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The Jones Act Revisited

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THE JONES ACT IS COSTLY TO CONSUMERS, AND

it is an obstacle to a speedy response to domestic disasters such as hurricanes Harvey, Irma, and Maria. It makes negligible contributions to foreign operations of the US military. Despite its high costs relative to benefits, the Jones Act has survived for nearly a century and retains strong support from elected leaders of both parties today.

The benefits of the act are concentrated among special interest groups, but the costs are broadly dispersed. Total costs are large, but costs per consumer are low. Consumers (voters) have only a weak incentive to mobilize against the act, even though it is wasteful for the general population. I explain these and other points in “An Economic Analysis of the Jones Act” (EA), published online by the Mercatus Center at George Mason University in May 2017.¹ The EA has been criticized in a position paper by the American Maritime Partnership (AMP), the main supporter of the Jones Act.² The purpose of this brief is to bring the EA up to date and respond to some points raised by the AMP position paper.

CRITICISM FROM THE AMERICAN MARITIME PARTNERSHIP

The AMP represents the shipyards, carriers, and labor unions that receive the concentrated benefits from reducing competition in waterborne transportation. Their members are aware that they gain from the Jones Act, and they have been very effective at persuading elected and appointed officials to support their cause. They have produced a document on their website, written by an anonymous author, that is mostly critical of my paper.³ Not surprisingly, the document disagrees with my main conclusions,

but it also produces a list of specific objections that will be evaluated.⁴

These objections include a claim that the arguments are one-sided and that costs of foreign-flag ships would be higher if they operated in the US market. The AMP paper asserts that arguments put forth by supporters of the Jones Act are ignored. The paper also makes a claim about job creation flowing from the Jones Act and attempts to defend the costs imposed by the act during national disasters as justifiable. I discuss each of these objections in turn.

ARE THE ARGUMENTS AGAINST THE JONES ACT ONE-SIDED?

The AMP accuses the EA of being one-sided because it does not take into account arguments made by Jones Act supporters. On the contrary, every one of the arguments raised by Jones Act supporters is evaluated and rejected. For example, they make two claims about costs. One is that the costs of Jones Act ships cannot be compared directly with costs of foreign-flag ships because the latter might incur higher costs if they were operating in the US market. For example, foreign crews might become subject to the US minimum wage and other US labor laws if they operate within the US. This point has been made by the Government Accounting Office and others, and it is discussed explicitly in the EA.⁵ This problem may have influenced the US International Trade Commission to cease issuing quantitative estimates of the costs of the Jones Act. A direct comparison is not possible because foreign-flag ships have not been allowed to operate in the US domestic market since 1920. The AMP emphasizes the difficulty of obtaining accurate estimates of certain costs of the Jones Act. However, its paper is conspicuously silent on the even more difficult problem of obtaining accurate and objective estimates of the benefits to national security from the Jones Act.

This measurement problem has some legitimacy for operating costs, but it has no relevance to the cost of acquiring new American-built versus foreign-built

ships. Costs of acquiring new ships can be compared directly, and American-built ships cost much more. The exact cost difference varies with the type of ship, but some American-built ships are five times as expensive as their foreign counterparts.

A second point about costs was made by Eric Smith, a former vice president of the AMP, when he claimed that costs of Jones Act ships were not higher than those of foreign-flag ships. According to Smith, “the Jones Act doesn’t cost the consumer a single penny.”⁶

In fact, higher costs of ships are passed on to consumers in the same way that gasoline taxes are passed on to buyers of gasoline. The cost difference is the main reason American businesses that export products hire almost entirely foreign-flag ships. Some of the same shipping companies that service Puerto Rico with American-flag ships also service foreign islands in the Caribbean with lower-cost foreign-flag ships.

AMP spokespeople regularly say they have sufficient capacity to satisfy the Puerto Rican market without the participation of foreign-flag ships. What they leave out is that the absence of competition from foreign ships has allowed some Jones Act companies to conspire on prices and charge markups that violate the Sherman Antitrust Act.⁷ Puerto Rican buyers who pay the higher prices do not feel satisfied.

ARE THE SUPPORTERS OF THE JONES ACT IGNORED?

The AMP claims that my paper ignores supporters of the Jones Act. On the contrary, the EA acknowledges the strong political support for the Jones Act from Congress and from both Democratic and Republican administrations. For example, Congressman Duncan Hunter from California has been a strong and outspoken advocate for the Jones Act. Representative Hunter’s district includes NASSCO, a division of General Dynamics, the largest US shipyard employer. He has accused Jones Act critics of “dubious claims of higher costs.”⁸

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Representative Hunter has not produced alternative cost estimates, but there is a more fundamental problem for him and his allies: why do American shipyards need protection from foreign competition if their costs are not higher?

Representative Hunter has received consistent financial support from the industry, and he recently demonstrated his commitment to his campaign supporters by holding a hearing for the House Transportation and Infrastructure Subcommittee on Coast Guard and Maritime Transportation, which he chairs. Every witness he chose to testify was a firm Jones Act supporter.⁹

In fact, political support for the Jones Act has been so strong that a Jones Act opponent, Senator John McCain, said that he could not find 20 votes in the Senate in opposition to the Jones Act. In international trade negotiations, both Democratic and Republican administrations have consistently excluded the Jones Act from negotiations about trade liberalization. US representatives in World Trade Organization negotiations considered the Jones Act to be “the most sacrosanct of the sacred cows.”¹⁰

DOES THE JONES ACT CREATE JOBS?

The AMP cites large numbers of jobs created by the Jones Act as a benefit of the act, but these numbers do not tell the whole story. The number of oceangoing ships (vessels at least 400 feet in overall length) produced in the US has steadily declined, from 45 per year in 1953 to 5 per year in 2015.¹¹ If the number of workers employed has not declined correspondingly, this implies that more workers are being employed per ship, which in turn implies low worker productivity

and higher costs per ship produced. Low productivity may be one reason new American-built ships cost five times as much as foreign ships. Consequently, nearly the only buyers of American-built ships today are those who are legally obliged to buy them. The high cost of American-built ships makes them uncompetitive on the world market, and it is a main reason why ship-building has moved to Asia.

Increasingly complex supply chains make the calculation of job creation more difficult. American shipyards are using an increasing percentage of foreign components, from ship design to engines to electronics. Thus, some of the jobs created by the Jones Act are overseas. All three American shipyards that produce oceangoing commercial ships have close relations with foreign shipyards. NASSCO partners with South Korean shipbuilding power Daewoo Shipbuilding and Marine Engineering. Philly Shipyard is a subsidiary of Norwegian Aker, ASA, whose shares are traded on the Oslo exchange. VT Halter is owned by ST Engineering, whose major shareholder is the government of Singapore. Offshore outsourcing of ship components creates foreign jobs, which is not the outcome intended by the Jones Act or most of its supporters. Outsourcing is used extensively for new ships and increasingly for servicing and refitting of old ships. The American shippers Matson and Pasha recently sent ships all the way to China for refitting, even though they had to pay a 50 percent US tariff for importing the services.¹² Even though Jones Act ships must be American built, regulatory authorities are now acknowledging the increasing use of foreign sourcing by referring to the ships as “American assembled.”

DOES THE JONES ACT INCREASE NATIONAL SECURITY?

Defenders of the Jones Act claim that the higher costs it imposes are justified because the act contributes to national security. However, when national security requires a quick and effective response to domestic disasters, such as hurricanes Harvey, Irma, and Maria in 2017, the Jones Act serves as an obstacle to recovery. The Jones Act prohibits the use of foreign ships for domestic transport, so by prohibiting a potentially useful transportation option, it is obvious that the act could slow disaster relief. Authors of the act acknowledged this potential shortcoming by allowing for waivers during national disasters that are declared by the president and the cabinet.

However, a waiver is not automatic, and the request for a waiver necessarily results in delay as the request moves through the bureaucracy. It must be submitted to Customs and Border Protection, and that agency must consult the US Maritime Administration (MARAD) to determine whether American-flag ships can provide the requested transportation. The AMP and its allies have frequently opposed waivers, which can result in a political delay. Waivers were granted in 2005 and 2012, but not in 2010 following the BP Horizon oil spill. In the BP case, foreign ships were eventually permitted to participate in skimming oil from the polluted water, but it took more than a month for the administration to determine that skimming oil was not prohibited by the Jones Act. Retired Admiral Thad Allen, who headed the BP Horizon cleanup effort, claimed the Jones Act did not hinder the cleanup, but the time lag between the offer of services of foreign ships and their actual participation is undeniable.

The same issue arose after Hurricane Harvey, as the government evaluated the request for a waiver submitted by Phillips 66 Oil. As Hurricane Irma approached the coastal United States, the government acted more quickly by issuing a seven-day waiver on September 5 that was later extended for two more weeks. A waiver was also issued for the damage done by to Florida by Hurricane Harvey. However, when

Hurricane Maria devastated Puerto Rico, the administration first denied a waiver. It later reversed the initial denial and issued a 10-day waiver. The delay and uncertainty about the waiver occurred while some people desperately sought electricity and fuel. The waiver process could be made quicker and more predictable if a waiver automatically took effect at the time the president or the president's agent declared a national disaster and if it lasted for the duration of the emergency.

The recent damage from Hurricane Maria has called attention to the adverse effects of the Jones Act on disaster relief in Puerto Rico. Even before Hurricane Maria, Puerto Rico suffered from long-term adverse effects of the Jones Act. Puerto Rico has higher costs of electricity than any of the mainland states. Prices of many other products are inflated because the Jones Act limits competition from foreign-flag ships.

After Hurricane Maria hit Puerto Rico, President Trump first hesitated to issue a Jones Act waiver. Following a request from the governor of Puerto Rico, Mr. Trump issued a 10-day waiver, but it was not long enough to allow ships to respond to the crisis. A Norwegian-flag ship that was docked in New Orleans offered to take supplies to Puerto Rico, but the waiver expired before it could complete its voyage.¹³ Similarly, Greenpeace representatives discovered that their Dutch-flag ship was not allowed to carry supplies from New York City and unload them in San Juan.

Many people in Congress, including Senator John McCain, Senator Mike Lee, and Representative Nydia Suarez, have called for a waiver or a permanent exemption from the Jones Act for Puerto Rico. Following a study of the Puerto Rican economy, the Federal Reserve Bank of New York called for a five-year waiver of the Jones Act for Puerto Rico. The Jones Act is an obstacle to providing quick relief from a domestic disaster.

IS THE JONES ACT RELEVANT TO TRADE WITH GUAM?

The AMP makes some quibbles, including denouncing the EA for claiming that Guam is harmed by the Jones Act. There is a so-called Guam exemption that makes it possible for US-flagged ships to avoid the US-built and US-owned requirements for trade between Guam and the US mainland. However, Michael Hansen has pointed out that Guam is de facto constrained by these requirements:

Although Guam is de jure exempt from the U.S. build requirement of the Jones Act and other such U.S. cabotage laws, it's functionally shackled to the domestic build requirement de facto. This [is] because the natural trade lane from the U.S. West Coast to Guam passes through Hawaii, which is subject to the U.S. build requirement, and shipping lines must call at both Hawaii and Guam to mount a financially successful voyage.¹⁴

Therefore, Guam is harmed by the Jones Act de facto, and that is why Guam's legislature voted in favor of a measure to exempt Hawaii from the Jones Act.

ADAM SMITH AND ABUSE OF THE NATIONAL DEFENSE ARGUMENT

The AMP document claims Adam Smith as a supporter of the Jones Act of 1920, because he made a national defense argument for the British Navigation Acts in the 1700s. The relevance of this point to modern transportation is a bit of a stretch, since there were no airplanes, railroads, trucks, or modern pipelines to substitute for ships in the 1700s. Furthermore, the British were wise enough to repeal the Navigation Acts in 1848.¹⁵

Because of the Jones Act, shipping today is regulated more stringently than any other mode of transportation. On domestic water routes, American businesses are not allowed to use foreign-built ships today.

However, American commercial airlines are permitted to use foreign-built aircraft on domestic flights, and they often do. European Airbus, Canadian Bombardier, and Brazilian Embraer are commonly used, and they provide effective competition for American aircraft builders. Surely the US Air Force is important for national defense, but the Air Force does not seem weakened by the absence of a "Buy American" requirement for US commercial airlines. Similarly, truckers and railroads are permitted to buy the best equipment available, whether it is foreign or domestic made. Claiming that the use of American-built ships for commercial water transportation is essential for national defense is an extreme abuse of the national defense argument put forth by Smith. Since national defense benefits the entire country, it is logical to finance it with a broadly based tax rather than imposing a cost burden on the shipping industry.

THE JONES ACT MOVES TRANSPORTATION FROM WATER TO LAND

Jones Act defenders claim that it contributes to national security by strengthening the US merchant marine. However, an unintended side effect is that by making domestic water transport more expensive, the Act has moved transportation from water to land. This point has been documented by Rockford Weitz and his colleagues at the Fletcher Maritime Studies Program at Tufts University.¹⁶

They point out that water transport in the United States is far less important (2 percent of total transport) relative to transportation of all modes than is water transport in the European Union (40 percent of total transport), and they cite the Jones Act as a contributing factor. Substitution of land transport for water transport has even been accused of causing traffic jams on land.¹⁷

THE JONES ACT AND SHIP SAFETY

Proponents have argued that the Jones Act would contribute to a strong merchant marine and a strong

navy. However, there is increasing concern that the Jones Act may have the unintended consequence of making the American merchant marine *less* safe. A tragic example of the possible safety issue is the sinking of the *El Faro* in 2015 that killed the entire crew. The *El Faro* was a 40-year-old Jones Act–eligible ship, and the extremely high cost of new American-built ships has contributed to the older age of the American-flag fleet. Higher costs have led owners to delay purchases of expensive new ships in favor of extending the lives of older ships. On October 1, 2017, the Coast Guard issued its report on the causes of the *El Faro* sinking, and it criticized the ship’s vulnerable design (possibly owing to its age), its failure to use the latest information about the hurricane, and its use of open life boats.¹⁸

The National Transportation Safety Board has announced that it will issue its report on the *El Faro* sinking in December of this year. If accumulating evidence indicates that the Jones Act is contributing to less safety, this information may weaken political support for the Jones Act.¹⁹ Will elected officials continue to support laws if evidence indicates that they compromise the safety of crews? Will union officials change their minds if the act is found to endanger the lives of seamen they purport to represent?

CORRECTIONS IN THE EA

Some minor errors in the EA were not noticed by the anonymous author of the AMP document. For example, contrary to the EA, ferry service is not in place among the Hawaiian Islands. Also, the percentage of American businesses that hire foreign-flag ships for exports and imports today is closer to 99 percent than the “greater than 80 percent” stated in the EA. These errors were corrected in the version of the EA currently on the Mercatus website.

CONCLUSION

After a thorough evaluation of the arguments made by supporters of the Jones Act, the conclusion remains

the same. The Jones Act is harmful to American consumers and businesses as a whole. Americans would gain from a major reform of the act, including a possible repeal. However, the supporters of the act have effectively protected it from repeal since 1920, and there is little evidence that their political support is diminishing. If repeal is not a reasonable option, reform of the act that would include relaxing the American-built requirement for ships would bring substantial benefits. A specific bill supported by the Hawaii Shippers’ Council would provide an exemption from the American-built requirement, but only for oceangoing ships traveling to or from the noncontiguous parts of the US (primarily Hawaii, Alaska, and Puerto Rico). The remaining features of the Jones Act would remain in place. To make the reform more palatable to shipyard employees, compensation could be paid to certain shipbuilders for a limited number of years. A precedent for such a buyout would be the tobacco buyout of 2004–2014.

NOTES

1. Thomas Grennes, “An Economic Analysis of the Jones Act” (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, 2017).
2. American Maritime Partnership (AMP), “Thomas Grennes’ Jones Act Paper Is a One-Sided Advocacy Document, Not a Real Study,” June 20, 2017.
3. AMP, “Thomas Grennes’ Jones Act Paper.”
4. The author of the AMP document objects to the frequency with which three authors were cited in the EA. The prolific authors were Michael Hansen of the Hawaii Shippers’ Council, John Frittelli of the Congressional Research Service, and Bryan Riley of the Heritage Foundation. The AMP finds nothing wrong with the content of the works of these authors. These same authors are also frequently cited by other writers seeking knowledge about the Jones Act. In fact, they are cited frequently precisely because they possess expertise on specific aspects of the Jones Act, and they have earned reputations for producing a large volume of accurate and high-quality work.
5. Government Accountability Office, *Puerto Rico: Characteristics of the Island’s Maritime Trade and Potential Effects of Modifying the Jones Act* (GAO-13-260, Washington, DC, March 14, 2013).
6. Grennes, “Economic Analysis of the Jones Act.”
7. Michael Hansen, “Sixth Shipping Executive Goes to Jail in Puerto Rico Rate Fixing Case,” *Hawaii Free Press*, December 10, 2013.
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9. Joseph Bonney, "US House Members: Do Not Extend Jones Act Waiver," *Journal of Commerce*, October 3, 2017.
10. Grennes, "An Economic Analysis of the Jones Act."
11. "The Decline of U.S. Shipbuilding," *Shipbuilding History*, January 21, 2016, <http://www.shipbuildinghistory.com/statistics/decline.htm>.
12. Michael Hansen, "Matson and Pasha Skirt Jones Act U.S. Build Laws with Coast Guard Okay," *Hawaii Free Press*, August 15, 2017.
13. "Relief Groups Hit Major Hurdles Getting Aid to Puerto Rico," *Gant News*, October 23, 2017.
14. Michael Hansen, "Guam Legislature Passes Jones Act Reform Resolution," *Grassroots Institute*, April 18, 2014.
15. Andrew Gibson and Arthur Donovan, *The Abandoned Ocean: A History of United States Maritime Policy* (Columbia: University of South Carolina Press, 2000).
16. Erik Olsen, "An Arcane Law Protected by Powerful Interests Is Causing Insane Traffic Jams," *Quartz*, August 7, 2017.
17. Olsen, "An Arcane Law."
18. Steve Patterson, Andrew Pantazi, and Joe Daraskevich, "Coast Guard Finds Fault in Captain, Owner, and Others after *El Faro* Sinking," *Jacksonville.com*, October 1, 2017.
19. Thomas Grennes, "Does the Jones Act Endanger American Seamen?," *Regulation*, Fall 2017.

About the Author

Thomas Grennes is an emeritus professor of economics at North Carolina State University. He has written extensively on topics related to international trade and finance. After the disintegration of the Soviet Union, he joined the newly founded Stockholm School of Economics in Riga, in newly independent Latvia, as a visiting professor. He coauthors the blog *Thoughts from across the Atlantic* with Andris Strazds at www.economonitor.com/thoughtsacrossatlantic.

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