Statement of
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Before the Senate Subcommittee on Merchant Marine
Commerce, Science and Transportation Committee
On S. 188, S. 206, S. 1616, and S. 1624
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Mr. Chairman and Members of the Subcommittee:

My name is Harold E. Shear, and I am the Maritime Administrator of the Department of Transportation. I am pleased to appear before the Subcommittee to present the views of the Administration with respect to S. 188, S. 206, S. 1616, and S. 1624, including the proposed amendment to S. 1624, sponsored by Chairman Stevens.

Before I get into the details of the Administration's position on these bills, I would like to make clear once again the President's commitment to the existing cargo preference laws. As you know, the two major policy announcements made by Secretary Lewis in May and August of 1982, which outlined the Administration's position on various aspects of maritime promotional policy, reaffirmed support for the cargo preference laws currently in effect. The Administration continues to strongly support these laws, and, where required, would support an appropriate clarification of existing law. However, as I indicated during hearings held before the House Subcommittee on Merchant Marine, we do not support either an expansion or a contraction of the scope of current law at this time, and for that reason the Administration opposes S. 188, S. 206, S. 1616, and S. 1624, including the proposed amendment I mentioned.

First I would like to discuss the basis for the Administration's opposition to S. 1624, the Merchant Marine Revitalization Act of 1983. This legislation would require that 5 percent of all U.S. bulk imports and exports be carried on U.S.-flag vessels in the calendar year following enactment, with the percentage increasing by 1 per centum per year until a level of 20 percent is reached. The proposed legislation would also require the Department of Transportation to establish and publish guideline rates for the carriage of bulk cargoes subject to the Act, and to establish an advisory committee to assist in finding ways to reduce U.S.-flag vessel operating and construction costs by at least 20 percent, which would be accounted for in computation of the guideline rates. Finally, unlike the proposed legislation currently before the other body, S. 1624 would make provision for a tax credit for shippers to offset a part of any freight rate differential resulting from the cargo reservation requirements of the bill, and permit the Secretary of Transportation to enter into an agreement with a shipyard under which the shipyard could deposit income generated under any shipbuilding or ship repair contract in a tax-deferred account to be used later for shipyard improvements.

The Administration supports the objectives of encouraging a newer, more efficient and less costly U.S.-flag fleet by lowering both shipbuilding and ship operating costs. One of the major concerns of this Administration has been the long-term decline of the American Maritime Industry. America needs a strong and viable merchant fleet, with modern cargo capabilities to enable it to compete on world markets. The pride this nation once had in its merchant fleet must be restored. A modern, revitalized American merchant fleet, manned by skilled and trained American seamen, is a goal which must be achieved.

However, we cannot support the approach taken by S. 1624, which employs the mechanism of cargo reservation, a measure which distorts the free market, to achieve those objectives. Our objections also reflect a number of other major concerns with the proposed legislation.

Cargo reservation would increase shipping costs of bulk imports and exports which would not be offset by the savings proposed by this bill. The annual cost of 20 percent cargo reservation for bulk cargoes has been estimated to be as much as $3 billion. This increase in shipping costs would increase the cost to the consumer and other users of bulk imports primarily petroleum, residual fuel oil, iron ore and bauxite; it would also increase the cost of U.S. bulk exports, such as coal and agricultural products, to the point that they could lose market opportunities.

A related concern is the severe adverse effect this legislation would have on U.S. agriculture. If historic rate differentials provide an accurate means of forecasting, the additional freight cost of S. 1624 on U.S. bulk agricultural exports could be as high as $1.9 billion. This would no doubt have a dampening effect on U.S. agricultural exports which are already decreasing. Further, since U.S. export and domestic prices for major bulk commodities are inextricably linked, the only way to maintain U.S. export volume would be for the price of bulk commodities to fall in the domestic market to compensate for higher freight costs from cargo preference. In addition, U.S. traders could become immobilized by the bill's procedures.

Further, the proposed legislation would place an additional administrative burden on the Government to monitor the program, set the guideline rates and administer the advisory committee on cost reduction. Such an expansion, requiring additional personnel and regulations, is clearly against the Administration's policy to simplify and minimize government interference in the market. The legislation would also be costly to employment in other sectors of the economy, and would restrict importation of maritime services with the attendant adverse impact on American jobs.

Finally, S. 1624 would have a negative effect on our foreign relations. Passage of the proposed bill would have adverse consequences for the Administration's commitment to liberalize trade in service industries, and to resist cargo allocation regimes in international liner shipping. This country has a commitment to, and a greater stake than any other country in, free trade. If this legislation were enacted, the U.S. would be viewed by its allies as endorsing a protectionist measure substantially at variance with this basic policy.

Experience has shown that an approach which relies on government intervention in the market does not serve the long-term interests of this country. It is imperative that we find ways to make the free market work for the benefit of this industry. Only in that way can we seek to secure the long-term viability for the U.S. merchant marine.

Over the past two years, the Administration has developed initiatives based on the premise that the forces of competition can be made to work for the benefit of the U.S. merchant marine. Our promotional bill takes this approach. We are also exploring ways to streamline and make more efficient the administration of our operating differential subsidy program. In addition, we are reviewing regulations which affect the maritime industry in order to lessen the regulatory impact on the industry by eliminating unnecessary and duplicative regulations. These and other measures will strengthen and revitalize the U.S.-flag fleet by making the industry more cost competitive and efficient.

As far as S. 1616 is concerned, let me go into more detail about the bill and the basis for the Administration position opposing the legislation. S. 1616 would repeal three cargo preference laws that apply to the ocean transportation of Government-impelled cargoes, and replace these laws with proposed legislation to be known as the "Government-Impelled Cargo Act of 1983."

The three cargo preference laws that would be repealed by the legislation are the Cargo Preference Act of 1904 (10 U.S.C. 2631), Public Resolution 17 (46 U.S.C. 1241-1), and the Cargo Preference Act of 1954 (46 U.S.C. 1241(b)), also known as Public Law 664.

As you know, the Cargo Preference Act of 1904 generally requires that military cargoes be shipped on vessels of the United States or belonging to the United States. The 1904 Act does not mandate the use of privately-owned, United States-flag commercial vessels. However, the Cargo Preference Act of 1954 requires that 50 percent of such military cargoes be shipped on privately-owned, United States-flag commercial vessels.

The second statute, Public Resolution 17, provides that it is the "sense of Congress" that in any loans made by a Government agency to foster the export of agricultural or other products, provision shall be made that such products shall be carried exclusively in vessels of the United States. Statutory waivers are granted when United States-flag vessels are not available. General waivers are granted to permit vessels of recipient nations to carry up to 50 percent of the ocean cargoes, provided that the United States-flag carriers do not experience discrimination in trade with the recipient nation. At the present time, about 75 percent of Public Resolution 17 cargoes are transported by United States-flag merchant vessels.

The third cargo preference law that would be repealed by the subject legislation is the Cargo Preference Act of 1954, which requires that at least 50 percent of Government-generated cargoes be shipped on privately-owned United States-flag commercial vessels to the extent such vessels are available at fair and reasonable rates. The Cargo Preference Act of 1954 is commonly referred to as Public Law 664.

Public Law 664 applies to all government agencies when shipping on ocean vessels "equipment, materials, or commodities" that have been procured by the United States for its own account, furnished by the United States for the account of a foreign nation, or for which the United States advances funds or credits or guarantees the convertibility of foreign currencies.

These cargo preference laws would be repealed and replaced by S. 1616, which would classify cargoes subject to the Act as waterborne cargo affecting the national security of the United States, and waterborne cargo not affecting the national security of the United States. Waterborne cargo not affecting the national security of the United States would be further classified in the bill as Government-impelled as the result of either direct Government involvement or indirect Government involvement.

Section 2 of the bill would require that 100 percent of all waterborne cargo affecting the national security of the United States be transported in United States-flag vessels. One of our concerns is that in most categories, this section represents an expansion of existing cargo preference requirements. For example, S. 1616 would require that all oil and other petroleum products procured for the Strategic Petroleum Reserve (SPR) be transported on U.S.-flag vessels, compared to the current requirement that 50 percent be transported in privately-owned U.S.-flag vessels. Such an expansion could increase the cost of transporting oil to the SPR and would impair the government's ability to purchase crude oil at advantageous prices on the spot market. Thus, while we believe that it is important to maintain the current 50 percent requirement for the significant contribution that it makes to the health of our merchant marine, we also believe that expansion of the requirement could well infringe on the flexibility needed by programs such as the Strategic Petroleum Reserve to fulfill effectively their statutory requirements.

Further, section 2 would mandate that 100 percent, rather than the current 50 percent, of all materials contracted for the National Defense stockpile be transported in U.S.-flag vessels. It would expand the current requirement that 100 percent of supplies bought for the Army, Navy, Air Force or Marine Corps be transported by U.S. ships, by adding the Coast Guard to the list of covered agencies and by expanding the scope of such cargoes from "supplies" to "equipment and supplies." Finally, it would add a whole new category to the 100 percent requirement described as "any other equipment, materials, or commodities, of any description, certified by the President as affecting the national security of the United States." The Administration cannot support any of these expansions.

Sections 3 and 4 of S. 1616 deal with waterborne cargoes not affecting the national security of the United States and require that not less than 50 percent of the gross tonnage of these Government-impelled cargoes be transported in United States-flag vessels. Such cargoes are classified in the bill as being Government-impelled as the result of direct or indirect Government involvement.

In the case of direct Government involvement resulting in the ocean transportation of non-national security cargoes, section 3 of S. 1616 provides that at least 50 percent of the gross tonnage of these cargoes be transported in U.S.-flag vessels and the requirement applies when:

a. The United States procures, contracts for, or otherwise obtains the cargo for its own account;

b. The United States furnishes the cargo to or for the account of any foreign nation free of any charge for the cargo; or

c. The United States sells the cargo to or for the account of any foreign nation at a price that is less than the cost to the United States of procuring, handling, and storing the cargo.

Public Law 664 currently provides that the 50 percent cargo preference requirement will apply "Whenever the United States shall procure, contract for or otherwise obtain for its own account, or shall furnish to or for the account of any foreign nation without provision for reimbursement, any equipment, materials, or commodities, within or without the United States . . . ."

In the case of indirect Government involvement resulting in the ocean transportation of non-national security cargoes, section 4 of S. 1616 provides that all waterborne cargo shipped to or from the United States shall be transported in U.S.-flag vessels whenever the United States provides to any entity, foreign or domestic, any form of grant, loan, credit, advance of funds, cash transfer, or guaranty, and such financial assistance is used to pay (a) at least 50 percent of the cost of procuring, contracting for, or otherwise obtaining the cargo, or (b) any of the freight charges for the cargo. In addition, section 4 of the bill provides that "Any grant, loan, credit, advance of funds, cash transfer, or guarantee provided in accordance with this section shall be conditioned on the responsible agency obtaining agreement by the recipient entity to comply with the requirements of this Act."

In this regard, Public Law 664 currently requires that the 50 percent cargo preference requirement shall apply "Whenever the United States . . . shall advance funds or credits or guarantee the convertibility of foreign currencies in connection with the furnishing of such equipment, materials, or commodities."

The Administration opposes sections 3 and 4 of the bill because it would substantially change the scope of existing cargo preference requirements. While the method of calculating the

50 percent limit in subparagraph (a)(1) is far from clear, it appears that these sections could expand the practical application of cargo preference requirements beyond their current application. As I just mentioned in connection with sections 1 and 2, the Administration does not support expansion of existing cargo preference laws.

Although section 4 of the bill provides that all waterborne cargo not affecting the national security of the United States shall be transported in U.S.-flag vessels, in fact, all cargoes generated by the Export-Import Bank and the agreed 100 percent U.S.-flag shipping requirement on foreign military sales administered by the Defense Security Assistance Agency would not be shipped in U.S.-flag vessels. Of the Export-Import Bank generated cargo, it is estimated that in 1983 approximately $40 million of the projected $65 million entitlement would be lost under the bill. With respect to the foreign military sales program, a reduction to a 50 percent U.S.-flag shipping requirement would result in a loss of $21 million in ocean freight revenue based on a $42 million projection. Specifically, the provisions set forth in paragraphs (1) and (2) of section 4 would effectively eliminate cargo preference requirements for these programs, as well as for the cargo generated by direct credit programs. This is because in many programs the United States may pay less than 50 percent of the cost of cargoes purchased with Federal assistance, and Federal funds may or may not be used to pay the freight charges or other transportation costs associated with the cargoes.

Lastly, on section 4, I must note that although section 4(a) has included the terms "cash transfer", "grant" and "guarantee" within the purview of the bill, any benefit gained from their inclusion is quickly lost in section 4(a)(1) by the requirements that such financing be directly used to pay at least 50 percent of the cost of procuring, contracting for or otherwise obtaining <u>the cargo</u>. Since funds advanced by these programs are commingled with other funds of their recipients, tracking a procurement to such funds is nearly impossible under Public Law 664 and could only be made worse by legislating such a requirement. For example, the $50 million in ocean freight revenue we have achieved through a side agreement with Israel under its cash transfer program would be jeopardized since we could not track the funds under the program.

Mr. Chairman, after careful study, we have concluded that although the three existing cargo preference laws are not without problems, they are too important for our merchant marine to attempt a major restructuring that would alter their content.

As this Subcommittee is aware, reserved cargoes generated by our cargo preference laws play an important role with respect to the health and well-being of the U.S.-flag merchant marine.

For example, the Cargo Preference Act of 1904 generates vast amounts of cargoes that U.S.-flag operators vigorously compete for. In fiscal year 1981, the Department of Defense generated 7.3 million measurement tons of dry cargo and 12 million long tons of petroleum cargo. Of this amount, U.S.-flag merchant vessels transported 6.8 million measurement tons of dry cargo, and 8.2 million long tons of petroleum cargoes. We would expect 1983 to approximate, if not exceed, these figures.

At the present time, cargoes subject to Public Resolution 17 are primarily generated by the Export-Import Bank. In 1980, such transactions involved total freight revenue of $87 million, of which $65 million was paid to privately-owned U.S.-flag merchant vessels. It is our projection that total freight revenue in 1983 will be in excess of $85 million, with U.S.-flag vessels receiving at least $65 million in freight revenues.

Finally, in 1980, the cargo preference requirements of Public Law 664 generated 9.3 million metric tons of cargo, of which 3.3 million metric tons was transported in privately-owned, U.S.-flag merchant vessels. In 1983, we would expect U.S.-flag vessels to receive in excess of 12 million metric tons of the total 20 million metric tons that should be generated.

It is clear from these figures that reserved cargoes are an important source of revenue for U.S.-flag carriers. I also might note that the vigorous efforts of my agency to enforce our existing cargo preference laws would appear to be reflected in the above figures.

Mr. Chairman, the Administration continues to strongly support our existing cargo preference laws. We do not deem it prudent to amend these laws which are so important to the U.S. merchant marine. Therefore, we are opposed to S. 1616, the Government-Impelled Cargo Act of 1983.

The third bill before the Subcommittee this morning is S. 206. Under the terms of this bill, the Secretary of Transportation would have the sole responsibility for determining and designating those programs subject to the cargo preference requirements. Every department having responsibility for a program so designated would administer it under regulations issued by the Secretary, and the Secretary would review such administration. It is clear that S. 206 would alter the status quo, and as I have previously indicated, the Administration cannot support either an expansion or a contraction of the existing cargo reservation laws at this time.

Finally, Mr. Chairman, I would like to comment on S. 188, a bill that would amend Title IV of the Merchant Marine Act, 1936, by adding a new section that would generally require the U.S. Postal Service to use exclusively U.S.-flag vessels for the international sea transportation of the U.S. mail in those cases in which a carrier operating such vessels is engaged in the provision of regular transportation services to the destination specified by the Postal Service. The rate charged would be required to comply with the Shipping Act of 1916 and would not be less than the sum of the fully distributed costs for the carriage of the mail plus a fair and reasonable profit. Also, no invitation to bid for the carriage of mail would be permitted to state specific size of containers.

As this Subcommittee is aware, a general requirement that United States mail be transported on U.S.-flag vessels first appeared in section 24 of the Merchant Marine Act, 1920. This requirement was generally continued in the Merchant Marine Act of

1928, section 405(a) of the Merchant Marine Act of 1936, and the 1960 revision of Title 39, "The Postal Service". However when Title 39 was again revised in 1970, no comparable U.S.-flag requirement was enacted into law, and the legislative history would appear to be silent on this point.

At the present time, air carriers transport the predominate part of overseas shipments by the U.S. Postal Service. During the first three quarters of fiscal year 1983, U.S.-flag vessels carried only 38 percent of the total oceanborne mail volume from the United States. The remainder of such ocean mail was shipped on foreign-flag vessels.

Mr. Chairman, the Administration cannot support S. 188. The bill contains a number of deficiencies. For instance, the rate established for U.S. flag transportation is a floor, not a ceiling, namely fully distributed costs plus a fair and reasonable profit. This standard is in sharp contrast to the ceiling contained in the Cargo Preference Act of 1954 of "fair and reasonable rates." Operations under the bill would subject the Postal Service to potentially unlimited increased costs in contravention of its mandate to achieve self-sustaining financial responsibility.

Further, the bill does not recognize legitimate service requirements of the Postal Service. These include sailing schedules and flexibility for container sizes. In some instances the U.S. carrier sailing schedules for foreign destinations are inadequate. Also some foreign postal administrations can handle containers only of certain specified sizes. S. 188, if enacted into law, would seriously undermine the Postal Service's ability to provide prompt and economic services for international surface mail. In addition, the bill expands the current cargo preference laws and, as mentioned above, the Administration does not support either an expansion or a contraction of these laws at this time.

The Administration appreciates the effort by this bill to further the development and maintenance of an adequate and well balanced American merchant marine. It is noted that without the bill U.S.-flag carriers in fiscal year 1983 will earn in excess of $4 million in revenue from carriage of Postal Service directed mail overseas of a total of about $11 million. Be assured that I will exert every effort to ensure that U.S.-flag carriers are afforded even-handed treatment in the ocean transportation of the U.S. mail.

Mr. Chairman, that concludes my prepared statement, and I will be pleased to answer any questions that you or the Members of the Subcommittee may have. Thank you.