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STATEMENT OF ALAN S. BOYD, SECRETARY OF TRANSPORTATION,
BEFORE THE SENATE COMMERCE COMMITTEE, SUBCOMMITTEE ON MERCHANT
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The Need Today

During this Nation's first century, a strong merchant fleet carried American commerce -- under the American flag -- to and from the seaports of the world.

From that early development of commercial water routes, our Nation grew to its present position as the world's largest trading power. In 1967 alone, more than 400 million tons of goods -- valued at over \$36 billion -- moved in our oceanborne foreign trade. This was about one-sixth of the world's foreign trade, far more than any other country's share.

Our national growth and prosperity have depended in part on this foreign commerce. Our future growth and prosperity demand that our trade in the markets of the world continue to expand. In little more than a decade -- by 1980 -- our waterborne foreign trade should nearly double in size, reaching 700 million tons.

In the course of our trade expansion, the U. S. Merchant Marine has lost much of its vitality. Because of outmoded and uneconomical practices, capital and operating costs have skyrocketed. Lower construction costs in foreign shipyards, and lower operating costs of foreign vessels, have made it difficult for the Merchant Marine to compete with ships of other nations to carry our foreign trade.

Both the Merchant Marine and the shipbuilding industry have become increasingly dependent on Government subsidies. In fact, direct and indirect subsidies, together with preferential movement of Government cargo on U. S. flag ships, are largely responsible for keeping our Merchant Marine alive.

This dependence on Government support has led to detailed Government involvement in matters of management.

Over the past several years, programs to strengthen the industries have been subjected to exhaustive study and intensive debate -- within the Government and in public forums as well. There have been a large number of proposals aired recently on what to do about the Merchant Marine. All of them agree that changes and reforms are essential and long overdue. At the same time there is little agreement regarding the direction or details of reform.

The problem is not an easy one. For the last three years we have analyzed and discussed the many arguments and the suggested solutions. We have talked at length to all representatives of the merchant marine and shipyard industries -- both on the management and labor sides. The Administration has thoroughly considered the possible alternatives. Now more than ever we are convinced that the future of our Merchant Marine demands a shift from past policies: To provide the streamlining and flexibility that is needed to enable it to cope with the competitive world of today and the future. These conclusions emerge:

- Subsidy support should be provided only to meet this Nation's security needs. Ship operating support should be clearly distinguished from ship construction support.
- Although Federal support must continue if the Merchant Marine is to survive, Federal dollars alone will not solve the problems of the maritime industries.
- The genius of the free enterprise system -- of skilled labor and profit-motivated businessmen, stimulated by competition -- must be called into full play if the industries again are to prosper.

- Our present subsidy systems do not provide incentives to use fully the resources and talents of American industry.

A New Maritime Program

I am here this morning to present the Administration's Merchant Marine program.

We are convinced that the program being proposed is based on the kinds of public interest considerations which should guide the formulation of any Federal program.

Certainly, the public interest requires of the maritime program that we examine:

- How much and what kind of a Merchant Marine we need to subsidize and for what purposes.
- How much shipbuilding capacity we need to support and to what extent this should be supported by subsidized merchant marine programs -- rather than Navy or other programs for building and repairing government-owned vessels.
- What specific policies and programs would best implement our determinations of the public interest in these areas.

We believe that America's maritime industries can reestablish their position of importance in the commercial life of this Nation, if they are

- revitalized through the application of advanced industrial technology and sound business practices.
- incorporated into an integrated transportation system.

The Administration proposes five major steps to accomplish these purposes to modernize our maritime industries:

1. Expand the scope and improve the system of ship operating subsidies, and establish the amount of subsidies according to the size of the fleet necessary for national security.
2. Reform the construction subsidy system and relate this subsidy to the Nation's need for an adequate shipyard capacity for national security.

3. Remove restraints on the freedom of shipowners to purchase ships in the world market -- treating ship-owners like other American purchasers of transportation equipment and subject to the same restrictions on foreign investments and expenditures.
4. Expand maritime transportation research.
5. Transfer the Maritime Administration to the Department of Transportation.

Ship Operating Subsidies

Enduring through the years as a tradition, the Merchant Marine has declined as an industry. Its decline parallels its increasing dependence on Government support through subsidies of one kind or another. Subsidies -- direct and indirect -- have been a compromise answer to a difficult situation. They have prevented both the death and the nationalization of the Merchant Marine. At various times in our history, the Congress and the Executive Branch have shaped the principle of subsidy to meet the demands of the day.

The Merchant Marine Act of 1936, which established the basic policy under which we operate today, was a remarkable accomplishment for its time. Three decades ago -- and for a considerable period after -- it helped to promote our foreign trade and our national security. Now it is time to take another thorough and searching look at the Merchant Marine and the subsidy system that sustains it. In this time of budget stringency, Government spending must meet the most rigorous tests of necessity.

The Merchant Marine -- like any other program requiring Government support -- should be subsidized only to the extent necessary to meet a compelling national need. That need can be clearly identified: We must have adequate shipping to meet our military requirements and those urgent non-military demands that would prevail in time of emergency. It is only to this extent that our maritime fleet should be subsidized. Beyond this level, the fleet should meet the tests of the free market.

Subsidy Reform

The subsidy system itself is in clear need of reform. Instead of encouraging innovation and productivity, the system focuses attention on the subsidy dollar as a source of income. A new system must be found that will induce the industry to take full advantage of advancing technology, management ingenuity, and the resources of a skilled labor force.

The Government now subsidizes the ship operator to make up the differences between certain elements of his operating costs and those of his foreign competitors. This process has proven inadequate and unsound. For example:

- It requires a network of Government auditors in the steamship company's offices, as well as an overseas staff of Government employees to provide estimates of foreign operating costs.
- It imposes cumbersome administrative procedures upon the operator, who is forced to make a detailed justification for each of his subsidy-related costs.
- It requires strict adherence to trade routes and restricts the operator from taking advantage of shifting market conditions.
- It gives the operator little incentive to hold down costs, since increases are borne by the Government.
- This direct subsidy has only been available to a part of the fleet.

To correct these deficiencies -- and at the same time to assure operators a reasonable rate of return on their investments -- the present system must be restructured to promote business judgment and operational flexibility, and minimize Federal involvement and intervention. The restructured system should be made available to other categories of ship operators to replace indirect subsidies they now receive.

The Administration recommends legislation to authorize the Secretary of Transportation to enter into contracts with qualified applicants to test more productive and competitive operating subsidy systems.

Over the past few years, a number of alternative subsidy systems have been studied and developed. These systems will be examined thoroughly. The Government and operators together will examine these systems and experiment with the most promising. Different systems can very likely be tried simultaneously, in different trading areas. Whichever are found the most productive through actual experience will then be put into effect. All operators will be required to use the systems selected to be eligible for subsidy support -- new operators upon entry and the present subsidized operators upon expiration of their current contracts.

Bulk Cargoes

Dry bulk cargoes total about 35 percent of our foreign trade. More than 140 million long tons are carried each year. By 1980, that trade is expected to rise to over 380 million tons. Very little of this goes on U. S. flag ships, however -- because

the American ships in this bulk trade are old and inefficient and unable to compete for commercial shipments. The answer is to promote the development of an efficient and up-to-date U. S. flag bulk carrier fleet. At the present, this cannot be done because operating subsidies are not extended to bulk carriers.

The Administration recommends legislation to authorize a system of innovative operating subsidies, such as those described above, for new bulk carriers to be built under a new construction subsidy program -- which is detailed later in this testimony.

Passenger Ships

Passenger ship operations under the American flag are costly in subsidies, and return only minor benefits. The sharply accelerating trend to air travel raises serious questions about the economic future of this mode of transportation.

At present, about \$50 million goes annually to the support of 13 ships -- which are turning more and more to luxury cruises. This is equivalent to \$275 for every passenger carried.

Once important as emergency troop transports, the defense value of these vessels is now minimal. Their subsidization can no longer be justified on this basis.

Operators of passenger ships will be encouraged to terminate their subsidy contracts voluntarily so that the funds can be allocated to more productive purposes.

Nuclear Ship Program

There is serious doubt as to the attractiveness and wisdom of proceeding with a broader nuclear ship program at the present time. It appears that power reactors of the relatively small sizes required for merchant ship propulsion will continue to be non-competitive with oil over the foreseeable future.

Construction Subsidies

At this time, the Administration does not seek increased subsidies for the construction of ships. For the present, I believe the construction subsidy program should be held at a level of about \$110 million, roughly its present level. For the future, however, we need to know how much will be required to meet national emergency demands for shipbuilding capability.

The proposed legislation would authorize the Secretaries of Defense and Transportation to recommend jointly to the President the level and character of ship construction subsidies.

Each year the two Secretaries will:

- Determine the national emergency need for private shipyard activity and capacity.
- Ascertain how much and what kind of Federal support is necessary -- beyond that provided through Navy and other programs which build Government vessels -- to maintain an adequate emergency capability for ship construction and repair.
- Determine to what extent this additional support should be provided by subsidies for merchant marine construction.

In making their determinations the Secretaries will consider such factors as long-range plans for emergency construction or repair, and the need to maintain specialized skills.

For Greater Flexibility

The present construction subsidy system is too inflexible. It does not encourage shipyards to propose a standardized design which several operators can use. It fosters, instead, costly individual designs. Under existing practice, an operator submits to the Maritime Administration a design tailored to his individual needs -- for one ship or a few. This individual design is then put out for bids among the shipyards. The bids are generally high -- reflecting the cost of constructing just a few custom-built ships. The small market for commercial ships in the U. S., and limited competition, add further to the cost of ships built in American yards. In large measure, these costs are borne by the taxpayer -- since the Federal subsidy to the ship buyer is the difference between the shipyard's high price and the estimated cost the operator would pay in a foreign shipyard.

The construction subsidy program should be made more flexible and better able to produce ships less expensively.

The Administration recommends legislation to encourage the shipyard to design and develop ships which can be built with the modern production techniques that have made our aircraft industry predominant in the world today.

Under this system, this subsidy would be paid directly to the shipyards. Shipbuilders would be told precisely what proportion of construction costs the Government would pay.

The yards would then compete with each other for sales to domestic or foreign ship purchasers on the basis of what they could construct with available subsidy funds. The proposals calling for the least subsidy dollar per productive unit would receive the subsidy.

With preference thus going to shipyards producing at the lowest cost per ship, yards will be encouraged to design and sell their ships on an efficient multiple-production basis -- just as aircraft companies aggressively market their designs to the airlines.

Foreign Ship Purchase

In the Nation's infancy, American shipowners were required by law to buy only American built ships. This was necessary then for the development of a shipbuilding industry. Today, America's ship construction industry is the largest in the world by nearly any measure. It can draw upon the country's great technological resources. Its size and health are ensured by a naval construction and repair program which infuses more than \$2 billion of Government funds into the industry every year. Yet our merchant shipowners are under almost the same constraints as those of two centuries ago. To engage in domestic trade, or to be eligible for a subsidy, they must buy only in U. S. shipyards.

Since merchant ship work under Government subsidy amounts to less than 10 percent of the shipbuilding industry's business, this restriction cannot be justified as essential to the industry's health. An American operator should not have to base his plans for purchases of new ships on the amount of construction subsidies available.

After the necessary level of ship construction in U. S. shipyards has been reasonably assured, American ship operators will be permitted to purchase their vessels in the world shipbuilding market and these ships would be accorded the same treatment as ships built in American yards.

To protect our balance of payments position, controls will be exercised in accord with our programs restraining foreign expenditures and investments. By requiring the cost of the vessels to be financed through foreign loans, we can avoid a drain on American dollars. Ships built in foreign shipyards for documentation under the U. S. flag would be required to meet all U. S. standards of safety and construction. They would be eligible for all privileges available to U. S. flag operators in the U. S. foreign trade. American flag operators in domestic trade would also be permitted to employ a limited number of foreign-built ships -- with procedures to assure established operators will not be harmed.

Reserve Funds

The maritime industry -- as do many other industries -- requires large amounts of capital for the construction of modern, efficient equipment. At present, certain ship operators are not taxed currently on funds put in reserve and used for this purpose. These operators therefore pay taxes on different terms from other ship operators and other businesses. This system is complex and inequitable.

The Administration program contemplates that the setting aside of these funds will be terminated at the expiration of the present contract commitments. The future capital investments of the Merchant Marine can then come under the depreciation guidelines and the investment credit rules of the Treasury Department similar to those governing other industries. We also contemplate orderly liquidation -- consistent with existing contracts -- of present reserve funds over a reasonable period of time.

In addition, the Secretary of the Treasury will undertake a review of our tax law as it affects the shipping industry including U. S. owned ships under foreign flags, with a view toward recommending other legislation to remove unjustified tax advantages.

National Defense Shipping Needs

National Defense Reserve Fleet

The National Defense Reserve Fleet was established at the end of World War II. It has served this Nation well in two major emergencies. During periods of crisis, the breaking-out of this inactive fleet has been an important factor in preserving our national security and in maintaining stable rates in the world shipping market. This method of meeting peak emergency needs is less expensive in limited emergencies and causes less disruption of commercial service than other alternatives.

To improve this capability, we ask authorization for an initial appropriation of \$30 million for Fiscal 1970, to revitalize the National Defense Reserve Fleet.

These funds will be used to build a limited number of new vessels of austere type, and to convert some relatively unused reserve troop ships into general cargo ships. These ships will be retained in the reserve fleet for emergency use.

Fast Deployment Logistic Ship Program

No expansion of the Merchant Marine will fill the military need for rapid-response sealift. This vital need can best be met through the Fast Deployment Logistic Ship program.

Fast Deployment Logistic Ships (FDL's) will not compete with the Merchant Marine. The ships are designed for quick and flexible military response. They can operate without ports, if necessary. They are an essential part of our strategic planning. They must be available at all times to enhance our national security. Last year the Congress did not act on the Administration's recommendation that an FDL program be started.

This year, the budget includes a request for \$184 million to fund this important program. The Administration urges the Congress to approve it promptly.

Expanded Research

The Administration recommends a 5-year program of \$25 million annually commencing in Fiscal 1970, to increase both basic and applied maritime research activity -- conducted in cooperation with private industry.

The goal of this research will be to improve the competitive position of the U. S. maritime industries by acquiring new knowledge of:

- ship operations and design,
- cargo handling systems on ships and ashore,
- port facilities,
- basic hydrodynamics related to modern merchant ship hull forms,
- ship construction methods,
- integration of sea and land systems.

Management-Labor Responsibility

The program of reforms that I have outlined will aid in bringing the U. S. Merchant Marine into today's competitive world and make it an active and productive part of our commercial life and our future growth.

The Government can go only a part of the way toward this goal, however. Essential steps must be taken by the elements of the maritime industries themselves -- management and labor in the operating Merchant Marine, in the shipbuilding industry, and in allied industries. Federal subsidy dollars must not be dissipated through price inflation or excessive wage increases. Otherwise, their potential benefits would never be realized. America's maritime capabilities would remain weak and ineffective. An important part of the program being recommended today is to insure that wages will be stabilized and that bid prices will be reasonable and competitive.

Wage Structure Stabilization and Work Stoppages

If the U. S. Merchant Marine is to respond to the needs of the American shipper, both management and labor must work closely to

- eliminate the recurring interruptions in service caused by work stoppages. Such interruption destroys confidence in U. S. flag carriers. Shippers consequently turn to foreign flag vessels for their needs.
- stabilize the maritime industry's wage costs.

A series of labor-management agreements, negotiated in 1965 to help assure wage stability, have in practice accomplished the opposite. Under these agreements, if the members of one union receive a wage increase or other benefit, other maritime unions can reopen their contracts through a "me too" clause and demand arbitration to obtain a matching increase. By the time several unions have received such increases, the first union is in a position to assert that it is once again behind the others -- and the cycle starts over again.

Because of this practice, employment costs in the industry have risen more than 30 percent since 1965. These costs increase Federal expenditures through the operating subsidy program and shipping costs on Government cargoes. They diminish the ability of the U. S. Merchant Marine to compete with foreign fleets. Not only do spiraling employment costs threaten the industry with economic ruin, they imperil the American public as well, for they have a shattering impact on our Nation's wage-price stabilization objectives.

We call upon management and labor -- working with the Secretaries of Labor and Transportation -- to begin discussions promptly to solve this problem.

An Integrated Transportation System

No improvements we can make in our maritime fleet will permit it adequately to meet America's need today unless it is fully integrated into a unified national system of transportation. When the President signed the Department of Transportation Act in October 1966, he expressed regret that the new Department did not include the Maritime Administration. He expressed hope that the Congress would reexamine its decision. This reassessment is now vital to our maritime future.

The Administration recommends legislation to transfer the functions of the Maritime Administration to the Department of Transportation.

This step will bring increased recognition to ocean shipping in the transportation policy councils of the Executive Branch.

The Department of Transportation was created to promote a more efficient national transportation system. This cannot be fully accomplished so long as the maritime component of the transportation system remains outside the Department's jurisdiction.

The Maritime Administration itself suffers in its isolation from the new technology and promotional support which the Department now provides to other elements of our national transportation system. Potential developments which hold great promise for maritime commerce affect other modes of transportation as well. Ports, for example, must provide facilities which can rapidly handle cargoes arriving and leaving by rail and highway. Container systems must be developed which can be economically used on all modes of transportation, so cargoes can move without interruption from origin to destination.

Transfer of the Federal Government's maritime programs to the Department of Transportation will permit fuller coordination of all our research resources for the improvement of our entire transportation system. Each mode will benefit greatly. But most important, the Nation's intricate and extensive transportation network will be strengthened, and better able to serve the complex needs of our society. This organizational change is the key to a truly effective maritime program. Legislation to accomplish this and other elements of the program I have outlined is attached as an appendix to this statement.

Conclusion

A strong and healthy Merchant Marine has been a proud element of our national strength. It can be so again.

It is deeply in the national interest that we revitalize our Merchant Marine and make it both effective and competitive -- a maritime service which is not just barely kept alive by Government subsidies and Government cargoes, but one able to attract a significant share of our commercial trade as well.

I believe the program I have outlined will accomplish this. With its passage, and with the cooperation of maritime management and labor, we can realize the goals we have set. This program provides the cornerstone on which we can build anew the maritime tradition of the American past.

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