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The Rush  
to LNG

March/April 2012

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Madsen is a big believer in clean  
energy and sustainable business  
practices. His company is too.

BY TONY MUNOZ





**D**uring the past six years the Department of the Navy and the Maritime Administration have been engaged in separate Dual-Use Vessel (DUV) and America's Marine Highway (AMH) programs to determine what should be done to encourage Jones Act operators to initiate ocean service on America's inland waterways with commercially viable and militarily useful "dual-use vessels." Recently funded studies have identified suitable vessel designs as well as likely ports of call.

Where do matters stand and what must be done to achieve success?

## BACKGROUND

Last November MarAd and the Navy announced a memorandum of agreement giving formal recognition to the relationship between the DUV and AMH programs. A year earlier the two entities had agreed to fund an \$800,000 joint American Marine Highway Design Project that would encompass:

A study of vessel types most suited for transporting trailers and cargoes normally driven over the road so that AMH can contribute to the reduction of congestion, pollution, and wear and tear

on the nation's highways – to serve the long haul freight market -- and suitable for military use in times of national emergency.

The contract was awarded; the work was carried out, and the results were submitted. Eleven vessel designs were selected for further study. Market assessments and economic analyses were also conducted. A Final Report was issued in January. In February the Military Sealift Committee of the National Defense Transportation Association issued invitations for a March 5 conference at which senior Navy and MarAd personnel could meet with Jones Act operators to present the results of the Final Report and associated studies and receive operator suggestions as to how these proposals should be modified and supplemented to best achieve DUV and AMH objectives.

At the March 5 meeting Navy personnel explained the DUV needs for their sealift fleet and their belief that the AMH program presented the most viable means of achieving this objective. MarAd personnel reported on the status of AMH implementation and on AMH corridor studies still underway. Reports of jointly funded expert studies on the "American Marine Highways Dual-Use Vessel Development Program" and the "Marine Highways

# THE DUAL-USE VESSEL PROGRAM AND AMERICA'S MARINE HIGHWAY – NEXT STEPS

By Clay Cook

A noted industry expert provides a prescription for progress.

System Evaluation Model” were given, and proposals for government actions to assist in the success of these efforts were tabled. At the conclusion of the meeting there was shared agreement that it had been worthwhile and optimism concerning further progress.

What are these DUV and AMH programs and what lies ahead?

## DUAL-USE VESSELS

The concept of the “dual-use vessel” can be said to date to the beginnings of the republic itself. And the nation’s principal 20th century maritime legislation – the Merchant Marine Acts of 1920, 1936 and 1970 – were express in their recognition of this dual-use role:

*That 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...sufficient to carry the greater portion of its commerce and serve as a naval or military auxiliary in time of war or national emergency.*

-Preamble, Merchant Marine Act of 1920

Section 27 of the 1920 Act was designed to meet this objective in our domestic trades. Government support under the 1936 Act and the 1970 Act was intended to ensure such a fleet in our international trades by providing “differential subsidy” payments that equalized the vessel operating and capital costs of U.S. owners with those of foreign competitors, coupled with MarAd Title XI govern-

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ment financing guarantees and Title VI government tax deferrals.

Today, only the Title XI financing guarantee and Title VI capital construction fund (CCF) tax-deferral programs remain available to support the construction of commercial vessels in U.S. shipyards and their operation in the domestic trades and as dual-use vessels in time of need.

**SHIPYARD AND VESSEL FINANCING**

The Navy's current DUV program began at a Senior Executive Sealift Forum in 2005, which welcomed participants with the injunction: "Our ultimate objective is to find out what it will require to induce U.S. shippers and ship operators to move cargo and operate U.S.-flag ships, respectively, that will have military utility and be available for military use during a major contingency."

The Navy's concern with the prices faced by Jones Act operators who would purchase and operate this DUV tonnage was addressed in Navy-sponsored National Shipbuilding Research Program Workshops in 2007 and 2008. In the 2007 Workshop attention was directed to methods by which shipyard production costs could be reduced. These presentations confirmed that U.S. shipyards might be able to offer commercially acceptable sales prices when multiple-vessel production was combined with foreign shipyard assistance.

While the shipyard price is the vessel "cost" for the Navy, the cost for a Jones Act purchaser is the shipyard price plus the cost of financing – the vessel's "fully financed cost." An analysis of

available financing alternatives to determine the means by which this "fully financed cost" could be minimized was prepared for the 2008 Workshop, which indicated that if the existing Title XI loan guarantee and CCF tax-deferral programs were made available, cost reductions of 15 to 30 percent could be achieved, and in some cases the CCF savings could entirely "erase" vessel financing costs and provide "zero percent" Jones Act vessel financing.

**"SHORT SEA SHIPPING" AND AMH**

A MarAd and Department of Transportation (DOT) "short sea shipping" program was announced by Maritime Administrator William Schubert in 2002 and discussed at length in his FY 2003 authorization testimony. The program was rechristened "America's Marine Highways" by Maritime Administrator Sean Connaughton.

Congress addressed these short sea shipping issues in the Energy Independence and Security Act of 2007, which contained provisions establishing a formal marine highway program within the federal government and charged DOT with responsibility for implementation and administration. DOT received a broad grant of authority for federal action and for federal and local government collaboration in order to attract public and private sector projects to access the nation's "ocean highways," including the authority for European-style Marco Polo and Motorways of the Sea programs. The merits of these initiatives to "move traffic from our highways to our waterways" were obvious.

The House version of the 2007 Act addressed the need for U.S.

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government-assisted financing for the required vessels by extending the CCF tax-deferral program to ro/ro and container services nationwide and authorizing \$2 billion for short sea transportation use from the Title XI loan guarantee program. As the 2007 Act was enacted, it included the CCF program extension but not the \$2 billion authorization for Title XI financing. Furthermore, it did not remove the 1986 Treasury initiatives that had been designed to curtail CCF program use and diminish its value.

No initial funding was provided for implementation of the 2007 Act's grants of authority, and only limited funding has since been available. However, MarAd moved ahead in designating Marine Corridors and Connectors and providing Marine Highway Grants and entering into Marine Highway Cooperative Agreements. Most importantly, as funds have become available MarAd has worked with the Navy to coordinate AMH and DUV program objectives.

### PRESCRIPTION FOR PROGRESS

The principal issues of shipyard construction are apparently agreed on the basis of the 2007 and 2008 Workshop recommendations and the Design Report assumptions. The potential for Title XI and CCF programs to reduce fully financed costs is apparently agreed as tabled during the 2008 Workshop, subject to the removal of the 1986 tax barriers to CCF program use.

With the Design Report in hand and two additional corridor studies due in May, MarAd and the Navy appear well on their way to achieving the Navy's 2005 Senior Executive Sealift Forum objective of learning "what it will require to induce U.S. shippers and ship operators to move cargo and operate U.S.-flag ships, respectively, that will have military utility and be available for military use during a major contingency."

The next step will be to obtain Office of Management and Budget approval for a series of legislative initiatives to include the following:

- 1 Repeal of the Harbor Maintenance Tax as applied to AMH services;
- 2 Repeal of the Treasury's 1986 CCF limitations enactments (returning that program to the form in which it was originally enacted);
- 3 Modification of the tonnage tax to allow its application on a strictly days-in-service foreign vs. domestic basis (returning the tonnage tax to the form in which it was originally drafted);
- 4 Authorization of a multiyear federal financing guarantee program that was a part of the House-passed version of the 2007 Act, backed by some form of multiyear appropriations funding; and
- 5 Authorization for a specific European-style Marco Polo program to mitigate start-up risks.

With industry support, congressional approval of such legislation appears achievable. And with these changes made it may be possible to initiate one or more AMH services with relatively modest forms of government start-up assistance. **MarEx**

**H. Clayton Cook, Esq.** has been involved with Jones Act issues for more than 40 years and served as General Counsel of the Maritime Administration from 1970-1973. He is currently Counsel to Seward & Kissel LLP in Washington, DC.

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