transport Act of 1998,” September 15, 1998, Available: <http://commerce.senate.gov/hearings/0915mcc.pdf>



of the cost, there is no doubt that the Jones Act adds costs to U.S. shippers, especially in areas where water transportation is the only economical shipping option, such as Hawaii, Guam, and Puerto Rico.

“In evaluating the claim that the current U.S.-build requirement is required to maintain a military shipbuilding industrial base, I believe other modes of domestic transportation provide some insight. I think most people would agree that the U.S. military aircraft manufacturing base is vital to the national security of the United States. Similar to naval shipbuilding, military aircraft production has declined in recent years. Yet domestic commercial air carriers are allowed to own and operate foreign-built aircraft in the domestic trade. Domestic rail and motor carriers are also allowed to use foreign-built trains and trucks. Additionally, a review of the recent commercial construction history of the U.S. shipyards that build Navy ships would prove informative.”<sup>290</sup>

This statement is pretty strong criticism of the Jones Act. It is obvious that Senator McCain views this barrier to free trade as a detriment and he points to the ability of other transportation sectors, and the craft construction industries that support them, to survive despite foreign competition. However, despite the support for Jones Act reform from these Senators, no legislation has received a vote, nevertheless been passed into law.

This fact, that no reform legislation has been passed, may be a sign that the majority of Senators and Congressman offer some level of support for the Jones Act. The most recent attempt to pass reform legislation, the three bills introduced by Congressman Ed Case of Hawaii, has received little support and the bills were introduced without cosponsors. On April 23, 1997, Congressman John Joseph Moakley of Massachusetts introduced a House resolution announcing congressional support for the Jones Act. The resolution, entitled “Expressing the sense of the Congress that section 27 of the Merchant Marine Act, 1920, popularly known as the Jones Act, and related statutes are critically

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<sup>290</sup> McCain, John

important components of our Nation's economic and military security and should be fully and strongly supported," was cosponsored by 244 Congressman, a clear majority, with one Congressman, Bob Schaffer of Colorado, withdrawing his name as a cosponsor one day after the bill was introduced.<sup>291</sup> With a majority of Congressman voicing support for the Jones Act, it would be difficult to pass any reform.

Support for the Jones Act has not been restricted to the legislative branch of government. Many of America's Presidents have also voiced their support for the Jones Act.

In a campaign speech, delivered to the National Maritime Union in St. Louis, Missouri, on October 9, 1980, President Ronald Reagan (then running for office) said the following:

**"The principle that a nation's own ships should carry its coastal trade, presently embodied in the Jones Act, has been a part of this country's maritime policy since the early days of the nation. I can assure you that a Reagan administration will not support legislation that would jeopardize this longstanding policy or the jobs dependent upon it."**<sup>292</sup>

The Reagan administration then discussed two amendments furthering the reach of the Jones Act in 1982. The first amendment would extend the coastwise laws to the Virgin Islands. The second amendment would extend Jones Act requirements to all vessels or structures (such as offshore drilling rigs) operating or positioned within 200

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<sup>291</sup> "Bill Summary & Status for the 105<sup>th</sup> Congress-H.CON.RES.65," Available: <http://thomas.loc.gov/cgi-bin/bdquery/D?d105:1:./temp/~bd3zMT:@@@L&summ2=m&/bss/d105query.html>

<sup>292</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 29

miles of the United States coastline, or the offshore economic zone. However, neither of these amendments was achieved and the attempts were shelved.<sup>293</sup>

The Reagan administration reaffirmed its support for the Jones Act in a letter from Admiral H. E. Shear, maritime administrator, to the president of the Society of Naval Architects and Marine Engineers.

“First and foremost, it has been, and continues to be, the fact that this Administration reaffirms the sanctity of the Jones Act. On May 20 and August 5, 1982, former Secretary of Transportation Drew Lewis announced the Administration’s position: ‘The administration reaffirms the sanctity of the Jones Act.’ The present Secretary of Transportation, Elizabeth Handford Dole, reemphasized this position at her confirmation hearing: ‘This Administration has no plans to revise the Jones Act and on the contrary recently reaffirmed the sanctity of the Jones Act.’ As recently as April 14 of this year, I noted before the Senate Merchant Marine Subcommittee, the Administration’s affirmation of the Jones Act, and in the same month, in remarks to the Society, I also noted the Administration’s firm support of the Jones Act.”<sup>294</sup>

More than a decade after President Reagan, a Republican, affirmed his support for the Jones Act, President Bill Clinton, a Democrat, gave his support. In 1997, President Clinton said the following:

“My administration also continues to support the Jones Act as essential to the maintenance of our nation’s commercial and defense maritime interests... Thanks to the Jones Act, the United States has a robust domestic shipping industry that directly supports 80,000 jobs and generates about 44,000 jobs in related industries. In addition to its economic contributions, the domestic shipping fleet supports our nation’s defense. Segments of this fleet—including tugs and barges serving the inland waterways and

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<sup>293</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 29

<sup>294</sup> Whitehurst, Clinton H., *American Domestic Shipping in American Ships: Jones Act Costs, Benefits, and Options*, pg. 29-30

the ships serving the Great Lakes ports-have also helped staff reserve ships during international emergencies.”<sup>295</sup>

During President Clinton’s administration the Maritime Security Act was passed.

With regard to this act, President Clinton expressed support for the national merchant marine when he said, “The American flag must always sail in the sea lanes of the world.”<sup>296</sup> Though the Maritime Security Act is not a cabotage law, it does provide subsidies to American ships. Thus, it is a form of governmental support.

Finally, the current President of the United States, George W. Bush, a Republican, voiced his support for the Jones Act during his campaign in 2000 in a position paper entitled “Maritime Transportation.” In the paper, President Bush stated the following:

“To compete in the global economy of the 21<sup>st</sup> century, Governor Bush believes the United States needs a maritime policy tailored to 21<sup>st</sup> century needs. Programs that have contributed to the growth of our domestic fleet, such as the Jones Act, and those that guarantee intermodal cargo lift and management services when needed in times of crisis or conflict, such as the Maritime Security Program, should be maintained. Additionally, Governor Bush will vigorously pursue negotiations aimed at ending international practices that disadvantage our industry.”<sup>297</sup>

Though to some this may seem to be merely political rhetoric, it does assert President Bush’s support for the Jones Act. (As an interesting side note, though it was not a campaign issue, while President Bush supports the Jones Act, his key opponent in the 2000 Republican primary, Senator John McCain does not.)

So it is clear that debate over the Jones Act spans the political spectrum. It is not a clearly partisan issue. Members of both major political parties have voiced support for

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<sup>295</sup> “Support for Jones Act and Merchant Marine Spans the Political Spectrum,” Lake Carriers’ Association website, Available: <http://www.lcaships.com/hpquotes.html>

<sup>296</sup> MARAD, Maritime Security Program Brochure

<sup>297</sup> “Bush Declares Support For Jones Act,” Maritime Cabotage Task Force website, Available: <http://www.mctf.com/bushjact.htm>

the Jones Act, as well as support for amending or repealing the Jones Act. As discussed earlier, there have been numerous attempts to amend the Jones Act in recent history, but none has been successful. Multiple lobbying groups have formed to defend their side of the issue. Right now, it seems that those who support the Jones Act have succeeded. With a majority of Congressmen voicing their support of the Jones Act, it would be difficult to pass any amending legislation. Yet, politics is a realm that is rarely constant. As time passes, new politicians with different views may take office. The political paradigm may shift and the Jones Act may someday be amended or repealed. For now, the Act appears as though it will remain in place.

## **Conclusions**

Protectionism has existed in America since colonial times. Following the American Revolution and the formation of the new government, one of the first legislations enacted by Congress was a protectionist law for the maritime industries. Though these laws were in part a reaction to the British navigation acts, they remained in place long after the repeal of the British acts.

The early American shipbuilding industry was extremely competitive. Skilled labor, cheap available timber, and a long coastline allowed the maritime industry to thrive in the young United States. Yet, as shipbuilding moved from wood to iron (and then to steel), the American maritime industry began to lose its competitive edge. Unable to compete with the British steel and shipbuilding industries, the United States found itself becoming a high cost producer of ships. During the 20<sup>th</sup> century, the only two periods of time when the United States possessed a dominant merchant marine were during and immediately following the two World Wars. During these time periods, the government undertook major building projects, producing very large quantities of ships.

In response to the first of these large builds, Congress passed the Merchant Marine Act of 1920 to dispense the fleet of ships to private investors. Included in the Merchant Marine Act of 1920 was Section 27 which reenacted the cabotage laws that had been temporarily suspended during the war. There was little debate over Section 27 at the time and, today, it has come to represent the core of our nation's maritime policy.

Cabotage restrictions impose a burden on the economy. The ITC has made multiple estimates of this burden, from a high of \$9.8 billion/year in 1991 to a low of

\$656 million in 2002. If the U.S.-build requirement were lifted, the ITC estimated the cost to the economy would be between \$138 million and \$380 million/year in 1999 and \$261 million in 2002. With the merchant marine and shipbuilding industry in decline it is important to ask if the Jones Act has met its objectives.

Many within the maritime industry have answered with a resounding “Yes.” They believe that the Jones Act secures a place for the maritime industry and guarantees the resources needed to provide and sustain a merchant fleet in time of war. They argue that if the protective restrictions were lifted, the entire U.S. maritime industry would falter and dissolve. Even Adam Smith points out that there may be instances when such restrictions are needed.

“There seem, however, to be two cases in which it will generally be advantageous to lay some burden upon foreign, for the encouragement of domestic industry.

“The first is, when some particular sort of industry is necessary for the defense of the country. The defense of Great Britain, for example, depends very much upon the number of its sailors and shipping. The act of navigation, therefore, very properly endeavors to give the sailors and shipping of Great Britain the monopoly of the trade of their own country, in some cases, by absolute prohibitions, and in others, by heavy burdens upon the shipping of foreign countries.”<sup>298</sup>

Adam Smith continues to offer some support for such regulations.

“The act of navigation is not favorable to foreign commerce, or to the growth of opulence which can arise from it... As defense, however, is of much more importance than opulence, the act of navigation is, perhaps, the wisest of all the commercial regulations of England.”<sup>299</sup>

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<sup>298</sup> Klausner, Joseph A., “Discussion-The Jones Act: Foreign-Built Vessels and the Domestic Shipping Industry,” SNAME Transactions, Vol. 91, 1983, pg. 189

<sup>299</sup> Klausner, Joseph A., pg. 189

However, Smith's argument for such regulation seems to assume that the restrictions should only be imposed when benefits are realized. If the regulations are merely supporting an ailing industry and the supposed benefits are not realized, then there should be no reason to maintain restrictive policies. With the shipbuilding and maritime industries in decline since the period following World War II, some change in maritime policy is warranted.

Many have proposed such changes, and in return have been met with hostility from those within industry. It is understandable that the U.S. maritime and shipbuilding industries oppose Jones Act reform. The Jones Act has been in place since 1920, with similar legislation existing since the nation's early history. These are the rules under which members of the industry have had to operate, and changing them would threaten the large investments they have made. It is understandable that they would want to protect their investments and jobs.

The national defense argument can swing both ways. Those who support the argument that the Jones Act provides for national defense believe that removing the act would completely cripple the shipbuilding industry, but the industry is in a desolate state and something needs to be done to revive it. On top of this, there are significant economic impacts due to the restrictions. The national defense objectives will be better served if the industry is strengthened. If the industry can be strengthened and money saved, then something should be done. The status quo is no longer sufficient.

The supporters of repeal seem to make more logical arguments. The evidence suggests that the greater good would be served with some change in the maritime policy. Those within the industry seem to be making more emotional pleas and appear to be a



little less rational due to the threat they perceive to their industry. Many of the politicians who support the act also seem to gloss over many of the issues and succumb to the lobbying of the industry special interests. It seems as though it is politically convenient to support the act because this creates the appearance that the politician is supporting national defense. The supporters for repeal, however, realize that with the industry in decline, and significant economic costs, that changes are needed.

Thus, the following changes to the Jones Act seem logical: 1) American vessels which are transferred to foreign ownership and then transferred back to American ownership should be permitted in the domestic trades. 2) Vessels constructed or repaired in foreign shipyards should be permitted in the oceangoing domestic trades. 3) In the spirit of the second proposed change, the ad valorem tax on American-flagged ships in the oceangoing trades repaired in foreign yards should be eliminated. 4) To guard against potential job losses, existing firms that come into direct competition with lower cost operators of foreign built ships could be given subsidies to allow parity in capital costs. This fourth change is not as important as the others, because the entrance of lower cost operators would merely replace the former operators with higher capital costs. However, if it is deemed necessary for the interest of fairness, these subsidies could be provided for the reasonable expected life of the higher capital cost ships.

The American flag, ownership, and operating requirements should be maintained. These three requirements fall in line with the national defense objectives of the Jones Act and would allow the government to maintain authority over the ships in case of a national emergency. Furthermore, by allowing foreign vessels constructed in foreign yards to

enter the domestic trades, operating costs may be lowered enough to encourage more vessels to enter the trades, thus increasing the national defense assets.

The inland and lakewise trades should remain as they are currently. The ITC studies suggest that these trades are sufficiently competitive. The majority of the maritime jobs also fall within these two categories, and thus the job loss seen by the industry would be drastically reduced.

The greatest portion of the economic costs associated with cabotage is a result of the build restriction. By removing this restriction, that large portion of the burden is lifted. The American shipyards that construct oceangoing vessels will suffer a little, but not much since most of their work derives from naval contracts which would undoubtedly stay within the United States. Also, the impact on American shipyards would be small since very few oceangoing vessels have been constructed in recent history and the outlook for future construction does not appear to be any better. There is also a remote possibility that the new competition for American shipyards may inspire innovation so that they may once again compete with foreign shipyards.

Cabotage has always been a part of the nation's maritime policy, but it is time for part of that policy to be amended. The Jones Act has failed in many of its objectives and it would be beneficial, both to the economy and the maritime industry, to pursue change.

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