WRITTEN TESTIMONY OF
JOHN P. LOVE
VICE PRESIDENT
PASHA HAWAII TRANSPORT LINES, LLC

HEARING ON
"REBUILDING VESSELS UNDER THE JONES ACT"
BEFORE THE
COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE
SUBCOMMITTEE ON COAST GUARD AND MARITIME TRANSPORTATION
UNITED STATES HOUSE OF REPRESENTATIVES
JUNE 11, 2008

John P. Love
Pasha Hawaii Transport Lines, LLC
Three Stamford Landing
68 Southfield Avenue
Suite 210
Stamford, CT 06902
(203) 276-5002

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Mr. Chairman and Members of the Committee, my name is John P. Love. I am a Vice President of Pasha Hawaii Transport Lines, LLC ("PHTL"). I appreciate the opportunity to testify today before the Subcommittee on Coast Guard and Maritime Transportation.

PHTL is a U.S. flag carrier that operates the JEAN ANNE, a U.S. built vessel carrying roll-on/roll-off ("Ro/Ro") cargoes in the coastwise trade between the U.S. West Coast and the Hawaiian islands. The JEAN ANNE is a state of the art pure car and truck carrier delivered in 2005. She was built at VT Halter Marine Shipyard in Mississippi specifically for the Hawaiian trade. The JEAN ANNE meets all of the requirements of the Jones Act.

When PHTL decided to build the JEAN ANNE, we assumed that the Jones Act, including the Second Proviso, would be vigorously enforced and that all shipowners would be obligated to comply with the same rules. In other words, we assumed that all vessels competing with the JEAN ANNE would be built and rebuilt in the United States. Yet, the JEAN ANNE is now competing with at least two vessels that operate at substantial cost savings due to their having been rebuilt in Chinese shipyards.

PHTL, together with the Shipbuilders Council of America, are plaintiffs in litigation currently pending against the Coast Guard in the United States District

Court for the Eastern District of Virginia regarding the conversion of a 25-year old, subsidy-built, pure containership in a foreign shipyard to a containership/roll-on/roll-off vessel. We have been forced to engage in this litigation because we have been unable to obtain any redress from the National Vessel Documentation Center or Coast Guard Headquarters.

The Second Proviso of the Jones Act requires that U.S. flag vessels be rebuilt in the United States in order to retain domestic (coastwise) trading privileges. Notwithstanding the current flurry of litigation by our company and others, we do not believe that the Second Proviso is "broken." However, the process for implementing it is.

The root of the problem begins with the fact that the decision making process employed by the Coast Guard is a secret proceeding closed to the public. No one knows when an application for a preliminary or final rebuild determination is filed. Moreover, the Coast Guard employs an *ex parte* procedure requiring minimal or no information from the applicant. As we have discovered recently, a typical application consists of a lawyer's letter with a vague general description of the project and one or two crude renderings of the vessel's profile.

Although the Coast Guard's regulations mandate detailed information -- accurate sketches or blueprints -- the Coast Guard does not require such submittals. There is little or no investigation of an application for a rebuild determination. It is our view that the Coast Guard typically rubber stamps the rebuilding request within days. As recent litigation involving rebuild determinations has revealed, often the project that is completed is not the project that was briefly described to the Coast Guard.

The rebuilding decisions also are not made available to the public. Unlike other federal agencies that oversee similar requirements, the Coast Guard does not publish its determinations. Instead, the only way to obtain these rulings is to file a request under the Freedom of Information Act ("FOIA"). As a result, competitors often do not know that a favorable rebuilding determination has been made until the project is uncovered by the press and, by then, work may be well underway.

Even when the rebuilding determination is finally obtained, it is difficult to ascertain just exactly what it is the Coast Guard has approved. The ruling letters are cursory, often only one or two pages long. The Coast Guard refuses to release the application and related documentation, citing commercial confidentiality under the FOIA. However, the administrative records in the cases under litigation have revealed that there is nothing commercially sensitive about this information. We have even had problems obtaining complete administrative records as we believe the Coast Guard has attempted to hide documents adverse to its decision.

There is little possibility of redress once the true scope of a project is finally known. By the time a competitor finally learns about a rebuild determination, the thirty day period for appeal has expired. In fact, this happened to us. We filed an appeal with the Coast Guard upon learning about a ruling, only to be told we were too late. Even if an appeal is timely filed within 30 days of the secret issuance of the preliminary rebuild determination, it is decided by the division that made the decision to begin with, the National Vessel Documentation Center. The director of the National Vessel Documentation Center in an interview with *Fairplay* publicly compared the rebuild issues to the automobile industry, claiming there is confusion over exactly what a U.S. vehicle is, noting that BMWs, Toyotas and even Mercedes are now built in

the U.S. The drawing of such an analogy to justify decisions allowing substantial vessel rebuildings overseas demonstrates a fundamental misunderstanding of both the Jones Act requirements and the clear intent of Congress mandating that coastwise eligible vessels be rebuilt in U.S. shipyards. The Coast Guard's headquarters in Washington appears to have abdicated all oversight adding frustration to the process, and in our case, forcing us to seek redress in the U.S. federal Court. Importantly, we are not alone.

Faced with this flawed procedure, competitors have found that the only relief available is to file a complaint in federal court. Obviously, that is an expensive and burdensome undertaking. One United States District Court Judge has called the Coast Guard's process a "mess." This Court severely criticized the Coast Guard for not seeking input from those opposing as well as seeking rebuilding determinations.

Not only is the procedural process flawed, but the decision making process is flawed as well. While the rebuild determinations made since the regulations were issued in 1996 are inconsistent, there is one discernable trend. The Coast Guard's enforcement of the Second Proviso has gotten increasingly lenient or non-existent.

For example, a major amendment to the Second Proviso was in 1960 when Congress added the requirement that any major component added to a vessel be constructed in the United States. While this was in response to a case where a midbody was added to a vessel, the Coast Guard has ruled correctly that this prohibition is not limited to midbodies, but includes other major components such as bulbous bows, decks and deck houses -- indeed anything over 1.5% of a vessel's discounted lightship weight ("DLW").

In recent decisions, however, the Coast Guard has written the "major component" requirement out of the Second Proviso. The Coast Guard has argued that the installation of new second inner hull on a single hull tanker to comply with Oil Pollution Act ("OPA") is not the addition of a major component because the hull is constructed "piece-by-piece" and no single piece weighs more than 1.5% of the DLW. This approach was soundly rejected by the Court earlier this year in the case of the *Seabulk Trader*. In another case, one we are involved in, the Coast Guard, departing from its previous precedents, held that a 265.5 ton deck added in China is not a major component because the heaviest piece lifted by the Chinese shipyard's crane was equal to .22% of the vessel's DLW. In other words, enforcement of the Second Proviso now rests on the lifting capability of the foreign shipyard crane employed in the construction of the major component. The method of construction rather than what was added to the vessel is now the determining factor. If the Coast Guard's logic is carried to its logical extreme, a midbody may be added in a foreign shipyard as long as it is constructed piece by piece or as long as the heaviest crane lift is less than 1.5% of DLW. We do not believe that this is what Congress intended.

The Coast Guard's regulations also set forth a percentage test of how much steel work can be performed on a vessel before it is considered rebuilt. Simply put, steel work under 7.5% of DLW is not a rebuilding, steel work between 7.5% and 10% of DLW may be a rebuilding, and steel work over 10% is a rebuilding *per se*. Although of paramount importance to its determination, the Coast Guard does not verify what the applicant claims to be the DLW, even if this is challenged.

The Coast Guard's implementation of the percentage steelweight test also shows an increased willingness to sanction foreign rebuilding. For example, there is work in

removing steel as well as in adding steel to a vessel in a foreign shipyard. Yet inexplicably the Coast Guard does not count both. It has announced a policy to count only the greater of the added or removed steel. Quite frankly, this makes no sense, particularly when a vessel is being converted where steel removed is not replaced, as opposed to undergoing a simple repair where steel is removed is replaced.

The Coast Guard typically does not count "outfitting" when counting steel work. Outfitting has been defined historically as inventory, equipment, furnishing and stores. Yet recently the Coast Guard has expanded this term to include "nonstructural" steel work -- although this distinction was rejected by another United States District Court Judge almost twenty years ago. The Coast Guard recently carried this newest approach to the ultimate extreme by classifying newly constructed Chinese auto decks as "outfitting." The Coast Guard does not investigate or question when applicants have abruptly reclassified "structural work" as "nonstructural" or "outfitting" to get below the 7.5% threshold.

The 7.5% test was meant to be the threshold when the regulations were adopted in 1996. The 7.5% to 10% range was to allow the Coast Guard some latitude if the foreign shipyard work did not change the dimension, structure or type of the vessel. In other words, the 7.5% to 10% range was intended to accommodate repair work, not major conversion work.

A review of the Coast Guard rulings since 1996 reveals that the Coast Guard has never found work in the 7.5% to 10% range to be a rebuilding. The real test is now 10% of DLW. This too has been properly criticized by the Court in the *Seabulk* case who has said if the Coast Guard wants to move the 7.5% threshold to 10% it should do so through notice and comment rulemaking.

The *de facto* 10% test, the piece by piece crane lifting approach, failure to count both added and removed steel, the characterization of steel work as "outfitting" or "nonstructural," and lax enforcement, have not surprisingly led to significant foreign rebuild projects, primarily in Chinese shipyards. A clear example of this is shown in the attached photographs. The first picture is a pure container ship "gutted" in China so that auto and heavy vehicle decks may be added to the vessel. The second picture shows this vessel after six levels of decks have been added in China comprising more than 100 days work. The Coast Guard ruled that this was not a rebuilding and this matter is now before the court. This case demonstrates the severe and unlawful competitive disadvantages to companies such as PHTL who played by the rules. Cases such as this have also had significant negative effects on our U.S. shipyards.

As recently held by a federal court, preliminary rebuild determinations convey no legal rights -- a position advocated by the Coast Guard in court. Rebuild applicants have been aware for years of the increasingly lax enforcement at the Coast Guard. They have asked for rebuild rulings that they know would never be approved by an agency dedicated to enforcing the Second Proviso. Applicants who have obtained these *ex parte* rulings without providing meaningful information to the Coast Guard and who "pushed the envelope" took a calculated risk that it would be "business as usual." Now that the Courts are responding, these companies should not be bailed out by Congress. These companies knew what they were doing in the foreign shipyards just as we knew the law when we decided to make significant investments in the domestic maritime trade. The Second Proviso would become meaningless if a company can knowingly rebuild its vessel in a Chinese shipyard and then be bailed out by Congress whenever a federal district court judge blows the whistle.

The problems at the Coast Guard National Vessel Documentation Center are having a ripple effect. Although we disagree with this approach, the Maritime Administration is following the Coast Guard in determining what constitutes a foreign rebuilding for purposes of the Capital Construction Fund. This has resulted in sizable tax benefits for vessels rebuilt overseas in China. In addition, while some of these projects are clearly major conversions requiring environmental and safety upgrades, the Marine Safety Center also appears to be following the lead of the National Vessel Documentation Center and by doing so may be creating issues concerning U.S. compliance with international treaties. All of this adds up to putting us at a significant competitive disadvantage because we chose to play by the rules.

Despite our criticism of the Coast Guard, we believe that the process can be fixed. We ask that Congress take steps to encourage the Coast Guard to enforce the Second Proviso by:

- making the rebuild application process completely transparent
- requiring the applicant to submit sufficiently detailed information in support of its application
- allowing input from all interested parties
- thoroughly investigating each application
- publishing rebuild determinations online or making them readily available by facsimile
- enforcing the prohibition against the addition of major components
- counting added and removed steel in applying the percentage total
- counting all steelwork -- structural and nonstructural
- maintaining the 7.5% threshold, particularly in cases where the work is not limited to repairs

- providing a meaningful appeal process to headquarters in Washington, D.C.

Thank you again for the opportunity to testify today and I am happy to answer any questions you may have.