STATEMENT

OF

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OF THE

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ON

GOVERNMENT POLICY AND THE DEFENSE
INDUSTRIAL BASE

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Mr. Chairman and Members of the Subcommittee:

My name is Ronald K. Kiss. I am the Acting Associate Administrator for Shipbuilding and Ship Operations of the Maritime Administration (MarAd), Department of Transportation. I am pleased to address this Subcommittee on behalf of Admiral Harold E. Shear, Maritime Administrator, with respect to the Maritime Administration's concern with the defense industrial base.

It is our understanding that the Subcommittee's primary interest in the maritime area concerns the used foreign sources for ship construction materials and components. Before addressing United States shipbuilding at that level of detail, I will give a brief overview of the maritime industry, especially the shipbuilding segment, and how the primary MarAd financial aid programs have operated in the past. These programs and policies are being carefully reviewed in the development of an overall maritime policy.

The Maritime Administrtion administers a number of programs to promote the American Merchant Marine, including shipping companies, shipbuilders, and ports.

Foremost among the statutes fundamental to our activities is the Merchant Marine Act of 1936, as amended. The declaration of policy of the Act states that:

> "It is necessary for the national defense and development of its foreign and domestic commerce that the United States shall have a merchant marine (a) sufficient to carry its domestic water-borne commerce and a substantial portion of the water-borne export and import foreign commerce of the United States and to provide shipping service essential for maintaining the flow of such domestic and foreign water-borne commerce at all times, (b) capable of serving as a naval and military auxiliary in time of war or national emergency, (c) owned and operated under the United States flag by citizens of the United States insofar as may be practicable, (d) composed of the best-equipped, safest, and most suitable types of vessels, constructed in the United States and manned with a trained and efficient citizen personnel, and (e) supplemented by efficient facilities for shipbuilding and ship repair."

Of primary importance to shipbuilding under this Act are the Construction-Differential Subsidy (CDS) program, the Federal Ship Financing Guarantee (Title XI) program, and the Capital Construction Fund (CCF) program. The CDS program provides for payment of construction subsidies directly to U.S. shipbuilders equal to the difference in price between constructing a vessel in a foreign shipyard versus having the same ship constructed in a U.S. shipyard, but not to exceed 50 percent of the cost of the vessel. The Title XI program provides long-term debt

financing guarantees at favorable credit rates for the construction or reconstruction of U.S.-flag vessels in U.S. shipyards. The CCF program provides for the deferment of Federal income taxes on funds set aside to construct vessels and certain related equipment in U.S. shipyards and factories.

The U.S. shipbuilding industry to which the above programs directly or indirectly provide benefits comprise about 180 shipyards of varying sizes. These shipyards are available for mobilization purposes in times of national emergency. Of special importance in planning for mobilization are the number of shipyards and building positions capable of constructing vessels of 475 feet in length and larger which can be used to carry supplies, ammunition, and petroleum products in the event of national emergency.

The shipyard capacity required for mobilization work, which include battle damage repair, normal repair, activation of reserve fleet vessels, and wartime construction is 83 building ways and 139 large drydocks, supported by a production work force of 136,000 employees. This capacity is represented by 54 shipyards amd ship repair facilities employing a total work force (production plus overhead) of about 210,000 employees. These 54 shipyards, which include the eight naval shipyards, are termed the "Shipyard Mobilization Base."

Within the "Shipyard Mobilization Base" are 26 commercial shipyards referred to as the "Active Shipbuilding Base." The "Active Shipbuilding Base" has been defined by MarAd as those major shipyards engaged in, or seeking contracts for, the construction of naval ships and/or major oceangoing or Great Lakes merchant ships. The 26 shipyards in the "Active Shipbuilding Base" now employ approximately 74,000 production workers. Seven of these 26 shipyards are currently benefitting directly from the construction-differential subsidy programs and in addition to these five, eight are benefitting from the Title XI program.

The foregoing data was largely derived from MarAd's annual survey of existing privately owned shipyards capable of merchant vessel construction. This survey, performed pursuant to Section 502(f) of the Merchant Marine Act of 1936 is intended to provide current data on the shipbuilding industry for purposes of national defense and national emergency planning.

The beneficiaries of our financial assistance programs also include a substantial number of smaller shipyards. For example, as of June 30, 1981, there are Title XI vessels on order or under construction in a total of 71 U.S. shipyards including the 15 shipyards in the "Active Shipbuilding Base" previously mentioned. These yards are located on all three coasts, the Great Lakes, and our inland waterways.

The U.S. shipbuilding industry is continuing to experience a generally declining orderbook and faces uncertain future prospects. Only four deep-draft merchant vessels were ordered during 1980. In the first 11 months of 1981, six merchant ships have been ordered. As of June 30, 1981, 41 deep-draft commercial vessels (the lowest number in 25 years) remained on the order-books, compared with 61 a year earlier. Twenty-nine of these 41 vessels are scheduled for delivery by the end of 1982.

There were two major bright spots for U.S. shipbuilders to help offset the decline in commercial vessel construction. As of mid-1981, a record number of 84 offshore drilling rigs were on order in 13 shipyards, and 101 Navy and Coast Guard vessels, 1,000 displacement tons or over, were under construction in 11 shipyards. Additionally, the market for offshore petroleum service vessels, inland barges, and towboats has been strong throughout

1981 and is expected to remain steady with the possibility of improvement in the coming years. Finally, repair of both commercial and naval vessels remains generally strong and indicates signs of increasing.

Considerable repair work is performed in the United States on foreign-flag ships. However, in contrast to most foreign flag vessels, which commonly have maintenance and repair services performed without penalty from their country of registry in the shipyards of other countries, the United States has maintained a 50 percent ad valorem tax on ship repairs to U.S. flag vessels accomplished abroad. This requirement is being reviewed as part of a study on the operating subsidy differential (ODS) program.

The Merchant Marine Act was amended as part of the Reconciliation Act to allow, in specified circumstances, the acquisition of foreign vessels by U.S. carriers receiving or applying for ODS. In particular the new Section 615 of the Act generally provides temporary authority through fiscal year 1983 to allow operating-differential subsidy to be paid to operators of foreign constructed, converted, or acquired U.S.-flag ships when CDS funds are unavailable. This permits ship construction in foreign yards, whereas previously, all ODS ships had to be U.S. built.

All other ship construction, including Navy shipbuilding, merchant ship construction for the U.S. domestic trade, shipyard heavy machinery fabrication, drill rigs, and ship repair activity remain unaffected by this legislation.

Other than the foregoing exception with respect to ODS, U.S. ship construction is a statutory precondition for receipt of governmental financial assistance through the CDS, ODS programs and a precondition as a matter of policy for the CCF, and Title XI programs. These programs set stringent limits on the use of foreign components. Furthermore, the Jones Act requires that ships used in the protected domestic trade be built in the U.S. Cargo preference requirements, as set forth in the Merchant Marine Act, require that eligibility for carrying government impelled P.L.-664 cargo be limited to ships built in the United States or to foreign built ships only after they have been registered under U.S.-flag for 3 years.

At this point I would like to shift the focus from the shipyards to the industrial supply base. Again let me emphasize that this is historically how the programs have operated, and that all these requirements are being reviewed in the maritime policy study. Although they are primarily directed at the shipbuilder and shipowner, MarAd programs, through their various restrictions on the use of foreign materials and components, also provide extensive protection to the shipbuilding industrial base. In addition, MarAd, in cooperation with the Department of Defense, participates in the Industrial Preparedness Planning (IPP) program which has the objective of ensuring that the national industrial base will be capable of producing adequate and timely deliveries of marine-related materials and equipment under mobilization conditions. Through this program we are alerted to decreases in the ability of the industrial base to meet anticipated logistics requirements.

In addition, we also participate in interagency groups such as the Department of Commerce's Industry Evaluation Board (IEB) that analyze industrial base issues, all with the objective of maintaining awareness of the capacity and capability of the supporting industrial base.

The administration of the "Buy American" requirements of the Merchant Marine Act also serves to alert MarAd to prospective problems in the supply industries. Section 505 of the Merchant Marine Act of 1936, as amended, states with respect to CDS grants:

> "In all such construction the shipbuilders, subcontractors, materialmen, or suppliers shall use, so far as practicable, only articles, materials, and supplies of the growth, production, or manufacture of the United States as defined in paragraph K of Section 401 of the Tariff Act of 1930; Provided, however, that with respect to other than major components of the hull, superstructure, and any material used in the construction thereof, (1) if the Secretary of Transportation determines that the requirements of this sentence will unreasonably delay completion of any vessel beyond its contract delivery date, and (2) if such determination includes or is accompanied by a concise explanation of the basis therefore, then the Secretary of Transportation may waive such requirements to the extent necessary to prevent such delay."

"Buy American," historically has been interpreted by MarAd to imply 100 percent American content for components. A component that has less than 100 percent American content has been considered to be of foreign manufacture.

Basically, there are only two situations where foreign procurement is permitted for CDS vessels. The first situation involves the "so far as practicable" language, under which a foreign source of supply is permitted when a component required for

normal ship outfitting is not available from a domestic source of manufacture. At the present time, only small foreign items such as manual typewriters, televisions, and binoculars have been consistently allowed in subsidized ship construction by the Maritime Administration. If the time came when foreign sources of supply were no longer available, it would be necessary to depend on the flexibility of the private-sector to respond to domestic needs.

The "so far as practicable" provision has also led to one special case in which partial foreign content has been permitted for CDS construction in a component. This special case is the slow speed main propulsion diesel. Prior to the rapid increase in bunker fuel prices in the early 1970's, main propulsion engines in large oceangoing vessels of the American merchant marine had traditionally been of the steam turbine type. Steam plant and turbine design and manufacture in the United States were at a very high level of technology development. Most of the other maritime nations of the world, however, were utilizing more fuel efficient slow speed diesel propulsion for which technology was rapidly improving as higher vessel powering requirements emerged.

In 1978 MarAd determined that the high cost of bunker fuel mandated an initiative to promote the development of a slow speed diesel manufacturing capability for vessel main propulsion in the Untied States. Development of such a domestic manufacturing capability could not realistically be accomplished without a transition period. New regulations were promulgated initially permitting some foreign content in slow speed main propulsion diesels for CDS vessels, provided that the engines are assembled in the United States and that the engine supplier submit to the Maritime Administration an acceptable manufacturing plan under which future engines for CDS vessels would ultimately be of 100 percent U.S. manufacture. We received and approved the manufacturing plans of three firms. Slow speed main propulsion diesels from one of these firms are currently being installed in three large CDS containerships under construction by Avondale Shipyards, Incorporated, for American President Lines Ltd.

The second situation for which foreign procurement may be permitted for CDS vessels involves avoidance of unreasonable delay in a vessel contract delivery date. "Buy American" waivers of this type, however, are so rare as to have no impact on this nation's industrial base.

The Maritime Administration's Title XI program does not statutorily require "Buy American" for shipbuilding materials and components as a precondition for receipt of Government financing guarantees. We have in the past as a matter of policy, however, extended in principle the precepts of the CDS "Buy American" requirements to Title XI vessel construction in that, unless we grant a waiver, the costs of any foreign materials and components are excluded from the actual cost of the vessel for which MarAd will provide a financing guarantee. This policy is also under review.

At the present time, the United States is not solely dependent on foreign sources for any essential component or production category. As noted previously, diesel engines with some foreign content have been used in U.S. constructed vessels. There is not at present a capability to forge large slow-speed diesel crankshafts in this country, although the necessary equipment is available. In an emergency, however, domestically produced steam turbines could be used in lieu of the slow speed diesels, as could medium speed diesel engines or gas turbines.

The Maritime Administration has assessed our shipbuilding industry's ability to respond to an accelerated construction program in the event of a national emergency. Our national war shipbuilding program plans provide for initial construction of product tankers and combination roll-on/roll-off container-breakbulk ships. Given the existence of plans and specifications for these ships, 3 to 7 months would be required to obtain materials and components to start fabrication of new merchant vessels. At present, the initial lead-time to delivery of new vessels in a protracted conflict is estimated at 18 to 24 months. If large-scale production continued, shorter lead-times could be achieved.

At the outset of a national emergency it is likely that the schedule controlling items would be propulsion machinery and heavy castings and forgings, regardless of what types of vessels were built. The nature of the shortfalls for propulsion machinery would depend on the type of machinery installed and on competing demands for Navy construction. Within the next few years slow speed diesel plants would be in short supply under current circumstances, as U.S. production capacity has not been fully developed. If steam turbine plants were used, turbines and reduction gears would be controlling in the early stages.

Mr. Chairman, this concludes my prepared testimony. I will be please to answer any questions that you or the Members of the Subcommittee may have.

Thank you.