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## *We and Mr. Jones: How the Misunderstood Jones Act Enhances Our Security and Economy*

Samuel A. Giberga\* & John Henry Tab Thompson\*

### I INTRODUCTION

Last year, a reputable Washington, D.C. think tank hosted a round table discussion on the Jones Act. As the general counsel of one of the largest owners and operators of Jones Act-qualified vessels I expressed interest in the event. Event organizers politely declined to include my viewpoints in the discussion. When I pressed the organizers to explain, their resistance became more pointed. The think tank informed me that they did not want to “let the opposition know our strategy.” This language struck me as odd. By what logic is a company that employs thousands of U.S. workers and has spent billions in U.S. shipyards the “opposition” of anyone? And is not the exploration of opposing ideas an integral part of what think tanks are supposed to do? As I dug further, it became clear to me that the Jones Act is terribly misunderstood even by some very smart people in Washington policy shops.

This paper defines the scope of the Act and evaluates the legislation on historical, national security, and economic grounds. It is my goal to clarify many misconceptions in the hope that as we think about the Jones Act, we will avoid echo chambers and instead engage in meaningful dialogue.

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\*Samuel A. Giberga is the Executive Vice President and General Counsel of Hornbeck Offshore Services, Inc., the owner and operator of one of the largest fleet of Jones Act qualified offshore service vessels supporting offshore energy development. John Henry Tab Thompson is currently a first year law student at the University of Chicago Law School.

## II JONES ACT VESSELS AND THE STATE OF THE JONES ACT FLEET

To understand the Jones Act and its role in American shipping policy, one must first understand what it means for a vessel to be a *U.S. flag* vessel and a *Jones Act-qualified* vessel. Not all U.S. flag vessels are qualified under the Jones Act. Missing this fundamental point is a common mistake that leads to flawed conclusions. So let us begin with the basics. A vessel with a United States flag is eligible for two possible endorsements to its registration with the United States Coast Guard: (1) a coastwise endorsement, or (2) a registry endorsement.

In order to receive a *coastwise endorsement*, a vessel must comply with the Jones Act (the Merchant Marine Act of 1920). In addition to operating under U.S. flag, the vessel must be constructed in the United States, it must be crewed by United States citizens and it must be owned and controlled by citizens of the United States. For purposes of the Jones Act, a corporation is a citizen if at least 75 percent of its ownership interests are held by citizens of the United States.<sup>1</sup> Only a vessel with such an endorsement is authorized to transport merchandise between or among two or more points in the United States.<sup>2</sup> Thus, when discussing Jones Act-qualified vessels

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<sup>1</sup>Outline of Jones Act citizenship requirements (from U.S.C. § 50501 (a)-(d)(4)): (1) "the controlling interest [must be] owned by citizens" (2) "at least 75 percent of the interest must be owned by citizens" (3) the corporation must be incorporated under U.S. or state law (4) the corporation's CEO and chairman of the board of directors must be citizens, (5) Noncitizen directors may not constitute a minority large enough to constitute a quorum. Source: NYU Law Review, 2014 ([http://www.nyulawreview.org/sites/default/files/pdf/NYULawReview-89-3-Michaeli\\_0.pdf](http://www.nyulawreview.org/sites/default/files/pdf/NYULawReview-89-3-Michaeli_0.pdf))

<sup>2</sup>The exclusivity given to Jones Act qualified vessels to operate domestically is not unlike other aspects of the transportation industry. We do not see Kuwaiti Airlines offering flights to U.S. travelers between Memphis and Chicago, because the United States wants to reserve the majority of its over-flights to airplanes owned and piloted by United States citizens. That does not mean that a Kuwaiti airliner cannot fly to the United States from Doha. It can, but after its flight, it needs to leave. Similarly, a Honduran trucking company cannot set up shop to haul fuel or chemicals between Tegucigalpa, Oklahoma City and Des Moines. While NAFTA allows Mexican trucking companies access to our highways, they cannot make intermittent stops. A

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and the Jones Act trade we are referring exclusively to domestic—not foreign—transportation of merchandise on U.S. flag vessels that have a coastwise endorsement. Think: New Orleans, Louisiana to Paducah, Kentucky.

A cargo vessel registered in the United States that does not have a coastwise endorsement has a *registry endorsement*. The requirements for obtaining such an endorsement are not as stringent as those for a coastwise endorsement. Such a vessel may be constructed anywhere in the world. For registry vessels, the requirement that U.S. citizens own 75 percent of the equity interests of the company does not apply.<sup>3</sup> Lacking authority to transport cargo in the domestic United States trade, such vessels engage exclusively in international voyages. Think: Los Angeles to Hong Kong.

As vessels committed to domestic service, the physical appearance of Jones Act vessels is very different from their international registry endorsement cousins. The two fleets are drastically different in terms of their size as well. While registry vessels tend to be large cargo carriers that we usually think of in the context of international shipping (the Maersk Alabama is a recently celebrated example), the Jones Act trade is dominated by movements of cargo on our internal waterways and our seaways. There are approximately 200 U.S. flag vessels with registry endorsements. On the other hand, there are currently nearly 40,000 Jones Act qualified vessels.<sup>4</sup> Critics of the Jones Act often misunderstand the distinction between these two fleets and cite

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Mexican truck can move cargo from Monterrey to Dallas. However, it may not then pick up a load and move it to New York. There are obvious and good reasons for these requirements, which apply perforce when we think about domestic waterborne transportation, and which will be discussed in greater detail later in this article. Suffice to say, there is nothing necessarily unique about the Jones Act in U.S. or international cabotage legislation.

<sup>3</sup>For registry vessels, the requirement that 75 percent of the equity interests of the company be owned by U.S. citizens does not apply. Source: [http://www.hklaw.com/files/Publication/4c464688-d79f-4406-980d-a70245e9d82c/Presentation/PublicationAttachment/7cf023ee-4b91-4b66-89e5-632dea70e2b5/USA\\_03\\_08\\_2013\\_10\\_44\\_42\\_530%20\(2\).pdf](http://www.hklaw.com/files/Publication/4c464688-d79f-4406-980d-a70245e9d82c/Presentation/PublicationAttachment/7cf023ee-4b91-4b66-89e5-632dea70e2b5/USA_03_08_2013_10_44_42_530%20(2).pdf)

<sup>4</sup>Source: 2011 US Water Transport Statistical Snapshot ([http://www.marad.dot.gov/wp-content/uploads/pdf/US\\_Water\\_Transportation\\_Statistical\\_snapshot.pdf](http://www.marad.dot.gov/wp-content/uploads/pdf/US_Water_Transportation_Statistical_snapshot.pdf)).

the declining size of the registry fleet to illustrate the “historic decline” of U.S. shipping as a whole. While the U.S. registry fleet has faced decline for reasons that will not be discussed in this paper, that decline does not characterize the 40,000 vessel strong Jones Act Fleet, which has consistently grown in size and capacity.

There are approximately 7,500 self-powered Jones Act-qualified vessels plying our domestic waters. As the name suggests, “self-powered” means a vessel has a propulsion system that allows it to move itself. These 7,500 vessels consist mostly of tugs, which push or tow approximately 30,000 barges. Barges are a key aspect to our national maritime system. They are loaded with everything we consume domestically. Coal from Kentucky moves on the Ohio and Mississippi rivers. Petroleum products from the Gulf Coast, and grains from the Midwest, move on the Mississippi River. Barges move all manner of rock, ore, grains and other bulk cargos on the Great Lakes and through the Saint Lawrence Seaway. The Columbia and Snake rivers feed West Coast consumers and exporters. Tugs and barges, which account for the vast majority of the Jones Act fleet, are the engines of American domestic commerce.

The next largest component of the Jones Act fleet consists of around a thousand offshore support vessels<sup>5</sup> that are used in the effort to explore for and produce hydrocarbons found on our outer-continental shelf, which is considered a point within the United States. On an invested cost basis, this component of the Jones Act fleet dominates in terms of value. The cost of constructing an offshore support vessel today is in the range of \$30 to \$40 million.

The smallest portion of the Jones Act fleet consists of about 200 hundred vessels that look more like the ships we think about when we think about international shipping. These 200 container vessels, tankers, roll-on and roll-off vessels and other bulk carriers carry cargo between ports within the continental United States, as well as between continental points and “non-

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<sup>5</sup>Source: [http://www.marad.dot.gov/wp-content/uploads/pdf/US\\_Water\\_Transportation\\_Statistical\\_snapshot.pdf](http://www.marad.dot.gov/wp-content/uploads/pdf/US_Water_Transportation_Statistical_snapshot.pdf).

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contiguous” points like Hawaii, Puerto Rico, Guam and Alaska. While comprising the smallest part of the Jones Act fleet, these vessels capture the lion’s share of attention from the Jones Act’s critics. Critics often claim that the Jones Act is keeping this number below its optimal level, or that these are the only ships that matter when evaluating the Jones Act fleet’s vitality. To the contrary, as noted above, the rest of the Jones Act fleet dominates both in sheer numbers and in terms of invested cost. This is not to minimize the importance of large tankers and bulk carriers to the domestic maritime industry. But they cannot be used as a proxy for the entire Jones Act fleet, nor can the trends that impact these vessels be blindly extrapolated to cover all sectors of domestic shipping.

A recent study from the Heritage Foundation provides a case in point. The authors argue that the U.S. shipping industry has been in decline and assigns the blame to the Jones Act.<sup>6</sup> While they are correct in that the international fleet of U.S. flag vessels (i.e., registry endorsement) has been in decline for decades, that decline has nothing to do with the Jones Act. Again, the Jones Act is concerned with domestic transportation; it has no impact on U.S. international shipping. Blaming the Jones Act for the decline in the prominence of U.S. international shipping is like blaming the barber for my weight gain. When investigating that decline, Heritage and other critics would do better to focus on the real culprits of lost competitiveness (more discussion of this later).

Compared to the fortunes of the registry fleet, investment in Jones Act-qualified vessels is far stronger. While the entirety of the registry fleet today is comprised of about 200 vessels, since 1987 an average of 176 self-propelled Jones Act-qualified vessels have been constructed in U.S. shipyards *every year*.<sup>7</sup> Not included in this number are the thousands of barges, ranging from small hopper barges to 300,000-barrel tank barges. As of 2014, U.S. shipyards were contracted to build 150 Jones Act vessels,

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<sup>6</sup>Source: [http://www.heritage.org/research/reports/2014/05/sink-the-jones-act-restoring-americas-competitive-advantage-in-maritime-related-industries#\\_ftn3](http://www.heritage.org/research/reports/2014/05/sink-the-jones-act-restoring-americas-competitive-advantage-in-maritime-related-industries#_ftn3).

<sup>7</sup>Source: [http://www.marad.dot.gov/wp-content/uploads/pdf/US\\_Water\\_Transportation\\_Statistical\\_snapshot.pdf](http://www.marad.dot.gov/wp-content/uploads/pdf/US_Water_Transportation_Statistical_snapshot.pdf).

consisting mostly of offshore support vessels, tugs and tankers being constructed to support the recent boom in shale oil production. Each vessel costs tens of millions of dollars to construct. This fleet, as noted, is owned by U.S. companies, which pay U.S. taxes, employ U.S. crews (also taxpayers), is built in U.S. commercial shipyards (paying U.S. taxes) employing thousands of shipyard workers (again, taxpayers) and supports communities and economies around the country. The industry's impact does not stop there. It uses steel from U.S. mills, marine engines built mostly in U.S. manufacturing facilities and many other American-made components. Shipping depends upon—and thus fosters—various supporting trades and professions. The domestic marine industry is a powerhouse, accounting for over 80,000 American jobs and impacting an additional 400,000 jobs.<sup>8</sup>

### III WHY DO WE HAVE THE JONES ACT?

It is not unreasonable to ask why we reserve domestic shipping to Jones Act-qualified vessels. Why not just allow vessels of any nationality to compete for work on our rivers, lakes and seaways? The reasons for this policy are deeply rooted. Quick to note that the Jones Act dates from the 1920s, many critics characterize the statute as an aging relic. Setting aside the dubious proposition that mere oldness makes a statute suspect (the United States Constitution is also an old statute), these critics have their history wrong. The Jones Act's historical *bona fides* date from far earlier than World War One. Indeed, the Jones Act is progeny of the United States' first "cabotage" law, which was the fourth act of the very first United States Congress.<sup>9</sup> Thus, cabotage—the idea that a nation should reserve domestic shipping for its citizens—is not something that was cooked up by Senator Wesley Livsey

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<sup>8</sup>*Contributions of the Jones Act Shipping Industry to the U.S. Economy in 2011*, prepared by PricewaterhouseCoopers for the Transportation Institute (January, 2014).

<sup>9</sup>The act can be read here: [https://en.wikisource.org/wiki/United\\_States\\_Statutes\\_at\\_Large/Volume\\_1/1st\\_Congress/1st\\_Session/Chapter\\_11](https://en.wikisource.org/wiki/United_States_Statutes_at_Large/Volume_1/1st_Congress/1st_Session/Chapter_11).

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Jones in 1920. It predated the founding and was adopted by the architects of our nation as a principle essential to the success of the United States.

The Founders understood that Americans are a maritime people. We were in 1790 and we are today. The first United States Congress was mindful of what Jones Act critics appear to ignore: great nations, throughout history, have been maritime ones. Spain lost its Armada and never recovered. Imperial Britain's greatest strength was its naval and merchant marine supremacy. We should not forget these lessons of history, particularly when maritime dominance is a well-publicized objective of the People's Republic of China (as evidenced by their exploits in the South China Sea). Russia's foray into the Crimea has, perhaps, as much to do with access to a key port on the Black Sea (thereby claiming a vastly larger share of Black sea oil deposits) than it does with reuniting ethnic Russians with the motherland.

The U.S. intensified its original cabotage laws on several occasions leading up to the passage of the Merchant Marine Act of 1920 (the legislation referred to as the Jones Act). Each intensification—like the original statute—followed international conflict at home or abroad. The original cabotage statutes followed our War for Independence. The Navigation Act became law following the War of 1812. World War One preceded the Jones Act. While many characterize the Jones Act as protectionist, the law and the principles it advances are more properly understood as derived from a healthy desire for the nation to be able to attend to its maritime needs as a matter of national security and internal defense. The Jones Act is not intended to protect an industry; it is rather *literally* protectionist in that it is intended to protect the nation. The historical record explains this intent. Congress, in passing the Jones Act went out of its way to emboss the statute with a preamble explaining its rationale:

It is necessary for the national defense and for the proper growth of its foreign and domestic commerce that the United States shall have a merchant marine of the best equipped and most suitable types of vessels sufficient to carry the greater portion of its commerce and serve as a naval or military auxiliary in time of war or national emergency, ultimately to be owned and operated privately by citizens of the United States; and it is declared to be

the policy of the United States to do whatever may be necessary to develop and encourage the maintenance of such a merchant marine . . . <sup>10</sup>

Our maritime heritage is one of the reasons that the United States has emerged as a great nation. We have always expanded with watery borders, be they inland waterways, such as the Mississippi River acquired as part of the Louisiana Purchase, or westward expansion to the Pacific, inclusive of our 49th and 50th states. To be a maritime nation requires a robust domestic maritime culture, steeped in traditions of seafaring, shipbuilding, maritime defense and stewardship of our oceans and other waters. Ronald Reagan, considered a leader in the modern advancement of free trade principles, was an ardent supporter of the Jones Act.<sup>11</sup> Reagan was in good company among free traders as it concerns cabotage laws. Adam Smith himself placed an asterisk upon his free trade theory when it came to Great Britain's maritime interests. Addressing the British Navigation Act, Great Britain's cabotage law at the time of Smith's publication of *The Wealth of Nations*, he noted:

. . . some particular sort of industry is necessary for the defense of the country. The defence of Great Britain, for example, depends very much upon the number of its sailors and shipping. The act of navigation, therefore, *very properly endeavors* to give the sailors and shipping of Great Britain the monopoly of the trade of their own country . . . <sup>12</sup>

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<sup>10</sup>Source: Original text of the Merchant Marine Act of 1920, from Section 46 of the Federal Code ([http://www.upa.pdx.edu/IMS/currentprojects/TAHv3/Content/PDFs/Jones\\_Act\\_1920.pdf](http://www.upa.pdx.edu/IMS/currentprojects/TAHv3/Content/PDFs/Jones_Act_1920.pdf)).

<sup>11</sup>The Reagan White House's position on the Jones Act: "The principle that a nation's own ships should carry its coastal trade, presently embodied in the Jones Act, has been a part of this country's maritime policy since the early days of the nation. I can assure you that a Reagan administration will not support legislation that would jeopardize this longstanding policy or the jobs dependent upon it." ([http://www.aei.org/wp-content/uploads/2014/07/-american-domestic-shipping-in-americas-ships\\_111755682253.pdf](http://www.aei.org/wp-content/uploads/2014/07/-american-domestic-shipping-in-americas-ships_111755682253.pdf)).

<sup>12</sup>Adam Smith's *Wealth of Nations* (<http://econlib.org/library/Smith/smWN13.html#IV.2.24>). Emphasis added.



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The “act of navigation” of which Mr. Smith wrote, while detested by the colonial Americans, was emulated by them upon the founding of the nation for the very reasons observed by Smith. Then as now, our national defense depends upon “the number of our sailors and shipping”.

The charge of “government support” or “subsidy” leveled at the Jones Act, as part of an attempt to paint the domestic shipping industry as wholly reliant on the government, does not hold water upon closer examination. Compared to the shipping industries of competitor nations such as China and Korea, Jones Act shipping in the U.S. is practically unassisted by government subsidies.<sup>13</sup> The fact that the Jones Act reserves the privilege of engaging in domestic shipping to American citizens (shipbuilding, crewing, etc.) does not mean that the domestic industry is “being propped up.” To characterize the Jones Act as protecting or “propping up” the domestic shipping industry, in the way that, for instance, billions of dollars in direct subsidies support American agriculture, is wrongheaded. The notion that American companies involved with the Jones Act fleet are recipients of gratuitous largess would come as a surprise to the employees and stakeholders of such companies. Yet, reality has not stopped critics from describing the

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<sup>13</sup>MARAD administers two programs designed in part to benefit vessels engaged in the coastwise trade of the United States: (1) the Capital Construction Fund (“CCF”) and (2) the Federal Ship Financing Program (commonly referred to as the “Title XI program”). The CCF program assists owners and operators of United States flag vessels in accumulating the large amounts of capital necessary for the modernization and expansion of the United States merchant marine. This program is similar to other policies aimed at lowering the cost of making crucial capital-intensive investments—a principle not unique to shipping. Additionally, the Title XI program promotes the growth and modernization of the shipyard industrial base in the United States through the provision of United States government guarantees for loans made to ship-owners who build qualified vessels in United States shipyards for operation in the domestic or foreign trade of the United States. While once an attractive program, the liquidity of the capital markets available for ship financing in U.S. shipyards has not made the Title XI program a necessity for Jones Act construction. Since 2010, MARAD has approved only 18 vessels for Title XI financing, as compared with the hundreds of Jones Act vessels under construction each year. (<http://www.marad.dot.gov/ships-and-shipping/federal-ship-financing-title-xi-program-homepage/>).

Jones Act as the creation of an unholy alliance of self-interested lobbyists trying to protect a failing industry.<sup>14</sup>

Misunderstanding the Jones Act trade as part of international shipping, some critics claim that Jones Act vessels cannot compete globally. This argument misses the point altogether. The Jones Act trade is a domestic trade. It is not supposed to compete globally. U.S. railroads also do not compete globally, but that does not subject them to free trade criticism.

#### IV THE JONES ACT'S ROLE IN OUR NATIONAL SECURITY AND DEFENSE

There are three roles that the Jones Act plays in our national defense. The first is to keep our internal waterways and coastal regions in the hands of people that we can count on the most to be loyal to the United States: U.S. citizens. We worry much these days, and justifiably so, about cyber-attacks and the security of our national telecommunications and utility grids. Attacks on that infrastructure by hostile powers could cripple our economy and leave us vulnerable. The same concerns hold true with respect to our waterways, which are the lifeblood of national commerce. Consider the consequences if we were unable to move grain, fuel or other basic commodities on our waterways for just a few weeks. Rivers and seaways can be shut down with blockades, downed bridges, scuttled vessels or other mischief. Keeping our waterways and the vessels that ply them in the hands of our own citizens is a measure that enhances our ability to defend the homeland. For the same reason, we do not allow foreign airlines to fly domestic routes in the United States. There are good and obvious justifications for not permitting our domestic skies to be covered by foreign pilots and foreign owned aircraft. Those

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<sup>14</sup>Many critics focus on the perceived role of unions as pro-Jones Act lobbyists. Indeed, it is understandable that certain labor interests would want to preserve an American merchant marine. However, what critics do not mention is that the vast majority of shipbuilders and other shipping sector workers are *not* union members.

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reasons apply with equal force with respect to our internal waters, which should not be allowed to become, in essence, open borders, allowing a future (or current) enemy to exploit access to commercial and logistical arteries that we count on each day.

The second role that the Jones Act plays in our national defense is to provide a ready reserve of mariners capable of operating vessels. For security reasons, we may not wish to utilize foreign citizens to transport our troops or other military cargos. It is also possible that in a time of conflict we may not find foreign mariners who are willing to contract themselves to the United States military as part of our foreign operations. Can we always count on foreign merchant mariners to enlist when a military conflict arises? Relying too heavily on such an expectation is foolish. Indeed, as recently as the Iraq War many foreign crews refused to serve on vessels transporting our military cargos. The U.S. merchant marine stands as a ready reserve of mariners that have been trained and have “signed up” to serve the interests of the United States if called upon to do so. The Merchant Marine has been a crucial piece of our military might throughout the nation’s history. In fact, one in every 26 merchant mariners was killed in the Second World War, the highest ratio for any service branch.<sup>15</sup> The vast majority of the merchant mariners of the United States serve on its Jones Act qualified vessels. We would significantly dilute, if not lose entirely, this force of experienced and loyal American seafarers by allowing our domestic shipping to fall into foreign hands.

The third role of the Jones Act is that it ensures our ability to transport military cargos and personnel, both internationally and domestically. The Jones Act serves as a prudent “insurance policy” should we find ourselves in a world with foreign partners unwilling to cooperate with us in maritime matters. The insurance policy is twofold: first, it preserves our ability to call upon domestic vessels in a crisis; second, it guarantees a robust

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<sup>15</sup>Of course, in *absolute* terms losses for other branches (Marines, Army, etc.) were much larger. But the high casualty rate for merchant mariners illustrates how critical this often-overlooked aspect of the war effort actually was.

domestic shipbuilding capacity—a capacity that could prove critical in a world hostile to our interests.

The domestic vessel reliance side of the Jones Act insurance policy is crucial in a time of war. Today, we use U.S. flag vessels—most with registry not Jones Act endorsements—as well as foreign flag vessels, to move military cargos internationally. The Heritage Foundation piece mentioned earlier claims that the Jones Act has little relevance to national security because the Department of Defense has recently used foreign vessels for its foreign sealift capacity. This is true, but unrelated to the Jones Act. The Jones Act's purely domestic objectives are not intended to provide transportation for DOD's international missions. If DOD can transport military cargos to foreign locations on available, friendly foreign ships at a lower cost, then it should do so. If it cannot, the Jones Act ensures that these cargos can ultimately be moved. The fact that the average Jones Act Ship is not a vessel ready for military maneuvers is beside the point. Merchant ships are just as necessary in wartime as naval vessels.

When Jones Act proponents argue for the preservation of a domestic fleet, we are not contending that existing offshore support vessels and barges alone could shoulder the burden of a large-scale military engagement. Instead, it is vital that the U.S. maintain the *ability* to meet any such challenge, which brings us to the second piece of the insurance policy: shipbuilding capacity. Shipbuilding is not an industry that can be created overnight. It requires vast quantities of capital: physical infrastructure, financial viability, and human resources in the form of skilled workers. Lest anyone doubt the importance of shipbuilding capacity in wartime, consider the case of World War Two. Axis attacks in the Atlantic decimated the European Allies' ability to provision themselves. America's shipbuilding capacity became crucial to defeating the Axis powers. In order to keep the Allied cause afloat, American shipyards remarkably constructed 5,549 ships in 1,739 days. These were not uniformly naval vessels like destroyers and battleships; they were merchant marine vessels, essential to provisioning Britain and our own troops, and auxiliary boats needed to support the vast machinations of the U.S. war machine—the "Arsenal of Democracy." Whether it was harnessed for naval or merchant marine purposes, the fact remains that American shipbuilding

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capacity—a capacity that survives today because of the Jones Act—was crucial in the last World War and would be equally important should another ignite.

To summarize, the Jones Act advances national security by not allowing our internal waters to fall victim to a foreign enemy disguised as purveyor of shipping services. In addition, it gives our nation assurance that the United States will retain a native mariner population who can be counted on to operate ships in a time of crisis, and that the nation will retain the ability to construct ships on a massive scale, if needed. Opponents of the Jones Act must first answer this question: Which nation would the United States turn to for seafaring capacity should it become necessary? China? Korea? A European state? We can only hope that these nations would comply—but, as Vince Lombardi observed, hope is not a strategy.

## V

### WHAT DOES THE JONES ACT COST US?

With the history, purpose and benefits of the Jones Act now properly understood, let us turn to its costs, both real and alleged. A frequent criticism leveled against the Jones Act is that Jones Act charter rates are higher than the charter rates charged by foreign vessels, and that this harms domestic consumers. While this argument has appeal on first glance, the contention does not stand up to scrutiny. The cost of transporting petroleum products is a good place to begin, since petroleum products account for the lion's share, nearly 35 percent, of all Jones Act cargos. If a bonanza to U.S. consumers is to be found in repealing the Jones Act, petroleum cargos are a good place to look.

The first question we need to ask is what portion of the price paid by a consumer consists of transporting the petroleum product through the distribution chain? Over the last decade, an average of 9.7 percent of the cost of a gallon of gasoline is attributable to both

distribution and marketing.<sup>16</sup> Thus, the theoretical cost savings to be derived from using a foreign flag vessel to transport that gallon of gasoline through all of its iterations from crude oil to final product, will live within that 9.7 percent. The impact on the ultimate price, while not *de minimis*, is never greater than 9.7 percent in any conceivable case. It is important to remember that this percentage is *not* a “Jones Act surcharge” billed to consumers. It is a necessary component comprised of the myriad costs facing an industry charged with shipping, distributing, marketing, and selling petroleum products. The main driver of gas prices remains, as ever, the price of crude oil; fluctuations in this price have an impact on consumers that dwarfs any costs imposed by the Jones Act.

Now let us chase that 9.7 percent further and explore, hypothetically, what the impact of repealing the Jones Act would be on the ultimate shipping cost. To explore this question, we need to understand a few basics about shipping economics. On average, crewing and insurance costs make up about 80 percent of a vessel’s daily operating costs. Cost savings must be generated within those categories to be meaningful to shipping prices. Second, fixed costs in the shipping industry are comprised mostly of vessel repair and maintenance. Vessel repair and maintenance are usually performed in close proximity to the vessel’s location to minimize out-of-service time. Third, the impact of vessel construction costs, while important, is diffused by depreciation (a vessel’s useful life is usually between twenty and thirty years). Finally, while tax rates for vessels that operate internationally are usually very low—close to zero—vessels that operate in U.S. domestic service pay U.S. tax rates. Indeed, the tax regime governing the shipping industry in the U.S. is one of the least business-friendly in the world.<sup>17</sup>

Given these factors, would repealing the Jones Act eke out additional savings to the U.S. consumer? Those of us who are concerned about uncompetitive U.S. tax rates, over-regulation and

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<sup>16</sup>Source: [http://www.eia.gov/petroleum/gasdiesel/gaspump\\_hist.cfm](http://www.eia.gov/petroleum/gasdiesel/gaspump_hist.cfm).

<sup>17</sup>Source: [http://www.pwc.com/en\\_GX/gx/transportation-logistics/publications/assets/pwc-choosing-your-course.pdf](http://www.pwc.com/en_GX/gx/transportation-logistics/publications/assets/pwc-choosing-your-course.pdf).

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nonsensical U.S. liability laws already know what the unfortunate answer is. If the Jones Act were repealed tomorrow and foreign flag vessels were allowed to participate in the domestic economy, would the Coast Guard, Environmental Protection Agency, Occupational Safety and Health Administration, Department of Labor and others fail to regulate these vessels and their workers? Would these vessels be exempt from U.S. labor requirements? Would U.S. courts turn away their injured or aggrieved workers, and choose not to apply our domestic liability laws? Would the IRS exempt them from the requirements of the tax code? Would the U.S. Coast Guard pretend they are not here? In short, there is no evidence to suggest that the burdensome regulations placed on domestic shipping would not fall just as heavily on foreign vessels were they introduced to the domestic market. Foreign flag vessels look cheaper when the international charter rate—unaffected by U.S. wage and regulatory burdens—is compared to Jones Act vessels' charter rate. But these savings will lose their luster once foreign ships incur the operating costs, tax costs, regulatory costs, liability costs and repair costs already borne by their Jones Act-qualified competitors. The cost of operating in the United States is simply far higher than operating internationally. It is not the Jones Act that is driving the cost differential between a Jones Act-qualified vessel and a foreign flag vessel. The real enemy is the high cost of doing business in the United States, which Jones Act vessels contend with every day. Those who pitch the notion that a repeal of the Jones Act will drive down U.S. domestic shipping costs are selling wooden nickels. There is little evidence to indicate that once domesticated in the United States, foreign ships would drive down transportation costs at all. Our cost-savings exercise will have little, if any, impact on the 9.7 percent of petroleum costs we sought to reduce.

Puerto Rico, Hawaii and Alaska—the non-contiguous Jones Act trades—have a relationship with the Jones Act that differs from the continental United States and so the economic and policy concerns are a little different. These regions depend upon Jones Act-qualified vessels to bring cargos that originate from or are destined to the United States. They would like to use cheaper foreign vessels to bring their cargos and blame the Jones Act for their higher domestic prices. Of course, everything imported into

Hawaii, Alaska and Puerto Rico does not originate in the United States. Just like the continental states, the non-contiguous zones import from all over the world, and therefore the Jones Act has nothing to do with the prices of many, if not most, of those goods. And, as we saw with respect to petroleum transportation (petroleum products comprise the largest share of Hawaii's imports), only a small part of the cost can be attributed to shipping, even if coming from the United States. While citizens in Puerto Rico, Hawaii and Alaska have every right to be unhappy with higher prices, they live in relatively remote areas. The logistics and associated costs with getting things to remote places are always more burdensome. We cannot lay the blame for this solely at the feet of the Jones Act.<sup>18</sup> Jones Act critics, however, seem willing to blame the legislation for all public policy problems in the non-contiguous zones—even Puerto Rico's \$50 billion debt.<sup>19</sup>

But more fundamentally, the remoteness of the non-contiguous zones means greater vulnerability. Hawaii's proximity to Asian powers has made it a target in the past, and Alaska is separated from Russia by a mere 55 miles. Were the world to take a serious turn for the worst, Hawaii and Alaska would be likely targets of foreign aggression and probably the first U.S. lands to require our seafaring support. These non-contiguous states could be attacked economically by having their shipping lanes cut off. It is often difficult to see past the short-term problems of the here and now. But it remains the case that shipping security and shipping certainty are probably most important to the citizens of our non-contiguous states. As ever, the Jones Act is the only means to achieve these goals.

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<sup>18</sup>Studies that report high Jones Act costs to non-contiguous zones often assume that these zones import goods *only* from the U.S. This is inaccurate, and implicates the Jones Act in costs that do not actually exist. If Hawaii, for instance, needs to import foreign petroleum to save money, the Jones Act is not stopping them.

<sup>19</sup>How the Jones Act could result in a gap between government revenues and outlays of this magnitude is unexplained. It seems the debt crisis in Puerto Rico is just the latest in a line of disasters that Jones Act critics are willing to use as opportunities to scapegoat the legislation.



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## VI TWO CASES: SALT SHIPMENTS AND OIL RECOVERY

Oftentimes, the Jones Act has become a scapegoat for problems it has not created. Let us take the road salt shortages during the unusually severe winter of 2013-2014 as an example. According to some, salt deliveries were interrupted because Jones Act vessels were unavailable. Further, it was noted, salt coming from South America is cheaper than salt from Louisiana because it can be shipped on foreign vessels. Calls for repeal of the Jones Act inevitably followed.

So let us take a closer look. The United States consumes about 33 million tons of de-icing rock salt during an average winter.<sup>20</sup> This is quite a bit of rock salt, so states and municipalities plan their salt purchases at least a year in advance. Understandably, this requires some guess work about weather, traffic patterns, population changes and the like. The logistics of moving salt from mines around the country to their ultimate users also requires significant planning. Because salt is corrosive, the ships, barges, trains and trucks that move it around the country are configured to handle corrosion and are contracted well in advance of the winter months.

The winter of 2013-2014 tested even the best-laid plans. States and municipalities were short, including New Jersey, which consumes about 150,000 tons of rock salt in an average year.<sup>21</sup> New Jersey complained that after having nearly depleted its salt reserves it was delayed in acquiring an additional 40,000 tons of salt from a Maine stockpile. The reason, they claimed, was that there were no Jones Act-qualified vessels available on short notice. And maybe there were not any vessels available on short

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<sup>20</sup>Source: Compass Minerals 2013 Annual Report on Form 10-K  
<http://www.phx.corporate-ir.net/phoenix.zhtml?c=148615&p=irol-SECText&TEXT=aHR0cDovL2FwaS50ZW5rd2l6YXJkLmNvbS9maWxpbnmcueG1sP2lwYWdlPTk0M TYwNDEmRfNFUT0wJlNFUT0wJlNRREVTQz1TRUNUSU9OX0VOVEISRSZzd WJzaWQ9NTc%3d>

<sup>21</sup>Source: id.

notice. But that unavailability was driven by the same dynamics that explain why I have a tough time finding a cab in New York on a Friday evening in the pouring rain. It is not that there are no cabs; it is simply that they are spoken for at a moment of high demand. This dilemma is the fault of poor planning or just bad luck; either way, it is unfair to blame the cab companies.

Interestingly, similar complaints were not heard from other states that presumably also experienced higher-than-usual salt demand. New Jersey's neighbors New York and Pennsylvania each consume, under ordinary conditions, 826,000 and 975,000 tons of rock salt, respectively; much more than New Jersey. Yet somehow they managed to procure additional salt using Jones Act vessels. Moreover, New Jersey's complaint was not that it could not get its planned 150,000 tons of salt. It did, and on time. In fact, all of the 33 million tons of salt that had to move on Jones Act vessels for the 2013-2014 winter was delivered as planned. But these 40,000 tons of salt, representing a little more than one tenth of one percent of all of the de-icing salt consumed in the United States in an average year, is reason enough—according to some—to repeal the Jones Act. That is a pretty tough standard to require of any law. I doubt that many laws would survive were such a strict standard uniformly applied.

There is another often overlooked aspect to the salt story. Some states, like Maryland, buy their salt from mines in Chile and Mexico as opposed to mines in Louisiana and the Midwest. The inferential leap made by critics is that the Jones Act makes it more affordable to ship this salt all the way from South America. But there might be another reason. Perhaps the cost of South American salt is cheaper than U.S.-produced salt because it is cheaper to operate a mine in Chile than the United States. Let us test that theory.

Compass Minerals International, Inc. is the largest producer of salt in the United States. While it has a couple of mines in Canada and the U.K., the vast majority of the 13 million tons of salt that it sold in 2013 came from mines located in Louisiana and the Midwest. According to Compass Minerals' financial disclosures,

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its 2013 salt sold, on average, for about \$49.15 per ton, excluding shipping costs.<sup>22</sup> With a quick search on Alibaba, I found Chilean de-icing salt available for export at a cost of about \$23 per ton, *excluding shipping costs*.<sup>23</sup> Is the Jones Act to blame for Compass' lost sales to Chilean salt producers? Of course not. Compass Minerals, which is an extremely reputable and well-run company, has to put up with high U.S. wage costs driven by the unions that control about a third of its U.S. workforce, environmental regulations affecting mining operations of almost any kind in the United States, high taxes and the many other impediments to competitiveness that American companies face on a daily basis. The Jones Act has nothing to do with why Maryland can absorb the shipping costs associated with a 7,000 mile journey into the cost of its salt. The salt was just cheaper to produce in Chile.

I focus here on the salt issue because it is a cautionary tale, one that should lead us to skepticism when we hear that the Jones Act is the cause of an economic distortion. There is usually much more to the story, as there was during the Gulf oil spill that dominated headlines in 2010. Letting no crisis go to waste, Jones Act critics—mostly from outside of the United States—took to the airwaves to complain that oil recovery efforts were being impeded because oil recovery vessels from the Netherlands were not being used by BP because of the Jones Act. But was this true? If so, it is an outrage. If not, it is equally outrageous that those responsible for dealing with the spill response would be required to pull their attention away in order to address a false complaint. It was Admiral Thad Allen, the National Incident Commander, who was called upon to finally set the record straight and explain that the Jones Act does not regulate the skimming of oil on the surface of the ocean:

In no case has the Federal On Scene Coordinator (FOSC) or the Unified Area Command (UAC) declined to request assistance or

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<sup>22</sup> Source: id.

<sup>23</sup> Link displays recent cost of Chilean de-icing rock salt: [http://www.alibaba.com/trade/search?fsb=y&IndexArea=product\\_en&CatId=&SearchText=chilean+de-icing+salt](http://www.alibaba.com/trade/search?fsb=y&IndexArea=product_en&CatId=&SearchText=chilean+de-icing+salt).

accept offers of assistance of foreign vessels that meet an operational need because the Jones Act was implicated. . . . To date, no waivers of the Jones Act (or similar federal laws) have been required because none of the foreign vessels currently operating as part of the BP Deepwater Horizon response has required such a waiver.<sup>24</sup>

## VII CONCLUSION

Reality belies the claim that the Jones Act has “fostered stagnation in the U.S. maritime shipping industry.” The industry supported by the Jones Act is a bright spot in our national economy. But more importantly, the Jones Act is fulfilling its statutory objectives. Investment in modern ships is occurring at a consistent and significant rate. Both new vessels and shipyard capacity are being maintained. Moreover, the U.S. merchant marine, consisting of the thousands of U.S. citizen personnel serving on Jones Act vessels, remains vibrant and available to fulfill our domestic requirements as well as to serve as an auxiliary force in a time of conflict.

If we were to play the tape forward, and look at the country several years post Jones Act repeal, what would we likely see? For one thing, we would have no U.S. vessel-owning companies. U.S. vessel owners “liberated” from the citizenship requirements of the Jones Act would do what their foreign brethren do. They would pay U.S. taxes on any U.S.-derived operations, but reincorporate in tax havens to avoid high U.S. corporate income tax rates on their worldwide income. We would lose U.S. citizen companies—companies that heretofore have invested heavily, created jobs, paid taxes and served the nation in times of need. Repeal would also mean the end of commercial shipbuilding in the United States. The 150 self-propelled Jones Act-qualified vessels on order in U.S. shipyards today would be the last ones ordered. The next order for a vessel would be for its construction

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<sup>24</sup>Source: Statement of the National Incident Command, July 17, 2010

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in a foreign yard, probably in China or Korea, which subsidize ship construction costs. That would spell the end of thousands of jobs.

Finally, and most concerning, the United States' status as a maritime nation would erode and, eventually, perish. Maritime activity would persist, but that activity would not be owned and dominated by American citizens. It would be foreign in character, culture and loyalty. For those very reasons, it could not be relied upon in a time of crisis. In the end, we would be inviting the very danger the Jones Act was instituted to prevent: the seizure of domestic waterways by foreign enemies, and the deterioration of our shipbuilding capacity. Repealing the Jones Act would jeopardize American jobs, American security, and America's maritime character. I hope that policy thinkers—and policy makers—will consider what is at stake when they debate this much-needed statute.