
America's Welfare Queen Fleet

The Need for Maritime Policy Reform

Rob Quartel

When Saddam Hussein invaded Kuwait, the United States responded just days later with a military sealift, the success of which is unparalleled. In just 45 days the United States moved to Saudi Arabia the equivalent of a city the size of Alexandria, Virginia—lock, stock, and barrel. Hussein's threat was met by a vast armada of American commercial ships crewed by thousands of young, well-trained Americans, on the world's fastest, most modern ships. The American merchant marine threaded its way through the dangers of the naval mines laid off Saudi shores. The military was able to call on the services of this private fleet at only a moment's notice and paid no more than market rates. This success story was made possible by a far-sighted competitive merchant marine policy set in place years ago by the U.S. Congress. *And with the exception of the first two sentences, this scenario is a myth.* Only the S&L debacle represents a bigger government-industry-special interest scam than that which today passes for a national merchant marine policy.

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hundreds of thousands of tons of military goods to the vicinity of the war zone—Singapore, the United Arab Emirates, and Haifa. But many relied on foreign-flag feeders with their foreign crews to complete the runs to Saudi Arabia and thus exposed the bankruptcy of the man-American argument that underpins much of U.S. maritime policy. No Jones Act vessels participated at all, and the Jones Act, that most sacred of sacred cows, had to be partially suspended to ensure adequate fuel for the nation's defense. In short, the success of the military sealift—a brilliant feat of logistics—occurred despite (rather than because of) 75 years of government subsidies, protectionism, regulation, and entry and management controls promoted as necessary for maintaining this so-called “fourth arm” of the nation's defense.

The problems inherent in existing maritime policy are not limited to issues of utility in the recent war effort, however. The various regulatory policies and subsidies that have grown up over more than 200 years, often by historical accident, are simply counterproductive. Once the largest private commercial fleet in history, the U.S. merchant marine is now a shadow of its former self, dependent on federal welfare for its marginal survival.

Unrecognized by government policy, a fundamental change is taking place in the underlying economics of ocean shipping. It is not just, as many in the industry argue, that profit levels are excessively low and markets overtonnaged; the changes

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taking place are far more basic. Although carriers have spent considerable time, money, and management effort to differentiate their markets and services, ocean carriage itself has become an increasingly fungible product. Each day the line between high- and low-value ocean carriage services becomes less distinguishable in the principal U.S. trades and product markets. When that line finally disappears, several difficult questions will face both nations and corporations that now own and finance relatively high-cost ocean carriers: Why own ships? Why maintain a flag fleet? Why not simply purchase ocean space, as the intermodal shipper now hires services from the trucking, airline, and railroad industries?

Federal maritime policy is divided into two distinct yet intertwined parts. Promotional (read "protectionist") policies are managed by the Department of Transportation's Maritime Administration (MarAd), and regulatory policy is promulgated by the independent five-member Federal Maritime Commission (FMC).

This article examines the network of promotional and regulatory policies and suggests dramatic departures from the themes that have motivated more than two centuries of government intervention in the maritime industry. But to understand the need for change, it is important to appreciate the state of the industry today.

The American Merchant Fleet: Where We Are

The most effective measure of a policy's success can often be found in the numbers its supporters would hide. In the case of the American merchant marine, the decline of the U.S. flag fleet offers unmistakable and conclusive evidence of the extent of the policy failure.

At the end of World War II, America had the largest fleet in world history—more than 2,000 vessels. By 1970, however, there were only 893 U.S. flag ships, and by the end of the 1990, the fleet had declined to 371 active vessels. Fewer than 100 ships remain in the oceangoing fleet, and although some observers note that the tonnage of these vessels has remained constant since 1970, the market share of the U.S. merchant marine continues to drop. In 1970 U.S. flag vessels carried 24 percent of all goods arriving at or leaving U.S. shores. Today less than 4 percent of those goods are carried in U.S. flag ships.

The labor picture is equally grim. Between 1979 and 1989 average monthly maritime employment fell more than 30 percent. Seafaring jobs alone declined 80 percent, down from a high of 56,000

billets in 1950 to about 11,000 today—reflecting in part better technology, but more significantly the basic decline in the American fleet's economic viability. Although subsidized merchant marine academics continue to churn out graduates, few entry jobs exist in the oceangoing flag fleet. The average unlicensed sailor is now 50 years old, the average officer 44. Meanwhile, through the operating differential subsidy, American taxpayers subsidize some 2,200 seagoing slots to the tune of nearly \$120,000 per year *each*.

The Policies behind the Green Door

How did an industry supposedly so vital to our nation's trading success arrive at such a state? To a large extent, the U.S. flag fleet is a victim of attempts to save it. The ins and outs of maritime economics and regulation often appear complex and forbidding to the uninitiated, but its essentials—the programs that govern the maritime industry and its markets—can be summarized in seven programmatic themes repeated throughout all of the legal and regulatory elements.

- *Cabotage* policies are designed to protect domestic shipping from foreign competition. The Jones Act (the Merchant Marine Act of 1920) requires shipments between U.S. ports (Los Angeles and Honolulu, for example) to be carried on U.S.-owned, operated, built, and manned carriers. The United States, almost alone among the major trading nations of the world, applies cabotage protection

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not only to its sailors, but also to its shipbuilders. International U.S. flag ships also face restrictions regarding the required mix of American ownership, labor, and repair work.

- *Shipyards* policies protect domestic yards from foreign competition by proscribing the use of foreign-built or repaired vessels in domestic operation and

in certain U.S. flag international trade operations. Although direct construction differential subsidies (designed to offset higher U.S. costs) are no longer funded, U.S. shipyards continue to be subsidized through federal mortgage and tax set-aside programs as well as through direct barriers to entry to foreign competitors.

- Virtually blanket *antitrust* exemption for international ocean cartels or "conferences" is combined with federal (FMC) government enforcement of the resulting price-fixing agreements through mandatory tariff filing and antirebating policies—all falsely in the name of common carriage, price stability, and international practice and comity.

- *Direct government subsidies* are provided to certain U.S. flag carriers. The so-called operating differential subsidies of over \$200 million a year, paid to four U.S. firms operating American-built vessels, are considered necessary to offset the cost differentials created by flag restrictions on labor, ownership,

The programs that govern the maritime industry and its markets include protectionist cabotage and shipyard policies, virtually blanket antitrust immunity, direct and indirect government subsidies, and manpower and national defense requirements.

capital investment, and management. But the subsidy comes with a price—regulatory constraints regarding terms of trade, routes, and asset sales. The government also restricts competition among U.S. ships in domestic Jones Act markets and through access to price-subsidized government preference cargoes.

- *Indirect subsidies* include: U.S. flag cargo preferences for military, agricultural, and other U.S. government goods; entry barriers and utility rate regulation in protected Jones Act markets; and tax subsidies for funds set aside for ship construction.

- *Manpower* requirements include shipboard labor pool restrictions and rigid crewing requirements, both in numbers of billets and in types of positions (radio operators, for example, akin to coal tenders on railroads) and archaic labor-management restrictions in U.S. shipyards. The demands of an aging fleet, caused largely by build-U.S. restrictions, cause further labor inefficiencies.

- A *national defense* requirement overlays all the other programs and requirements. The law requires that the commercial fleet be in a position to be a useful auxiliary to military operations, whether military commanders want them or not.

U.S. maritime policy has been over 200 years in the making. The first legislation to protect U.S. shipping interests was passed in 1789 by the first Congress. A tariff placed on imported goods was reduced by 10 percent if the imports were carried on vessels built in the United States and wholly owned by Americans. Other policies and regulations have been added to the mix since 1789, but despite efforts to address problems through periodic adjustments to the subsidies and restrictions, the state of the maritime industry continues to deteriorate.

New Markets, New Players, and a New World Order

Conditions today are very different from those that existed when America's maritime laws were first written. In 1789 America was a developing country with a tiny fraction of the world's trade. Today the United States represents nearly 26 percent of world GNP, almost 12 percent of world exports. Nearly a trillion dollars (or approximately 95 percent) of U.S. foreign trade moves by ship. The world's economy simply cannot exist without either the products we sell or the markets we provide.

Dramatic changes in international markets also continue to alter the mix. The advent of European market integration, new political systems in Eastern Europe, new markets and aggressive new producers in the Pacific Rim, the potential for a new GATT and various free-trade agreements, and numerous other events—both noteworthy and minor—all contribute to major changes in the fundamental economics and consequent market relationships in the maritime sector. Innovation, entrepreneurship, and competition in transportation logistics only increase the uncertainty surrounding market outcomes. But maritime law and policy have been slow to recognize, let alone adapt to, these rapidly changing realities, including our evolving position in world markets.

The second fundamental economic change is in the character and structure of ocean carriage itself. The ocean shipping business no longer consists simply of ships on the ocean. Today's industry leaders provide intermodal docks that accommodate trucks and rail, as well as ships, door-to-door pick-up, packaging, and delivery, and electronic tracking, customs documentation, and billing.

Furthermore, the ocean leg, which accounts for 70 to 80 percent of the intermodal bill is itself an increasingly fungible market of ocean space and movements. Today the competitive advantage goes to modern foreign (frequently Asian) fleets manned by smaller, less highly paid crews, who ride on cheaper foreign-built, foreign-financed ships than their American counterparts. The competitive disadvantage of the high-cost American flag fleet leaves no future for an industry penalized by both flag and Jones Act restrictions. Policymakers cannot continue to treat the merchant marine as simply an ocean service. It is increasingly an international, intermodal service industry.

A New Maritime Paradigm

It is well past time for a fundamental rethinking of the maritime world order and what many suppose to be its universal laws. It is time for the development of what might be called a new maritime paradigm. Three points represent the essential pillars on which this new strategy must be built.

First, the new paradigm should represent a commitment to reforming *policy*, not just restructuring current *programs*. That requires both a commitment to dig down to the roots of the industry's productivity and competitiveness problems and the resolve to get from where we are today to where we want to be in clear, decisive steps.

Second, the new paradigm should encompass a broad policy outlook with a detached, analytical view of international shipping as a link in the trade network of an increasingly globalized economy. U.S. maritime policies should be based on more than emotion and the narrow parochial interests of dying labor unions, debilitated companies, and congressional PAC contributions. The needs of ocean transportation *users* (not just the needs of the carriers), real national security requirements (not empty rhetoric), and a realistic appraisal of the tough federal budget limits that will exist into the foreseeable future should drive decisionmaking.

Finally, the new paradigm will require a high degree of boldness and imagination. The greatest obstacle to maritime reform today is political timidity and lack of imagination and vision.

Although most observers within the industry and inside the government bureaucracies that promote and regulate U.S. shipping know that the current policy has failed, few seem able to visualize conditions under which the U.S. flag fleet could compete. In part, that stems from the inability to consider



"I MUST HAVE MISSED SOMETHING. WHEN DID WE BECOME PROFIT-MAKING?"

either rearranging or eliminating the self-inflicted penalties of current flag and Jones Act policies. But just five key policy changes would radically alter the state of this industry by allowing it to reorganize itself along more competitive lines and by freeing industry participants from both government largess and the associated government entanglement and interference.

First, we must sever the linkage among shipbuilding, commercial shipping, and military planning and develop independent strategies in a stand-

Changes in the world's economy, in international markets, and in the character and structure of ocean carriage require that policymakers treat the merchant marine as an international, intermodal service industry.

alone context for each. To the extent that each policy is independently successful, all will be served.

Second, we must eliminate the industrial welfare mindset by deliberately reducing and phasing out operating subsidies as well as the restrictions applying to labor, ownership, and assets of U.S. flag and Jones Act vessels. In addition, we need to carefully restructure and eliminate indirect subsidies, from tax deferrals to cargo preference.

Third, we should directly address military manpower and sealift requirements. To the extent the U.S. commercial fleet represents a real national

defense asset, budget decisions should be consolidated with all other defense-related maritime programs under Defense Department control.

Fourth, we need to jump-start a true, internationally competitive shipping industry. Eliminating the shipping cartel's antitrust exemption, tariff-filing requirements, and extensive government oversight of internal market practices would start the process.

Fifth, we must create an aggressive, internationally focused program within the multilateral trade framework to systematically eliminate foreign subsidies, restrictions, and antimarket practices.

The Lessons of Desert Shield and Desert Storm

The recent war effort should expose the national defense underpinning of current maritime policy for what it is—largely a myth. The maritime aspects of the Desert Shield/Desert Storm operation clearly demonstrated the importance of a fully integrated, intermodal system of transportation, including a

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comprehensive maritime leg, but they did not demonstrate the need for a merchant marine, particularly one as inefficiently maintained as the one we have today.

Military goods sent to the Persian Gulf were moved by rail, air, and truck to ocean ports, and a variety of ships were used, both U.S. flag and foreign, with American and foreign crews alike. The most highly valued cargo—the troops—were moved to the Gulf almost entirely by air, as was certain other high-value, high-force, time-sensitive weaponry.

Although there was an undeniable, urgent need for ocean transportation, Desert Shield/Desert Storm established beyond the shadow of a doubt that the military can efficiently execute its mission even without an American-built, American-crewed commercial fleet. Ninety-one percent of dry cargoes were moved on military prepositioned fast sealift

vessels, U.S. and effectively U.S.-controlled ships, and foreign (largely NATO countries) charter vessels. Only six of the fifty-nine ships specifically subsidized for the purposes of national defense actually moved through the minefields with their all-American crews directly into the war zone in Saudi Arabia. Thirty-eight other subsidized vessels transported goods on their regular liner service routes but used foreign-flag feeders, with foreign crews, to move the military goods to their final Persian Gulf destinations.

Many ships were simply unavailable to the military. Shipowners and military officials were concerned that any diversion of these ships for military purposes would lead to a permanent disruption of service and the loss of market share. In other cases the technical needs of military shipping coincided to only a limited degree with the needs of the merchant fleet. The container ships that dominate international shipping and the U.S. merchant fleet are virtually useless for the short-notice transport of tanks and other military equipment that must be rolled aboard. Prepositioned ships operated by the military—Roll-on-Roll-off (or “Ro-Ro”) and fast sealift vessels, for example—and a well-maintained, standby reserve fleet structured to meet changing defense needs would be more useful in providing rapid response and deployment. Continuing to tie the military to the viability of the commercial fleet today benefits neither party and, in fact, may harm both. Eliminating the already severed national defense linkage from civilian maritime policy is thus a necessary first step toward a rational consideration of the future of the U.S. commercial fleet.

The first casualty of this new policy would be the operating differential subsidy. The question is no longer how to save or reform this subsidy, but how to eliminate it in a way that maximizes the probability that the U.S. flag fleet can be saved and even expanded. Although the subsidy could be capped as a start, a more effective policy would entail a phased elimination of the subsidy in a way that allows U.S. carriers to adjust. One option would be simply to eliminate the subsidy as contracts expire and simultaneously to eliminate labor, market, and other flag restrictions.

Another alternative would be to incorporate a build-abroad option, combined with a per ship operating differential subsidy cap based on Coast Guard-derived manpower requirements and a phasedown of subsidy payments using a formula based on existing contract expiration dates. Given, in addition, the authorization to build and seek

greater ownership or financing abroad and to use mixed crews, U.S. carriers would thus have an opportunity to become strong competitors in the international trades.

Reducing or eliminating the personnel restrictions applied to U.S. flag carriers is as critical a piece of the puzzle as any other. The most cost-effective course would be full authorization for the use of international or mixed crewing. If the Defense Department identifies an actual wartime manpower requirement, then this could be met with a minimum American manpower commitment to, for example, two or three jobs on each ship on the basis of high-need, low-availability national defense categories. The subsidy would follow the specific jobs and would be limited to the incremental cost of maintaining the billet as American. Thus, national defense manpower requirements, if they really exist, need not be jeopardized.

A merchant marine reserve offers comparable advantages, and it would quantify and specify the military manpower requirement in a way that allows the military to advertise for and train individuals for availability in wartime—just as we now do in the other military reserves. This merchant marine reserve, with manpower requirements tied to specific reserve vessel billets and skill requirements, could be phased in as the operating differential subsidy is phased out. The Navy could, as another alternative, simply redirect a small portion of its existing naval reserve program to this purpose, at only the net cost of the transition.

The final and most potent element in reforming the commercial sector would be the consolidation of oversight and control of defense-related maritime programs in the Department of Defense. If defense is the skirt behind which maritime promotional programs are hidden, then let the defense planners decide when to lift it. Defense planning and budgeting would be better served under Defense Department control, and taxpayers would be better protected under a system where maritime budget allocation decisions had to compete with defense programs that realistically serve as substitutes or complements.

Shipyard Policy

The fate of American commercial shipyards occupies a crucial place in the policy arena. Although the shipyards have historically driven much of the debate regarding maritime policy—certainly the modern build-American requirement—today the

yards are almost universally viewed as an albatross around every other sector's neck. Over the past decade, the industry has lost a third of its capacity and more than 7,000 jobs, and today only one major oceangoing vessel is under construction in an American commercial yard. This has led to considerable political anxiety, but despite rhetoric to the

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contrary, it is not at all clear that the anxiety is generated by defense concerns.

From the national defense standpoint, two questions about U.S. shipyards are relevant. Is there any foreseeable military circumstance in which the United States will have the time or luxury to wait the one-and-a-half to two years necessary to build a ship for use in supplying troops at war? If not, is there a special policy requiring the maintenance of ship repair facilities for ship combatants in need of repair or breakout?

In response to the first question, regional or isolated wars of the sort we have seen over the past ten years are generally viewed as the most likely types of conflicts in the foreseeable future. The speed of those wars would preclude the construction or use of any vessels not in the fleet at the outset of the conflict. If a global war should break out, it is not likely to involve extended conventional warfare. There is little military justification for subsidizing commercial shipyards to build supply ships for a type of war we are unlikely to fight. This is independent, of course, from the naval shipbuilding programs that respond to longer-term defense needs.

On the other hand, reliable, U.S.-based repair facilities would be needed if the United States were involved in another war. But shifting the emphasis to repair facilities also suggests a much lower-level policy response than the industrial policy that is in place today.

In fact, commercial shipbuilding may well be able to stand on its own, but a variety of policy changes are required to give shipyards the flexibility and the marketing mindset needed to compete

effectively. First, competition itself is necessary to promote a competitive shipbuilding industry. Current restrictions on the use of foreign-built or foreign-repaired ships in either international or domestic commerce should be removed. Second, restrictions on the sale of U.S.-made, noncombat military vessels should be eliminated. Third, a limited, temporary, OECD-acceptable export credit program should be instituted to legitimately promote sales of U.S. ship

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products overseas. Fourth, federal R&D assistance to shipyards could be increased. Finally, there must be a serious commitment to pursuing government-to-government efforts—through GATT and other international forums—to reduce unfair practices, subsidies (both direct and indirect), and market impediments.

These approaches are aimed at three things: creating a competitive environment, benefitting from any comparative advantage that may exist in American shipbuilding, and creating a cash flow that leads to the renovation of aging yards. No policy can guarantee a competitive industry that no longer lives on federal handouts, but continuing current policies, notably the build-and-charter programs or reviving the construction differential subsidies, would without doubt perpetuate an uncompetitive dependence on taxpayer largess. And that largess is reaching its limits.

The Need for Regulatory Reform

If the promotional programs described herein are tied to arguably legitimate (although perhaps misguided) policy objectives, the FMC's regulatory mandate is far more tenuous, for it is based on the notion that a free fleet cannot compete in subsidized, cartelized, noncompetitive world markets.

The FMC operates under four basic statutes—the 1916 and 1936 Shipping Acts, the 1984 Shipping Act, and the 1988 Trade Act. These statutes constitute the basic regulatory regime covering roughly

half of ocean trade—the ocean liner or regularly scheduled common carrier portion of ocean shipping. The other half of ocean trade—that which carries bulk commodities such as oil and grain—is virtually unregulated from an economic standpoint.

A recent FMC study noted that the commission's regulatory focus has been on enforcing "requirements that international shipping practices be just, reasonable, and nondiscriminatory" and that international liner shipping regulation has "never" controlled entry or prices. The study also reported, "A second major difference between the regulation of ocean shipping and the regulation of other domestic transportation industries is the international scope of the activities involved." These statements, which are disingenuous at best, nevertheless articulate two key flaws embedded in maritime regulatory policy: first, that the international scope of the activities involved is more significant than those of other transportation sectors (the aviation industry would no doubt disagree), and second, that there are no barriers to entry.

Although the FMC administers no direct carriage barriers, significant barriers to both entry and exit, to financial innovation, and to management flexibility clearly exist in the network of federal policies from which regulatory policy cannot be divorced. The purpose of the flag restrictions and the Jones Act is, after all, to limit entry. Furthermore, the FMC itself enforces several indirect entry barriers. Bonding and tariff requirements for transportation middlemen, the enforcement of cartel pricing through the FMC's tariff-filing requirements and antidiscount rules, and the administration of other programs, including rate determination for domestic offshore (Jones Act) shipping, all serve to discourage new entrants.

There are modest genuflections to competition contained in the 1984 Shipping Act (which serves as the guidepost to the current commission). The 1984 changes have led casual observers to suppose that ocean carriage has been deregulated just as other transportation sectors have been. The reality, however, is that the adjustments introduced in 1984 merely provided protective cover from the Justice Department's Antitrust Division. Despite the limited nature of the changes, however, mandatory independent action (which allows a carrier to break from cartel pricing on one day's notice) and service contracting (which allows carriers and shippers to write public contracts outside the tariff, the terms of which must be made available to all who are willing and able to take them) provide at least a

glimpse of what could happen in a competitive market. True deregulation will have occurred, however, only when policy reforms are aimed at encouraging market-based competition, increasing customer/shipper options, and increasing benefits to American consumers. No such emphasis appeared in the 1984 act which is, at bottom, really designed to protect ocean carriers and the carrier cartels.

The century-old ocean carrier cartel (or conference) is one of the most defining and tenacious characteristics of the liner trade. At the turn of the century, the conferences were closed and thus met the test of a true cartel. Today, conferences in the American trades must be open—they must allow any carrier that meets their conditions to enter—but their ratemaking and market-restricting practices not only remain but are strengthened and enforced by government action. The conferences enjoy virtually blanket antitrust immunity, and the FMC enforces the tariffs. The commission's ability to intervene in conference actions is also limited to a few narrowly defined findings of unreasonable increases in price and decreases in service.

It is time for the American trading community to ask why the maritime industry should be treated differently from other international businesses. Are ratemaking cartels, revenue pools, restrictions on the right to contract with shippers, and so-called stabilization agreements that keep 10 and 20 percent of capacity off the market any more appropriate here than in trucking, rail transportation, retail sales, or the oil industry? If we oppose such practices in other industries, why not in ocean shipping?

Those who defend the cartel structure argue that modern ratemaking groups bear little resemblance to the early conferences. Proponents argue that the conferences are evolving from rate-setting cartels to efficiency-oriented organizations that help "rationalize" the ever-changing interactions between the supply of and demand for ocean carriage space. If the conferences are, in fact, undergoing such a metamorphosis, the U.S. government should be taking steps to speed the process. The reduction or elimination of antitrust immunity for ocean conferences, the removal of impediments created by the tariff-filing and enforcement process, and the removal of restrictions on the ability of individual shippers and carriers to write individualized contracts would all be steps in the right direction. Taken together, these reforms would create a revolution in shipping and would set a benchmark much of the international community would have to follow. There are three defining needs in regulatory reform.

Antitrust Immunity. The 1984 Shipping Act gives virtually blanket antitrust immunity to the ocean conferences. The bulk of this immunity can and should be removed. Carrier antitrust protection for all rate-setting activities, including the authority to discuss, fix, or regulate transportation rates, should be eliminated. Similarly, antitrust immunity applying to pooling (revenue-sharing) agreements should be removed. Successful pooling agreements are a significant impediment to flexible service, to technological and structural innovation, and to price competition. Because pooling agreements are usually effective only in trades where government support for them exists (the South American trades, for example), prohibiting these arrangements would not only improve ocean transportation services but would also provide a disincentive for bilateral agreements restricting ocean trade.

Ocean carriers should, however, be allowed to continue to establish efficiency-enhancing, cost-reducing rationalization agreements. Rationalization agreements that work—space chartering and facili-

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ties sharing, for example—often increase the ability of the carrier to compete and enhance its level of service. These types of agreements closely resemble joint ventures, and the Justice Department should be asked to determine whether this type of agreement even needs antitrust immunity. But worthwhile rationalization agreements also need to be distinguished from the capacity-reduction pacts that are simply agreements to restrict the use of vessel space and provide no benefits to shippers. Antitrust immunity for these capacity-reduction pacts should be eliminated.

Tariff Filings. The FMC administers the tariff-filing and enforcement program. All import and export rates must be filed, and a thirty-day wait is required for rate increases to take effect. If antitrust immunity for the conferences were eliminated, tariff- and

contract-filing requirements would probably go too, although tariff and contract filings are viewed by many as necessary to the notion of common carriage.

It is frequently argued that the tariff system protects small shippers by giving them access to the same rates the large shippers receive, but it is actually small shippers who are most bound by the tariff rates and requirements. As much as 60 percent of ocean shipping occurs through special service contracts outside the tariff, and these contracts allow shippers with market power to negotiate rates below the tariffs. There is nothing wrong with larger shippers' receiving volume discounts, but the existing

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tariff system tends to stymie possible deals for smaller ocean carriage users by discouraging rate reductions. In practice, tariffs generally provide few, if any, of the theoretical benefits of common carriage said to justify the system.

Enforcement by the FMC centers on eliminating discounts or, as they are sometimes called, rebates. Under the tariff system a carrier cannot reward loyalty through a tailored customer discount as it could in any other line of business. Where most would see a legitimate market practice, many in the ocean trades wrongly see unfair competition.

When the common carriage—unfair competition myth is set aside, the combination of tariff filing and enforcement is nothing more or less than interference with the ability of shippers and carriers to arrive at mutually agreeable contracts. Tariff-filing requirements drive competitive ratemaking under the table and turn a legitimate rate discount into an illegal rebate. Shippers and their customers end up paying more for ocean transportation than they would under a more liberal system.

Current tariff-filing and antirebate rules should be eliminated, or if tariff filing is retained, the thirty-day advance filing requirement should be replaced by a same-day filing requirement that would let rates move up and down as market forces dictate.

Service Contracts. In 1984, 459 specialized service contracts (the essential terms of which are made public) were filed with the FMC. In 1989 the number of contracts had increased by more than ten times to 5,250. Both shippers and carriers clearly view service contracts as beneficial.

The ability of carriers to write independent service contracts should be expanded, if not completely deregulated. If the conference system is retained, then the FMC's power to regulate or prohibit the use of service contracts should be eliminated. Furthermore, the contracting parties should be allowed to keep the essential terms of their agreements secret. Such privacy, which is afforded most other contracts, would accelerate the pace of the transaction and thus would increase competition.

The Future

Shipping interests and farming interests fight over cargo preference requirements. Gulf Coast seaports battle Great Lake ports over set-aside provisions. MarAd has been hauled into court by one maritime union that feels a recent subsidy decision will unfairly benefit a rival union. Various U.S. flag companies are involved in protracted legal battles over whether there is excessive competition in the protected West Coast-to-Hawaii trade. Is this any way to run a merchant marine?

It is no wonder that the U.S. merchant marine is in trouble. It is time to recognize that the U.S. flag fleet is in serious trouble *because* of the programs established to save it. Jones Act requirements, protective conferences, regulatory restrictions, and subsidies encourage, indeed often require, highly uncompetitive cost structures. Attempts to salvage these programs drain resources from the battle against the ultimate culprits—unfair practices abroad and labor and management lethargy at home.

The heart of our maritime policy has always been industry protectionism. Although some observers view maritime laws as the major part of the problem, other have come to live by them. Seamen and shipyard workers, bankers and vessel owners, and government regulatory officials and civil service maritime planners worry about what would happen if subsidies were cut, cargo preferences limited, or cabotage laws revised. The key differences between those who favor continuing these programs and those who favor more market-based reform are the fears of the former that the U.S. shipping and shipbuilding industries simply cannot compete effectively. But the industry is in

serious trouble now, and the only hope for turning it around over the long term is through procompetitive reform.

It cannot be true that the best this nation can do in terms of maritime policy is to increase the taxpayer and consumer burden through continued subsidies and economic protectionism while maintaining the government flag penalties that create the problem. Fundamental economic questions must be tackled directly, and changes that reflect the real interplay of markets and competition must be considered and implemented. It is time to set aside

the perceived limitations arising from both industry mythology and nationally self-inflicted restrictions.

If the maritime industry wants to be in a competitive trade position by the end of the century, then we must realize that other economic actors will increasingly play by the rules of markets and competition. The limits we place on our ability to play by these rules will be reflected in our shippers' inability to innovate and compete. And the limitations themselves will only be a mirror of our own inability to play on the world stage.