Section 2

Status and Issues in Cargo Policy

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OVERVIEW

Both national and international approaches to cargo policies have recently undergone changes.[2] These changes stem both from industry developments and from events in the public policy arena. For example:

- The UNCTAD Liner Code has been in effect for over a year, and experience with it is growing.
- Both U.S. and foreign liner companies have begun some round-the-world shipping services; intermodal services are also growing.
- Serious overcapacity persists world-wide, especially in bulk shipping, forcing some companies out of business and others to seek government protection.
- Discussions are proceeding between the United States and its developed country trading partners regarding effects of the UNCTAD Liner Code and the refusal of the United States to participate. Agreements to help assure U.S. carriers competitive access to cargoes are under development, especially for cross-trades.[3]
- Initiatives to extend U.S. cargo preference to commercial cargoes continue to meet strong opposition. Such changes are unlikely in the near term.
- There have been attempts to repeal certain existing preference programs. Record U.S. trade deficits provide a strong argument for those who favor maintaining the lowest possible transport cost for U.S. exports.
- Bilateral cargo-sharing initiatives from some trading partners have met substantial U.S. opposition and few have advanced beyond the discussion stage. In some other trades, discussions of bilateral provisions and agreements took place in 1983 and 1984. Existing South American/U. S. bilateral agreements, for example, are undergoing re-evaluation.
- The Shipping Act of 1984 (Public Law 98-237) is considered to have some effect on cargo policies because of a provision that allows U.S. action against foreign operators whose country unfairly restricts cargo access by U.S. carriers.
- UNCTAD is proceeding, slowly, toward an evaluation of perceived problems with the "open registry" system.4 Some LDCs are expected to continue pressure for the phase-out of open registry, It is not clear whether the U.S. Government has developed an adequate strategy to responds

The volume of world seaborne trade increased in 1984 for the first time since 1979 (see fig. 2), with containerized general cargo accounting for most of the increase during 1983-84. Some continued expansion in world trade appears likely in the near term, most likely in certain selected dry bulk commodities and in the container trades (fig. 3). For most U.S. carriers, the container trade is the most significant,

While this trade in general cargo is expanding, the major liner companies are both shifting and expanding services. New, larger ships are begin-

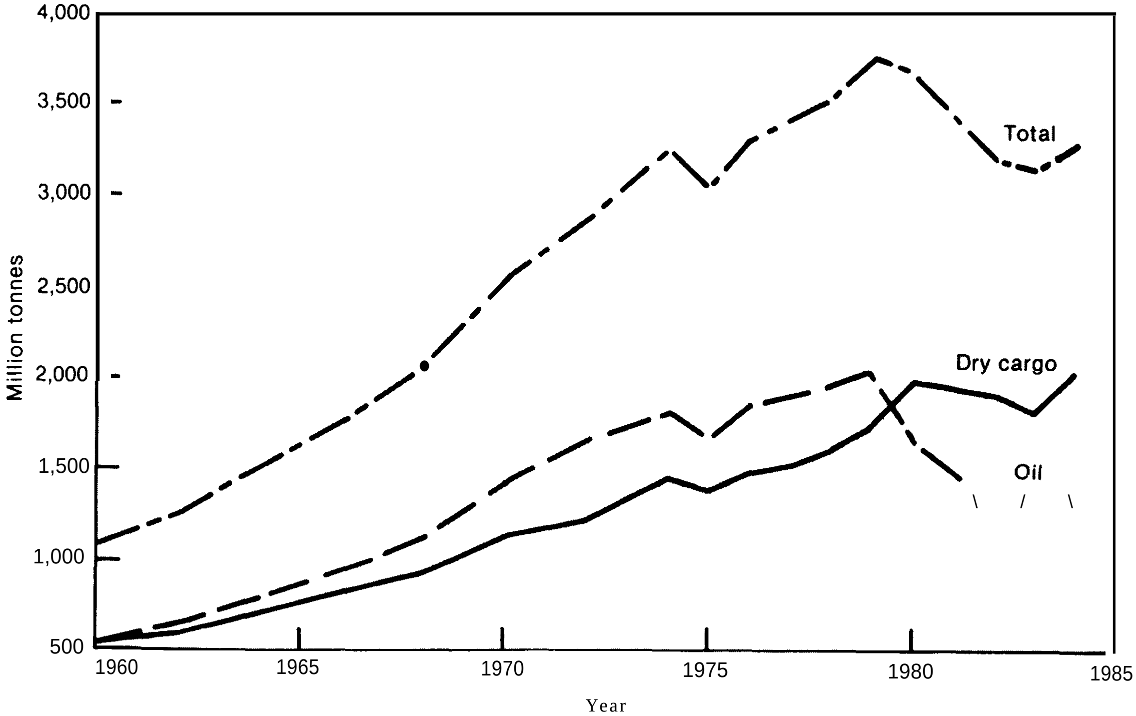
[2]The historical basis for unilateral, bilateral, and multilateral structures affecting cargo allocation are described in the 1983 OTA assessment This supplement provides an update of the key cargo policy topics of current interest.

[3]A "cross-trade" is defined as trade between two nations where the ocean carrier is a ship operator from a third nation.

[4]Open registry sometimes called 'flags of convenience' refers to the practice of registering ships in a country (I. Iberia and Panama are prime examples), while corporate owners reside in one of the major industrialized countries. The United States is the largest owner of open registry fleets.

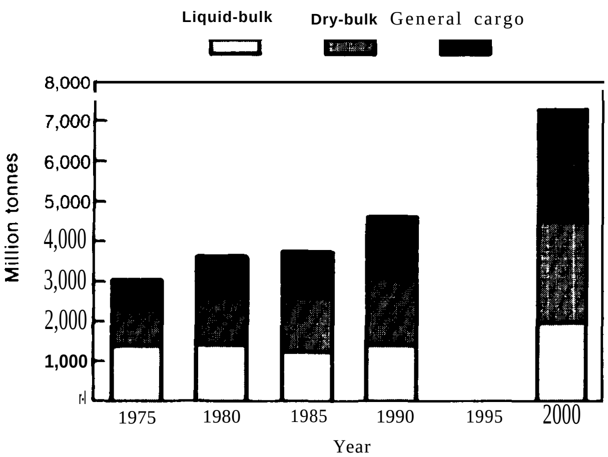
[5]Some industry participants at the OTA workshop disagreed saying that the Administration has consistently opposed this UNCTAD initiative. The State Department also disagrees, claiming that the United States intends to continue to work with developed countries in an effort to insure that any agreement reached would provide rights to owners to register vessels in the countries of their choice (Sam Keller, Office of Maritime and Land Transport, U S Department of State: personal communication, May 21, 1985) Beyond these claims, however, OTA has not been" able to obtain any documentation of an overall strategy or specific guidelines for the UNCTAD negotiations. If it exists, such documentation may be classified and thus not available for use in public policy debate

Figure 2.—World Seaborne Trade, 1960-84



SOURCE OECD & Fearnleys, 1984

Figure 3.—Projected World Seaborne Trade, 1975-2000



SOURCE Wharton Econometric Forecasting Associates.

ning "round-the-world" services calling at only major hub ports, and the same firms are offering more comprehensive intermodal rates and services. Some industry spokesmen have observed that increased rationalization in both large- and small-volume trades is forcing changes in the economics of liner shipping. Some industry analysts believe that "fewer, larger, more efficient enterprises will compete for market shares in future years. "[6]

The OTA cargo policy workshop, together with an analysis of the key questions raised by the workshop and other sources, has identified four issues that appear to be important not only to the health and vitality of the U.S. shipping industry, but also to other vital national interests involved in world trade and U.S. participation in that trade. These issues, discussed in the following sections, are:

- U.S. cargo preference;
- multilateral cargo sharing;
- bilateral cargo sharing; and
- defense needs that affect cargo policy.

[6] Peter Finnerty in *World Ports*, February 1985.

U.S. CARGO PREFERENCE

Current Authority

Cargo preference laws in the United States have not changed since OTA's *Assessment of Maritime Trade and Technology* was published in 1983. In essence, current law requires U.S.-flag preference on Government cargoes. This ranges from 50 percent of Government-impelled civilian cargoes to 100 percent for military cargoes. The current Administration has opposed any extension of cargo preference to commercial cargoes.

Three major cargo preference statutes are presently in effect. The Military Transport Act of 1904 (33 Stat. 518) mandates that 100 percent of Department of Defense cargoes must be transported on U.S.-flag vessels. The Cargo Preference Act of 1954 (Public Law 83-664) calls for 50 percent of U.S. Government-impelled cargoes (including military) to be carried on privately owned U.S.-flag ships. Public Resolution 73-17, passed in 1934, has evolved in practice to require that 100 percent of cargoes financed by loans made by the U.S. Government to encourage exports must be carried on U.S.-flag ships. Such cargoes are largely financed by Export-Import Bank loans. However, up to 50 percent of these shipments can be carried on the vessels of the borrower's choice if a waiver is granted by the U.S. Maritime Administration (MarAd), upon a finding of non-discrimination to U.S.-flag shipping.

Federal agencies have also made cargo preference a topic of interagency debate: those representing shippers take one side, and those representing operators take the other. During the OTA workshop, however, Federal agency representatives stated that the current Administration favors neither an expansion nor a reduction in existing cargo-preference laws. Most of these officials appeared to agree that present laws are reasonable, but that any proposals to extend preference to commercial cargoes would be strongly opposed.

Impacts of Liner Cargo Preference

Existing cargo-preference laws are important to U.S. liner operators. For the liner industry, such cargoes account for only 4 to 8 percent of total carriage, but these are frequently the "base cargoes" that make operations on some trade routes commercially feasible.

Proponents argue that the added cost of U.S. cargo preference for liner cargoes is usually small, because rates are set by industry conferences and vary little from carrier to carrier. The added cost may be higher in some instances, but such differentials tend to be minor in the aggregate, since preference shipments represent less than 10 percent of total U.S. liner cargoes. Other industry observers, however, claim that if a large portion of cargo in any trade were merely allocated to a conference by law, with no other competitive or regulatory controls, then prices could in fact rise unreasonably.

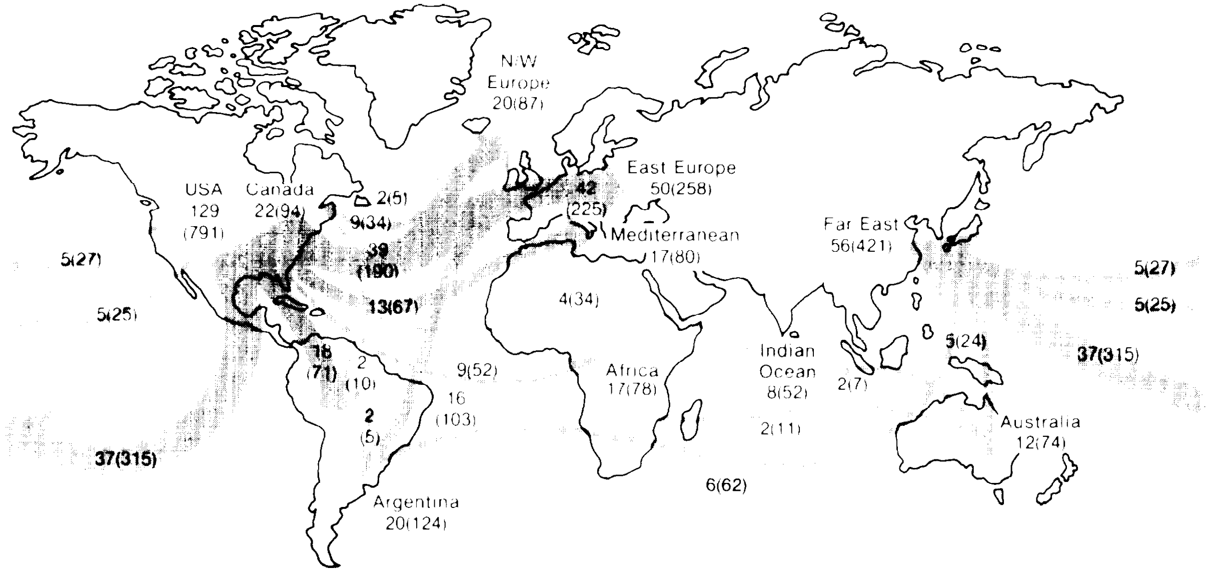
However, liner carriers do differ from each other in terms of the other forms of Government support they receive. One workshop participant suggested evaluating whether the Government should take into account the operating subsidies paid to carriers when evaluating their bids for preference cargoes, in order to compare the total cost to the Government. This is done for bulk shipments already and has been recommended by the Administration for liner shipments. The Department of Transportation has sent to the House and Senate a proposal for legislation to accomplish this by increasing insurance fees and/or reducing subsidy payments to operators carrying subsidized cargoes.

Impacts of Bulk Cargo Preference

For the few U.S.-flag bulk carriers, preference cargoes are sometimes the *only* cargo carried (see fig. 4). For bulk preference cargoes, rates are negotiated between shipper and carrier. However, the rates must be reviewed by the responsible agency, such as the Department of Agriculture (USDA). The agency will approve rates only up to the "fair and reasonable guideline" ceiling calculated by MarAd.

Spokesmen for bulk shippers at the OTA workshop opposed cargo preference and spoke emphatically in opposition to any expansion of preference

Figure 4.—World Grain Shipments, 1983



NOTE Main Inter-area movements in million metric tonnes (billion ton-miles in brackets) Only main routes are shown Area figures and totals including smaller routes are not shown separately Total trade 199 million tonnes (1,135 billion ton.miles)

SOURCE" Fearnleys

laws. They presented statistics on the increased costs that would result for agricultural exports under commercial cargo preference, indicating that if a 20-percent preference had existed in 1982, agricultural export costs would have risen substantially. If U.S. goods are to be competitive and U.S. farmers to make a profit, they claim transportation must be at the lowest possible cost. In shippers' eyes, the current U.S. trade deficit makes it even more imperative that U.S. exporters not be burdened further with higher transportation costs.

The preponderance of bulk preference cargoes are shipments of agricultural commodities under Public Law 83-480, which established major U.S. agricultural commodity aid programs. These requirements received significant attention during the OTA workshop discussions. Under the Cargo Preference Act of 1954 (Public Law 83-664), U.S. food assistance to less developed countries (LDCs) is subject to a 50-percent U.S. carrier reservation. USDA, which manages the preference requirements for these Public Law 83-480 Title I (concessionary sales) shipments, cited a transportation differential cost of $120 million paid for U.S.-flag carriage of food assistance cargoes in 1982. MarAd pointed out that the cost differential had declined to $65 million in 1983 and $76 million in 1984. Comparable detailed statistics are not available for the Title II (gifts of food) shipments, whose preference requirements are monitored by the Agency for International Development (AID). However, a GAO study estimated that U.S.-flag liner carriage under the Public Law 480 Title II program could have cost $0.73/ton more than foreign-flag carriage in 1980. At only $600,000 for 1980, the Title II cost differential was small compared with Title 1.[7]

At present the U.S.-flag bulk fleet has operating costs that average two to three times those of certain foreign competitors. These cost differentials are very significant to shippers, and U.S. bulk

[7]U. S. General Accounting Office, *Economic Effects of Cargo-Preference* Laws, GAO/OCE-84-3 (Washington, DC,: GAO, Jan. 31, 1984).

carriers are utterly dependent on preference shipments for their survival. Panelists also pointed out that the U.S. bulk fleet is modernizing significantly, which could lower future costs. A MarAd study of Public Law 83-480 shipments to Egypt showed that in 1981, 61 percent of Public Law 83-480 shipments were on bulk carriers over 22 years old, while in 1984, 63 percent of shipments were carried on vessels 5 years old or under.[8] This may lead to greater efficiency and reduced differentials in the future, because the new vessels are more automated and use less fuel; but it does not imply that the U.S.-flag bulk fleet is nearing profitability. A severe depression exists worldwide in bulk shipping, and foreign competitors are offering very low rates.

Government participants at the OTA workshop disagreed on the actual burden imposed by preference requirements. It is clear, however, that there are problems with the bookkeeping, both in the timeliness of information collection and, in some instances, of records being kept at all. Further study on the costs and benefits of cargo preference might be useful.

Implementation

Liner industry spokesmen at the OTA workshop alleged that the "50-percent requirement" is not being met in a single U.S. preference program. While they are not pressing for expansion of cargo-preference laws, liner operators are extremely concerned that current laws are not being enforced and that U.S. carriers are not getting the share of cargoes they are due. Participants suggested that part of the problem is that MarAd does not receive information on cargo carriage until well after the movement; it is difficult to enforce compliance after the fact.

Concern was greatest with respect to agricultural cargoes, and operators claimed that when new programs are started they are usually designed to avoid preference requirements. In addition, a number of DOD programs are not covered. Recently promulgated Federal acquisition regulations call for 50-percent preference. For these programs, liner operators note that the 1904 Act requires that 100 percent of DOD cargoes are to be carried by U.S.-flag ships. Some ExIm Bank programs, like the short- and medium-term guarantee programs, do not have U.S.-flag requirements. Finally, conversion of AID's commodity-export program to a cash-transfer program effectively diminished U.S.-flag participation. Industry representatives made a strong plea for enforcement of existing laws and suggested that it would be very helpful for the President to make a clear statement in support of those laws to assure compliance by Federal agencies.

An example of the controversy over implementation of existing laws is the litigation resulting from USDA's failure to apply cargo-preference requirements to the "Blended Credit "[9] export promotion program (Transportation *Institute v. Dole and USDA).* A recent U.S. District Court decision found that USDA and the Department of Transportation had violated the law by not requiring the use of U.S.-flag ships for this program. The Administration has appealed the decision, but it has also suspended the Blended Credit Program and announced plans for a new export promotion program that will not be subject to cargo preference. Legislation has also been introduced in both the House and the Senate that would exempt some or all agricultural commodities from cargo-preference rules.

OTA reviewed some of the claims of noncompliance in cargo-preference programs during 1984. The most recent data available measuring compliance are for calendar year 1982, as reported by MarAd in their Fiscal Year 1983 Annual Report .[10] That year's data show fairly good compliance, with some instances of U.S.-flag carriage well above the 50-percent requirement. Carriers represented at the OTA workshop, however, claimed that in 1983 and 1984 many programs did *not* comply with these preference quotas. Data for these years have not yet been reported by MarAd.

[8] Lewis Paine, U.S. Maritime Administration, presentation to OTA workshop Panel on Current Policy Initiatives.

[9] This program offers a "blend" or combination of two types of credit to a nation purchasing U, S agricultural exports – one type being direct interest-free loans from the Commodity Credit Corporation and the other being commercial loan guarantees

[10] MarAd is responsible for monitoring the ~dr~(~-preference programs of other agencies, such as DOD, USDA, and AID, and for reporting their findings to Congress

The question of compliance or noncompliance has been the subject of an exchange of letters between MarAd and the other agencies, especially AID and USDA. Many of these letters concern interpretations of how to collect and use cargo-preference data and the circumstances that may or may not be covered by cargo preference. For example, MarAd has exchanged several letters with USDA's Foreign Agricultural Service (FAS) on the subject of whether or not FAS complied with the Public Law 83-480 Title 1/111 program in 1983.[11] MarAd claimed that the cargo statistics showed only 48.2 percent of the program's total cargo was actually shipped by U.S.-flag carriers. FAS claimed that they approved 50.1 percent of the total tonnage for U.S.-flag shipment but cannot control precise loading dates at the end of each year; thus, actuals may be above or below their "approved" number.

Such a debate over 1983 statistics may serve to clarify the nature of the problems and the complexity of the rules, but it shows little promise of resolving the basic issue of cargo-preference compliance, Since a major Federal responsibility is resolving conflicts in the public interest, it would be useful for the agencies to jointly formulate compliance guidelines, methods of reporting data, and practical methods of allocating cargo before shipment. Since an Interagency Shipping Policy Group already exists, Congress could require it to bring the agencies together on this subject and prepare the cargo-preference guidelines and procedures.

[11] Under this program, food is sold to foreign governments on lenient financing terms.

Discussion

U.S. cargo-preference programs appear to be flawed compromises, in which no one is fully satisfied. On the one hand, many U.S. ship operators and builders view cargo preference as a necessity, both for countering similar practices in other countries and for maintaining an industry vital to national defense. Operators stress not only the need for cargo preference policies, but also the need for implementation. Many operators who participate in existing cargo-preference programs claim that current laws are not properly enforced and that cargoes are not always reserved for U.S. operators as required. In addition, those who favor Federal promotion of maritime industries maintain that expanding cargo preference is an equitable method of indirect subsidy that is urgently needed to replace the direct construction subsidies of the past.

On the other hand, some Government shippers as well as many commercial shippers view cargo-preference laws as an unjustified cost burden. Such policies increase program funding needs, especially for agricultural support programs; or they reduce the funding available for what are perceived to be other, more important uses; or they make U.S. shippers noncompetitive in the world market. Shippers—especially those of agricultural products—have been strident in their opposition to cargo preference, claiming that existing laws have hurt the U.S. export position and that any expansion would cause further damage.

MULTILATERAL CARGO SHARING

UNCTAD Liner Code

The UNCTAD Liner Code calls for sharing of liner conference cargoes[12] between the fleets of trading partners, with some portion reserved for third parties (cross-traders) if agreed to by the national-flag lines. The Code was developed by Third World nations in an effort to capture for their own carriers a larger percentage of their trade with the industrialized world. The United States strongly opposed the Code and refused to ratify it, but the Code went into force among its signatories in October 1983. While it is too soon to assess its long-term economic effects, no significant impacts are apparent yet.

[12] That is, those cargoes which are carried by the various companies who are members of a liner conference operating in that country.

A recent European analysis of the potential effects of the UNCTAD Liner Code, based on known reservations (or exclusions) to the cargo-sharing principle (such as the European Economic Community's reservation and the policies of the Centrally Planned Economies), found that only about one-third of all trade will be regulated.[13] The study suggested that while the eventual consequences of the Code are still uncertain, it is likely to have only a small effect in practice.

Potential Bulk Code

Workshop participants discussed the possibility of an UNCTAD bulk code, generally concluding that it is unlikely to happen. Many LDCs are less interested in pushing for a bulk code than they were because they no longer perceive that it would be in their interests. Many of these nations simply do not have the wherewithal to build and operate commercial fleets. In addition, there is clear opposition on the part of most OECD countries. Bulk trade, unlike liner trade, does not follow established routes on a regular basis. Rather, bulk trade tends to be "round the world, " with contract carriage of a specific cargo from one place to another. This arrangement does not lend itself to some forms of cargo allocation.

Open Registry

Underdeveloped countries who espoused the Liner Code and proposed bulk code, now seek to phase out open registries as well. While no action has thus far been taken on a bulk code, conferences on open registry were held in 1983 and 1984.

At issue is an attempt to phase out "flags of convenience": every carrier would be required to have a "substantial relationship" with the country under whose flag its ships sail. Many LDCs believe that if Western lines now flying the flags of convenience registries, such as Panama and Liberia, were required to register elsewhere, these other LDCs would capture a substantial share of the new registrations and the resulting economic benefits. Another view expressed by LDCs on this subject is that if Western flag-of-convenience carriers are forced to register their ships under their own national flag and employ Western seamen, they would be unable to operate economically and thus would phase out of many trades, enabling LDCs to increase their share of the carriage.

Phase-out of open registries is opposed by the major shipping nations that make significant use of convenience flags. The "U.S. effective controlled" (USEC) fleet of U, S.-owned but foreign-registered vessels represents the single largest fleet of flags-of-convenience vessels in the world. Two UNCTAD meetings, one in July/August 1984 and another in February 1985, failed to reach any consensus on the open registry issue but produced a negotiating text which was considered at a July 1985 session. (As this background paper was going to press, reports from the open-registry talks in Geneva indicated that a compromise agreement may be reached.) The U.S. Administration believes it is unlikely that open registry will be banned any time soon.[14] However, efforts to do so will probably continue.

One workshop participant compared the U.S. approach to multilateral shipping agreements to the negotiating approach that the United States has taken in other areas of international marine affairs. The issue expressed was whether U.S. tactics in this area will be analogous to the on-again off-again U.S. approach to Law of the Sea, where the United States wound up out of sync with the rest of the world; or whether it will instead be analogous to the cooperative approach used for the 200-mile fishery zone, which resulted in a system that requires other nations that fish in the U.S. zone to adhere to U.S. conditions.[15]

Relations With Europe and Japan

Relations between the United States and its major trading partners—members of the European Economic Community and Japan—continue to be unsettled in the wake of their adoption of the UNCTAD Liner Code. The United States resisted the passage of the UNCTAD Liner Code and has

[13] T. Wergeland, "UNCTAD Liner Code, 40-40-20: Potential Redistributional Effects for Liner Vessels," *Lloyd's Shipping Economist*, February 1985, pp &Q.

[14] It should be noted that U.S. officials did not think that the now-ratified UNCTAD Liner Code had any chance of passage either.

[15] Transcript of OTA Workshop on 'Cargo Policy, p. 406.

Photo credit: Exxon

A typical ship in the "U.S. effective controlled" fleet. This Exxon tanker was built in Japan and is registered under the Liberian flag.

rejected its implementation in U.S. trades. European nations tend to favor the Code and either have already implemented it or are moving to do so, but they would exempt intra-OECD trade from its purview. Japan has stated that it will ratify the code with no reservations.

It appears that each side is suspicious of the other's dedication to free trade. In a March 1984 symposium of leading shipping officials, Europeans accused the United States of protectionism, citing in particular the Jones Act, Operational Differential Subsidy, and cargo preference. The U.S. Maritime Administrator, on the other hand, pledged that the United States would fight any efforts toward protectionism. He cited the UNCTAD Code as "the most pervasive protectionist initiative" and expressed fear that European signatories would try to exclude U.S. cross-traders. He also said that the United States opposes bilateralism" conceptually, but will protect U.S.-flag markets if necessary (see the section on "Bilateral Cargo Sharing" below).

Protectionism was also a major topic of government meetings between the United States and the Consultative Shipping Group (CSG) from Europe and Japan, held in September 1984 and January 1985. A major area of contention was the EEC/Japanese ratification of the Liner Code and their perception that the United States is moving, toward protectionism. The United States has steadily opposed the UNCTAD Liner Code, while at the same time discussing bilateral agreements with several LDCs in response to threats of unilateral cargo reservation. Both the United States

[16]Government-to-government agreements between two trading nations where cargo shares are allocated to the ships of those nations under some fixed ratio.

and the CSG, in short, perceive anticompetitive actions on the part of the other, while at the same time recognizing that coordination and cooperation are in the best interests of all parties.

The Europeans would like the United States to enter into a binding agreement under which each signatory would "resist protectionism ." The specifics of such an agreement are not clear, and at least some United States representatives see no benefit in yet another ambiguous statement on the subject. The January 1985 CSG meeting addressed the problem of assuring U.S. carriers access to cargoes in trades between the Third World and other industrialized countries. No agreement has been reached on this point, although U.S. Government participants reported a narrowing of U.S.-CSG differences. These discussions are currently under review by the Administration. U.S.-flag liner operators have urged the Administration to terminate current negotiations.

Cross-Trades

With increasing acceptance of the UNCTAD Liner Code by foreign governments, some observers are concerned that U.S. liner operators could be squeezed out of traditionally profitable cross-trades. Five U.S.-flag carriers (American President Lines, Delta, Lykes, Sea-Land, and U.S. Lines) carried nearly 3 million long tons[17] of cross-trade cargo in 1982, producing gross revenues of almost $300 million. Loss of such trade could have serious consequences for U.S. carriers.

Participants at the OTA workshop liner panel stressed that cross-trading by U.S. carriers also benefits U.S. shippers and U.S. commerce in general. Revenues from cross-trade cargoes contribute to the overall profitability of U.S. carriers, allowing them to remain competitive in the hotly contested U.S. trade routes. Opportunities for cross-trading will also be increasingly important as carriers develop and pursue round-the-world trade routes.

A study prepared by Manalytics, Inc., for the Maritime Administration concludes that the U.S. Government can effectively protect U.S. liners' interests because a far larger percentage of U.S. trade is carried by third-flag vessels than is carried by U.S. carriers in foreign-to-foreign trades .18 In 1982, for example, Northern European flag ships lifted 12.9 million long tons of cargo as cross-traders in U.S. liner trades, while U.S. cross-traders carried less than 0.6 million long tons in these nations' trades. Thus, the threat of withholding access to significant volumes of cargo in U.S. trades could provide leverage in negotiations over impediments to cargo access by U. S .-flag carriers in foreign-to-foreign cross-trades. The Manalytics study also noted that many of the countries whose carriers are major cross-traders in the U.S. trades generate relatively little trade of their own.

The study listed the following possible U.S. Government responses to artificial impediments raised to bar U.S.-flag carrier access to cross-trades:

- cancellation of cross-trade tariffs of foreign carriers;
- discriminatory reservation of cargo against foreign carriers;
- imposition of operating restrictions; and
- imposition of taxes or currency exchange controls.

Shipping Act of 1984

Section 13(b)(5) of the Shipping Act of 1984 (Public Law 98-237) specifically permits Government actions in response to foreign actions that are discriminatory to U.S.-flag carriers in foreign-to-foreign trades. OTA workshop participants discussed the potential use of this provision in the future. Agency representatives believed that the threat of sanctions, rather than actual imposition, would in most cases be sufficient to achieve U.S. objectives. No cases have yet been brought under section 13(b)(5).

Several workshop participants also stressed the role of the 1984 Shipping Act in enabling U.S. interests to gain market access in international liner trades. The Act allows conferences to establish intermodal rates, giving shippers the advantage

[17] A long ton equals 2,240 pounds.

[18] Manalytics, Inc., *U. S,-Flag Crosstrading*, prepared for the Office of Market Development, U.S. Maritime Administration, July 1984 (contract No. DTMA91-83-C-30045).

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of a through bill of lading. It also requires conferences to assure the right of independent action for any individual conference member, requiring a maximum of 10 days notice prior to such action. Shippers' associations are authorized, although antitrust exemption does not extend to them. The rate-approval process required by FMC is considerably accelerated and simplified.

The rights of all carriers in U.S. trades for protection against discrimination is provided. The Act retains section 19 of the Merchant Marine Act of 1920, under which the tariffs of any country's vessels may be suspended, effectively excluding them from U.S. trades. Provisions of the Controlled Carrier Act of 1978 are also retained in the new Act. Under this provision, action may be taken against controlled carriers of any flag that unfairly compete by offering less than compensatory rates. Finally, as noted above, section 13(b)(5) of the new Act gives FMC power to suspend the tariff of any carrier in U.S. trade if the country whose flag it flies, or the commercial practices of the carrier, unduly impairs the access of U.S. carriers as cross-traders in foreign-to-foreign trade. Several participants stressed the importance of this latter provision, which they viewed as vital in protecting U.S. carriers against certain cargo-sharing schemes in effect around the world.

Future Strategy

The Administration's strategy for future international cargo policy negotiations is to continue resisting all forms of cargo-sharing agreements, but if resistance fails, to negotiate bilateral agreements with competitive elements, It may be useful for congressional deliberation if the Administration were to develop an explicit statement of these strategies, which would include: responses to UNCTAD initiatives; positions relative to CSG discussions and agreements; and the intended use of U.S. provisions, such as those in the new Shipping Act, in response to cargo policies of other nations. Congress could call for such a strategy paper, possibly requesting that the Interagency Shipping Policy Group prepare it.

BILATERAL CARGO SHARING

Current Policy

The Administration's policy toward bilateral agreements was summarized in 1984 by the Deputy Secretary of Transportation, speaking before the Maritime Law Association in New York.

> Any bilateral arrangements we might ultimately reach would be designed to place minimum constraints on trade and preserve maximum marketplace competition. They could also include both free access without Governmentally imposed barriers for national-flag carriers and a significant role for cross-traders. Our objective is to limit the amount of trade that is arbitrarily or Governmentally reserved to the flag carriers, while preserving equal access to reserved cargo, Naturally, our resistance to bilateral pressure will be tempered by realism and the need to protect our carriers' interests as well as our broader shipping and general trading interests. "

Thus it appears that, at present, the United States will only reluctantly accept cargo-sharing agreements with market-economy nations. Few such agreements have been concluded over the years, and only two are currently in effect .20 During 1983 and 1984 one bilateral cargo-sharing agreement, involving the United States and Brazil, was renegotiated. Discussions of competitive access have been held with three other countries, including the possibility of bilateral agreements with more competitive provisions.

The negotiation of such "procompetitive" bilateral agreements that recognize the maritime-promotion objectives of U.S. trading partners is an option that the Administration may pursue, as a last resort, in cases where other nations insist on some form of cargo allocation as a condition of trade, Such bilateral agreements may be the only feasible compromise between free trade

19 James Burnley, U.S. Deputy Secretary of Transportation, address to the annual meeting of the Maritime Law Association, New York, May 4, 1984.

20 App. B contains descriptions of some specific bilateral agreements.

and protected trade objectives of various trading partners, especially for the present Administration, which has objected so strenuously to multilateral regimes such as the UNCTAD Liner Code.

Given that bilateral cargo-sharing agreements exist today with two U.S. trading partners, and may be introduced with others from time to time in the future, it is important to address future strategies for these agreements. Strategies are needed that will seek to satisfy the goals of efficiency and good service, as well as supporting each country's national interest. It may not be possible to balance all conflicting interests.

Cargo Sharing and Competition

A major issue raised during the OTA workshop was whether bilateral shipping agreements can be devised that will preserve elements of price and service competition. Historically, the United States has entered into such agreements only when another country has made it a condition for the carriage of its cargo. The agreements with Argentina and Brazil are examples of the U.S. response to those countries' cargo-allocation policies (see app. B). The Federal Maritime Commission (FMC) has been investigating the competitive environment in these trades since late 1984. The current U.S.-Brazil agreement is due to expire at the end of 1985, and the Administration will soon begin discussions with Brazilian authorities. Discussions with Argentine officials are likely to follow.

Most workshop participants agreed that restraint on competition is unhealthy. But they also agreed that restraints do exist in many countries, and that U.S. carriers and shippers must deal with them. A possible role for the U.S. Government, therefore, is to protect shippers and operators from unfair competitive practices on the part of foreign governments and carriers, In the liner trades, for example, where price and service are fixed by conference system, competition is still considered necessary. A conference must be sufficiently powerful to maintain stability, that is, but outside competition should also be strong enough to prevent the conference from earning monopoly profits, Conferences in U.S. trades are open to any carrier desiring to join; trade is open to nonconference carriers; and the right of independent action by conference members is fully protected.

A radically different system was hypothesized during the OTA workshop panel on alternative approaches, in which competition would be assured within a bilateral agreement. Bilateral treaties would be negotiated without allocation of fixed shares of cargo, but with third-flag carriers excluded. Every carrier would be independent; rates would not be fixed; and carriers of either trading nation could compete for as much of the cargo as they could capture. Such an arrangement might allow U, S, carriers to compete more effectively, or enhance overall efficiency for the trade routes in question, [21]

Government Participation

A major concern expressed by workshop participants was whether national governments were involved in both regulating and operating their international shipping industries. A number of industry participants believed that bilateral agreements maintained by commercial conferences would neither impede trade nor work counter to the interests of carriers and shippers. However, they raised several questions about government participation in the shipping industry, which is common in many other countries.

A recent analysis, prepared as part of FMC's investigation of the U.S.-Brazil and U. S.-Argentina trades, identifies some of the problems arising from bilateral agreements that involve substantial government involvement.[22] The staff paper concludes that these trades are protected by government-supported cartels; that a few liner operators carry nearly all of the cargo in these trades; and that these trades are marked by entry restrictions and little or no service and price competition. One of the key problems, according to the report, may be that the Brazilian and Argentine agreements themselves create an entry barrier and that, "by mandating conference and

[21] Leslie Kanuk, Baruch College, presentation to OTA Workshop Panel on Alternative Approaches to Cargo Policy.

[22] Statement of Austin L. Schmitt, Chief Economist, Federal Mari time Commission, "Section 19 Inquiry—U S, Argentina and U.S. Brazil Trades, " Docket #84-33, Washington, D. C., Dec. 31, 1984.

pool memberships, set the stage for the lack of service and price competition.”[23]

The question that remains to be answered is what the United States can effectively do to open these and other trades to greater competition. The U.S. State Department has indicated that in future bilateral negotiations the United States will resist agreements that require cargo sharing. Whether this will be possible in the increasingly protectionist international environment remains to be seen. Congress could also call for the development of an Administration policy strategy paper on bilateral, in a manner similar to requesting a strategy paper on multilateral (see above).

Trade Barriers

Shipper representatives at the OTA workshop expressed concern that all trade barriers—whether cargo preference, conference action, or bilateral or multilateral cargo reservation—are inefficient and uneconomic. They gave the example of a container shipped from the Midwest to Argentina or Brazil: via Europe, the cost is $3,400, while direct shipment costs $5,000. Shippers were optimistic that the Act addresses some of these problems and that the new Shipping Act will result in a better balance between carriers and shippers than existed under the 1916 Act. However, they remain concerned that conferences can still set rates, pool revenues, restrict sailings and volume capacity, and prevent competition.

“U.S. Maritime Commission, Docket #84-33, Section 19 Inquiry—U. S, Argentina and U.S. /Brazil Trades, Memorandum of Law, p. 10.

Shippers feel that the success or failure of the Act will ultimately depend on how carriers respond to its independent action provision. Competitive opportunities are available to both shippers and vessel owners, including the ability to provide intermodal services,[24] independent action,[25] and a prohibition against loyalty contracts,[26] except as allowed under antitrust law. Thus far, however, the impact of the Act has varied by trade area. In general, carriers in the OECD trades have been more aggressive in seizing new opportunities than have those in LDC trades. Independent action has become common in the Pacific trades, while carriers on the North Atlantic appear afraid of starting a new rate war.

Individual shippers have taken advantage of new provisions, such as service contracts, to a greater or lesser degree. Shippers’ associations are not yet common, and leaders in organizing them have yet to come forward. Many shippers fear antitrust problems and therefore have adopted a “wait and see” posture. However, the recently formed Shippers for Competitive Ocean Transport (SCOT) has provided a means of bringing shippers’ interests into focus and representing those interests in national and international negotiations. SCOT supports a competitive regime that will encourage good service, reasonable rates, and innovation.

[24] A contract for shipping services covering several modes of transportation (truck, rail, ship, etc.).

“The right of a carrier in a conference to offer independent service and rates.

[2]* Confidential loyalty agreements between shipper and carrier in exchange for favored rates,

DEFENSE NEEDS AND CARGO POLICY

A number of workshop participants expressed concern about the ability of the U.S. merchant fleet to support wartime needs, today and in the future. The rationale for most forms of Federal subsidy to the maritime industry, including cargo preference, is national security. The U.S. merchant fleet would be tasked in wartime with both direct military support and continued support of the civilian economy. DOD recently completed a study to determine wartime logistics needs and adequacy of the merchant marine to fulfill them .[27]

[27] The study is classified, but Deborah Christie’s presentation to the OTA Workshop Panel on Current Policy Initiatives contained the unclassified highlights.

The findings were that sufficient container capacity exists for carriage of containerized military cargoes. However, there is a significant shortfall of capacity—breakbulk[28] and Ro/Ro[29]—to carry large units of equipment (such as tanks). DOD has launched two initiatives to ameliorate this problem: 1) purchasing older breakbulk and Ro/Ro vessels on the open market and putting them in the National Defense Reserve Fleet (NDRF); and 2) purchasing the flat racks and sea sheds needed for converting containerships, which make up most of the U.S.-flag liner fleet, to carry large equipment such as tanks.

When the liner cargo panel was told that DOD is considering acquiring its own in-house fleet to provide sealift capability, participants questioned whether this would be cost effective compared to promoting the development of needed capacity in the private sector. A clear policy decision needs to be made as to whether it is desirable to have a largely nationalized fleet maintained at Government expense, or whether it would be more efficient to build and operate a commercial fleet with some Government support. DOD contends, however, that there are few ideas for stimulating private sector growth, and that DOD considered those that were around when launching its program:

> In fact, our program is cheaper than past policies (ODS, CDS, and cargo preference), which were not providing the needed capability, and we have yet to hear any suggestion that shows promise of stimulating significant growth in the flag fleet for equal cost.'[30]

[28] Ships that carry genera] cargo in a large variety of sizes.

[29] Ships that carry vehicles or trailers that are loaded and discharged by "rolling on and rolling of f."

[30] Letter from Deborah P. Christie, Division Director for Projection Forces and Analytical Support, Office of the Secretary, Apr. 30, 1985.

Photo credit U S *Maritime Administration*

National Defense Reserve Fleet at anchor.

National defense requirements were discussed in some detail during the bulk cargo panel, since product tankers[31] are valuable defense assets, The USEC fleet of U.S.-owned, foreign-flag ships contains sufficient large crude oil carriers to serve defense needs, in the panel's opinion. But some participants expressed concern about the number of usable tankers: most of the USEC tanker fleet is made up of large crude oil carriers, which may not be as useful militarily as smaller oil-product tankers, Because of consolidation in the world petroleum industry, furthermore, the tanker fleets of U.S. oil companies and of our NATO allies are declining in size and significance. A separate point raised by shipping interests was the cost of defense-related features of their fleet and whether these costs should be borne by U.S. taxpayers, rather than by a small number of shippers.

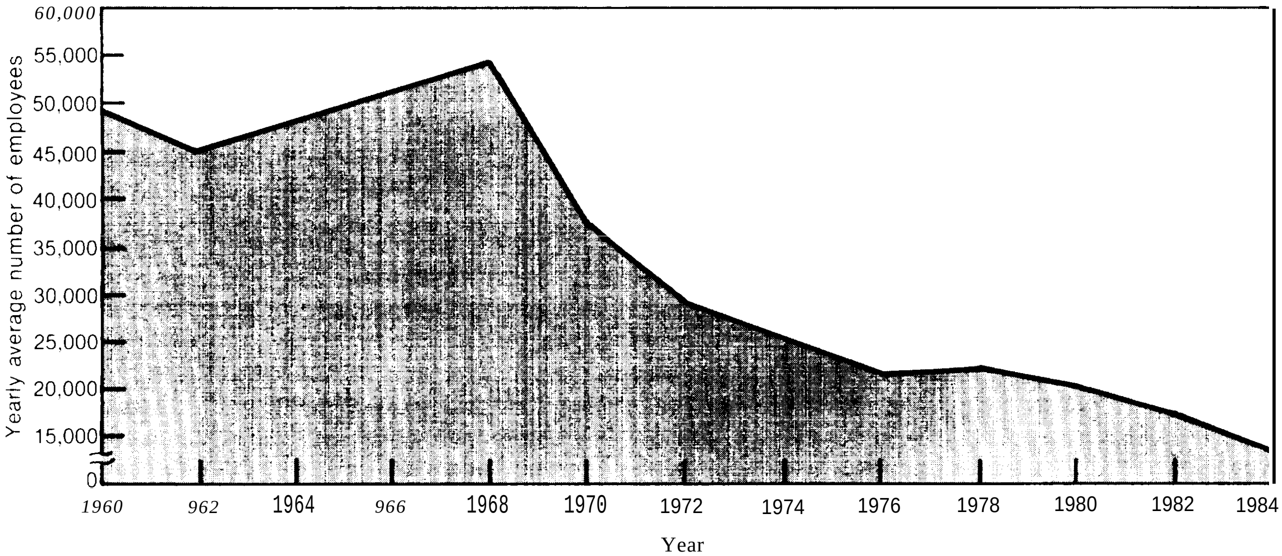
Another issue raised by workshop participants is the adequacy of the pool of merchant seamen to crew reserve fleet ships, should they be required. The recent decline in number of U.S. merchant seamen is expected to continue due to retirements and the declining crew requirements of modern vessels (see fig. 5). As a result, several participants questioned whether an adequate number of crew members could be found for military support operations in wartime.

I] Tankers that carry refined petroleum products, such as gasoline, diesel, fuel oil, etc.

Workshop participants agreed that these and other defense issues merit further study. Among the topics mentioned were a cost-benefit analysis of the merchant fleet as a defense support base, the cost of defense requirements to the merchant fleet, and the crewing issue. Congress may wish to call for more specific, in-depth analyses of these issues, possibly as part of the charter of the newly established Commission on Merchant Marine and Defense. Workshop participants suggested three specific areas in which additional analysis could improve future policies:

1. A cost comparison of alternative approaches to providing needed military sealift capability (for example, comparing the cost of having DOD buy or build the ships they need vs. the cost of encouraging the commercial operation of those ships through subsidy programs, including hidden costs, multiplier effects, etc.).
2. An analysis of actual costs of providing defense features in shipbuilding, and who ultimately pays for them. At present the commercial industry is thought to be funding certain features and practices that support national defense goals, but without direct DOD support.
3. An analysis of the relative military usefulness of the existing commercial fleet. DOD claims that it does not currently have access to the types of vessels needed for mobilization; others claim they do.

Figure 5.—Seafaring Employment— U.S.-Flag Oceangoing Commercial Ships



These data are for oceangoing commercial ships only which include the coastal (Jones Act) trade but not the inland waterways. The data show a steady decline since 1968 which stems from a number of factors including a decline in the active fleet, a switch to larger ships, a reduction in crew sizes and the general slump in world trade. In addition, these figures are for the privately-owned fleet only and do not include the 3,000 to 4,000 jobs currently in the government operated fleet (principally MSC).

SOURCE: MarAd data, 1985