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**Shipbuilders Council of America**

**BEFORE THE**

**UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE
SUBCOMMITTEE ON COAST GUARD AND MARITIME TRANSPORTATION**

**On**

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***Rebuilding Vessels Under the Jones Act***

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**Testimony of**

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Thank you Chairman Cummings and members of the Subcommittee on Coast Guard and Maritime Transportation, for the opportunity for the Shipbuilders Council of America to testify at this important hearing regarding the Rebuilding of Vessels Under the Jones Act. I am Matthew Paxton, President of the Shipbuilders Council of America, the largest national trade association representing the U.S. shipyard industry. The SCA represents 31 companies that own and operate over 100 shipyards that are located along the eastern seaboard, the Gulf coast, Great Lakes, west coast and Hawaii. SCA's member build, repair and maintain America's fleet of commercial vessels. These shipyards also constitute the shipyard industrial base that services and repairs Navy combatant ships and builds small and midsized vessels for the U.S. Coast Guard, U.S. Navy and other government agencies.

A core value of the SCA is to promote and protect the Jones Act, which requires vessels that operate in the domestic (coastwise) trade be built in the U.S. and owned and crewed by U.S. citizens. The policy for this nearly 200 year old law is extremely clear – it is in the best interest of our nation to maintain a merchant marine that is sufficient to carry its domestic water-borne commerce and also capable of serving as a naval and military auxiliary in time of war or national emergency, which is owned and operated under the United States flag by citizens of the United States and supplemented by efficient facilities for shipbuilding and ship repair.[1]

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[1] Merchant Marine Act, 1936 (46 App. U.S.C. 1101).

From the shipyard perspective, the Jones Act ensures that the U.S. maintains critical shipyard infrastructure and a skilled workforce that can build and repair the domestic "Jones Act" fleet that consists of over 38,000 vessels. These vessels were built in U.S. shipyards and represent an aggregate $48 billion investment. Over the last decade, however, the U.S. ship repair industry has experienced a substantial decline in the amount of maintenance and rebuilding work on the Jones Act fleet. Increasingly more Jones Act vessels are going overseas (primarily China) to perform major rebuild work – work that previously sustained the U.S. ship repair industry. The result has been a significant downsizing of major ship repair facilities, closure of shipyards, and the outsourcing of skilled labor needed to maintain the domestic fleet.

This is not the first time that U.S. shipyards have been faced with the loss of work on Jones Act vessels. In 1956, the Congress introduced a bill to add the "Second Proviso" to the Jones Act. The Second Proviso clarified that rebuilding of Jones Act vessels is prohibited in foreign shipyards. The legislative history on the purpose of the Second Proviso was, "to assist the shipyards of the United States by making applicable to vessels rebuilt in foreign yards the historic policy of exclusion from the coastwise trades which has always been applied with certain exceptions to vessels constructed outside the United States."[2] Indeed, this committee in 1956 provided in its House Report accompanying the passage of the Second Proviso bill that –

[2] S. Rep. No. 2395, 84th Cong. (2d Sess. 1956) at 1.

> "With major developments in technology in recent years there have been instances of American-owned, American-built vessels which have been substantially rebuilt in foreign shipyards, and then have returned to operate in American coastwise trade. Even though these rebuildings have been so extensive as to completely change the character of the vessels. . . [t]his appears to be a gap in the law, which is clearly inconsistent with traditional policy. This bill is designed to close the gap and deny the right of vessels rebuilt abroad to operate thereafter in the domestic trade."[3]

Unfortunately, this "gap" has appeared again not in the law – the Second Proviso is plain in its reading and intended application – but in the regulations implementing the Second Proviso. The law under the Second Proviso states:

> No vessel which has acquired the lawful right to engage in the coastwise trade, by virtue of having been built in, or documented under the laws of the United States, and which has later been rebuilt, shall have the right thereafter to engage in coastwise trade, unless the entire rebuilding, including the construction of any major components of the hull or superstructure of the vessel, is effected within the United States.[4]

Interpreting this provision of the Jones Act, the Coast Guard issued regulations in 1996 to determine when a vessel is rebuilt foreign and provided two tests:

> (1) a vessel is deemed rebuilt when a major component of the hull or superstructure not built in the U.S. is added to the vessel; and
> (2) a vessel is deemed rebuilt when worked performed on its hull or superstructure constitutes more than 10 percent of the vessel's steelweight; work below 10 percent to 7.5 percent is within the Coast Guard's discretion; and work done below 7.5 percent will not be deemed a rebuild.[5]

The "gap in the law, which is clearly inconsistent with traditional policy," that exists today is the inconsistent application and enforcement of these regulations by the Coast Guard to determine a foreign rebuild. The Coast Guard has simply not enforced

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[3] *See e.g.*, H.R. Rep. No. 2293, 84th Cong. (2d Sess. 1956) at 2.
[4] 46 U.S.C. § 883.
[5] 46 C.F.R. § 67.177.

the "major component test", the first test noted earlier. The Agency has articulated that it is "long-established practice of the Coast Guard, [that] only components added to the vessel which amount to 1.5 percent or more of the vessel's steelweight, prior to the addition, are considered major components."[6] However, when presented with a situation that a component, such as the addition of an inner-hull or a deck, the Coast Guard ignores the major component test and proceeds instead to the steel work calculation test (the second test noted above). By ignoring the major component test, the Coast Guard can allow for much bigger rebuild jobs to be done overseas, which of course is prohibited under the Second Proviso.

In addition, the Coast Guard has never exercised its discretion to determine that a vessel has been rebuilt when foreign work projects involve between 7.5 percent and 10 percent of a vessel's steelweight. Instead, with no analysis the Coast Guard has simply implemented a de facto 10 percent steel work threshold test to determine whether a vessel that has been rebuilt in a foreign shipyard. Since the regulations went in place in 1996, there has not been a single instance of the Coast Guard utilizing its discretion to prohibit a foreign rebuild project. Now, couple this with the fact that Coast Guard ignores the major component test, the clear indication from the Agency is it seeks ways to allow Jones Act vessels to be rebuilt in foreign shipyards in contravention of the intent and purpose of the Second Proviso.

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[6] Coast Guard Final Rebuild Determination, M/V Mokihana, Oct. 23, 2007.

Further complicating the Coast Guard's regulations is the fact that the standards or tests for what counts in a foreign rebuild project is constantly changing. Under its 1996 regulations, the Coast Guard once counted the total of steel added and steel removed from a vessel. When rebuild jobs became increasingly larger, the standard put forth by the Coast Guard was to count the greater of either the steel removed or added in calculating the 10 percent threshold.

The Coast Guard's most recent determinations are simply baffling and show the extremes to which the Agency will go to permit extensive foreign rebuild work on Jones Act vessels. For instance, the Agency determined that adding an entire inner hull to a single hull vessel is not considered a rebuild or an addition of a major component because, "the work is intrinsic to the hull itself," and thus the Coast Guard "declined to characterize it as a separable component that will be added to the vessel similar, for example, to a bulbous bow or additional decks added to the superstructure." The addition of an entire inner hull is not a rebuilding under the clear language of the Second Proviso? This logic has effectively nullified an Act of Congress.

In a subsequent ruling which involved the addition of several decks to the superstructure of a Jones Act vessel in China, the Coast Guard disregarded its previous analysis that decks are considered separable components and instead applied a new test that looked at whether or not any crane in the Chinese shipyard could lift a single major component weighing at least 1.5 percent of the steelweight of the vessel. Upon determining that the Chinese shipyard did not have cranes that could lift one single

component weighing 1.5 percent of the vessel's total steelweight, the Coast Guard determined no major component was added and a rebuild could not possibly have taken place. The recommendation for foreign shipyards: invest in smaller cranes!

Pursuant to this latest "crane lift" analysis by the Coast Guard, a vessel can be rebuilt one crane lift at a time as long as no single lift is greater than 1.5 percent of the vessel's total steelweight. This twisting of the Coast Guard regulations effectively eliminates the prohibition in the Second Proviso against adding a major component to a Jones Act ship in a foreign shipyard.

The inconsistent application and changing tests and standards applied by the Coast Guard to allow larger rebuild and conversion jobs to go overseas has resulted in confusion and uncertainty not just for U.S. shipyards but across the U.S. maritime industry. Jones Act operators no longer have faith in what the true capital construction costs are to operate in the domestic trade. Is it building a new vessel in a U.S. shipyard or rebuilding your Jones Act vessel in a Chinese shipyard?

The Shipbuilders Council of America supports the Jones Act and the consistent application of the Second Proviso. I would recommend that this committee consider legislation to clarify the Coast Guard regulations to provide a transparent and predictable process so everyone in the maritime industry understands the standards for rebuilding Jones Act vessels. This clarification should take a common sense approach to the identification of "components" of the hull and superstructure. A component should be

looked at in its entirety, as Congress intended, when applying the Coast Guard's existing "major component" test, irrespective of its manner of installation. The U.S. District Court for the Eastern District of Virginia recently addressed this issue. Judge Brinkema noted in her decision to remand and revoke the coastwise endorsement for a Jones Act vessel rebuilt in China that –

> "...However, the manner in which the component is added to the vessel-piece-by-piece or wholesale—is irrelevant to whether the component is "major" ...Although a deck or a component of the hull can be added to a vessel as one discrete pre-constructed structure, it surely can be added piece-by-piece, beam-by-beam, and rivet-by-rivet. Shipowners could easily frustrate the entire operation of the Second Proviso simply by dictating the manner of installation"[7].

The Shipbuilders Council of America agrees with this assessment and believes the Second Proviso has effectively been written out of the Jones Act.

Thank you again for inviting the Shipbuilders Council of America to testify on this important issue for the Jones Act.

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[7] *Shipbuilders Council of America, Inc. et al., v. U.S. Department of Homeland Security et al.,* Civil Action No. 1:07cv665 at 15-16.