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DOMESTIC OFFSHORE SHIPPING

GOVERNMENT

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HEARINGS
BEFORE
THE MERCHANT MARINE AND FISHERIES
SUBCOMMITTEE OF THE
COMMITTEE ON
INTERSTATE AND FOREIGN COMMERCE
UNITED STATES SENATE
EIGHTY-SEVENTH CONGRESS
FIRST SESSION
ON
THE PROBLEMS OF THE NONCONTIGUOUS AREAS SHIPPING
INDUSTRY AND TO THE ECONOMIC IMPACT ON THE OFF-
SHORE AREAS SERVED

MARCH 6, 7, 13, AND 14, 1961

Printed for the use of the Committee on Interstate and Foreign Commerce

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DOMESTIC OFFSHORE SHIPPING

MONDAY, MARCH 6, 1961

U.S. SENATE,
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
SUBCOMMITTEE ON MERCHANT MARINE AND FISHERIES,
Washington, D.C.

The subcommittee was called to order, pursuant to notice, at 10 a.m. in room 5110, New Senate Office Building, Hon. E. L. Bartlett presiding.

Senator BARTLETT. The subcommittee will be in order.

Before proceeding with the hearings, I should like, for the record, to outline briefly the nature and scope of the subcommittee's interest.

The present hearing is an extension of the inquiry commenced in the last session on problems of the domestic shipping industry. Earlier hearings were directed to the problems of the coastwise and intercoastal segments of the domestic shipping industry. Attention now will be directed to the problems of the noncontiguous shipping industry and to the economic impact on the offshore areas served.

Shipping to the major noncontiguous areas of the Nation operates under the same basic statutes as those which govern coastwise and intercoastal transportation, except for economic regulation, and is confronted by the same cost problems and operating conditions. Rate levels of transportation between the continental and noncontiguous areas have advanced in a continuing and accelerating round of general increases in postwar years. In some instances, new general increases have been filed before final decisions on previous rate increases. At present separate rate cases affecting the three major noncontiguous areas of Alaska, Hawaii, and Puerto Rico are in process of determination.

A continuing conflict has developed between the crucial need for reasonable transportation rates to the noncontiguous areas necessary to their survival, and the need of carriers for increased revenue to meet mounting costs of operating, cargo handling, and vessel replacement. It has become quite apparent that, almost irrespective of the merits of decisions in specific rate cases, the piecemeal approach of present regulatory proceedings offers no long-range solution of the fundamental problems.

It is the purpose of the present hearings to take, we hope, a "new look" at not only the specific problems but at the basic policies and programs of Government as they affect the present shipping services to each of these important domestic areas. It is the subcommittee's intention at this time to hear from all who are concerned and affected by present conditions seeking specific information, ideas, or proposals which might be relevant in developing appropriate legislation.

I think I speak for my fellow committee members when I say these problems must be viewed as national problems—and their resolutions must, therefore, be reflections of a national policy. It is our hope that each witness will, without the restraints of tradition, speak on both the specific issues and policies that will best serve the long-range national interest.

The record of these hearings will remain open for supplementary statements and material for a period of 6 weeks following the last day upon which testimony is received.

I am going to ask unanimous consent, which will be promptly granted, to follow the statement which I have just made with an associated statement bearing more specifically upon the general subject, but I will not consume time now by reading it.

(The statement follows:)

PROGRAM FOR STUDY OF SHIPPING PROBLEMS OF THE DOMESTIC NONCONTIGUOUS AREAS

I. NEED FOR THE STUDY

Recent rate increases requested by American-flag ocean carriers for service to U.S. noncontiguous areas and States—principally Alaska, Hawaii, Puerto Rico, and Guam—point up a critical conflict: that between the need, by the carriers on one hand, for higher freight revenue to meet mounting operating and vessel replacement costs; and on the other hand, the requirement that these noncontiguous areas have low transportation rates in order to survive and develop their economies. At the present time the following facts are component parts of a statement of the problem; the noncontiguous areas are mainly dependent on ocean transportation for export and import movements; most of this traffic is between the U.S. mainland and these offshore areas; under the terms of the cabotage laws trade with the mainland is restricted to American vessels; and, rate regulation in such trade is under the jurisdiction of the Federal Maritime Board.

Assuming that the primary national interest is best served by fostering and expanding trade between the mainland and U.S. territories and noncontiguous States, the problem becomes how to provide reasonable freight costs that will not penalize or undermine the local economies. Experience with case by case regulatory disposition of these rate matters amply justified the conclusion that no long-range resolution is to be gained on a piecemeal basis. In each proceeding, the agency has been confronted with the choice of penalizing the carrier and its future ability to serve or penalizing the industry and consumers in the area served. This adversary atmosphere, heightened by the frequency of rate controversies, has not lent itself to judgments that go beyond the narrow confines of the record.

What is needed, and what the Merchant Marine Subcommittee must concern itself with, is a policy on this matter that best serves the national interest.

II. PURPOSE AND SCOPE OF THE STUDY

To determine (or redetermine) such a policy will require initially a definition of what the national interest is—what commercial and defense goals are sought and what prestige and foreign policy objectives must be fulfilled by this trade. Conversely, a delineation must be made of the values not to be protected.

Next, an examination in depth must be made of the problems facing both the areas served and the ocean carriers serving these areas. Such examination cannot be limited solely to the present high cost—low rate conflict, but beyond to anticipate, for example, the popular industrial ambitions of each noncontiguous area and the rates and service frequency needed to fulfill the goals.

Finally, alternative policy solutions would be proposed and their effects considered. In each case the alternatives will be tested for their consistency or inconsistency with the definition of national policy.

Failure to deal affirmatively with this problem, not at a very critical point, invites a policy of drift.

III. SUGGESTED FORM OF HEARINGS

A. Statement by representatives of the local government of Hawaii, Alaska, Guam, and Puerto Rico: These statements should encompass all aspects of the problem as seen by the offshore areas. At this session technical data should be submitted by witnesses backing up the main speaker.

B. Testimony from the carriers involved in the trades between the mainland United States and the noncontiguous areas. This general material also to be accompanied by technical data.

C. After this statement and joining of the problem, the various Government agencies and Departments would be invited to give their views of how the national interest is involved, and how best it is to be served.

D. Presentation and consideration of alternative methods for resolving the transportation problem: Several of the previous witnesses may want to return to express their views on the soundness of these alternatives.

It is to be noted that the committee does not anticipate that the differing factual problems of each offshore area will necessarily be susceptible to the same solutions.

Senator BARTLETT. Now the witness list before me reveals that the able and distinguished Senator from Hawaii, Senator Hiram Fong, will testify first.

STATEMENT OF HON. HIRAM L. FONG, U.S. SENATOR FROM THE STATE OF HAWAII

Senator BARTLETT. We are glad to have you.

Senator FONG. Senator, I am very happy to be here this morning. I deeply appreciate the opportunity to appear before you and express my views on a matter of vital importance to the State of Hawaii.

Hawaii is the only island State and is completely dependent upon shipping for her sustenance. The attainment of statehood and the increased commercial activity resulting therefrom has served to emphasize this dependence.

In his recent testimony before the Federal Maritime Board, Dr. James H. Shoemaker, vice president, Bank of Hawaii, stated that more than two-thirds of the food consumed in Hawaii is shipped by surface transportation from the mainland, and more than 90 percent of consumer goods other than food, which include clothing, automobiles, and building materials, are similarly imported. By the same token, the chief agricultural products of Hawaii, sugar and pineapple, must reach mainland markets by ship. In 1958, 2,699,287 tons of consumer and industrial goods were shipped to Hawaii from the mainland, while 1,472,744 tons of Hawaiian products similarly moved to the mainland. Service is provided between the mainland and all deep-water ports located in the islands by freighter.

For many years, Matson Navigation Co. has been the chief carrier of freight between the west coast of the United States and Hawaii, and has likewise carried passengers to and from Hawaii. Matson has served Hawaii efficiently and well.

However, since 1946, because of rising costs, this company has placed nine general rate increases into effect. Two of these resulted in hearings and in each instance the Federal Maritime Board found that the increases were just and reasonable.

Pending now before the Board is a further application by Matson for a 12½-percent increase. This increase is being opposed by the State of Hawaii and by local industrial interests. It appears that a point may have been reached where the freight costs not only

have become a burden upon consumers and business interests in Hawaii and a hindrance to economic development of the new State, but that costs incurred by this shipping company are such that it may be uneconomic for it to continue to do business without further rate increases.

I do not take any position, Mr. Chairman, with respect to the reasonableness of these rate increases. The decision on what a fair rate of return should be to the owners of a shipping company is one which requires meticulous study by accountants and economists. I am tremendously concerned, however, by the increasingly heavy burden placed upon consumers in Hawaii and upon local industries which export their products to the mainland.

The pineapple industry offers a good example of the dependence of Hawaii's business interests on shipping as well as the burden of rising freight costs on a local industry. This is a \$125 million industry which employs between 10,000 and 20,000 persons, depending on the season. Today, this industry finds itself in a highly competitive market, and its position as one of the basic income producers in Hawaii is jeopardized. A leader in the industry has stated that competitive conditions have prevented the industry from passing on the most recent freight increases to its customers and that the industry is in no position to absorb any further freight increases.

The Federal cabotage laws (46 U.S.C. 289, 46 U.S.C. 883) prevent the carriage of goods and passengers between Hawaii and the mainland on other than American-flag vessels. This legislation has been justified on the ground that it encourages the growth and development of an American merchant marine which can be made immediately available in time of war. I am in full accord with this principle.

However, because of these laws, offshore areas such as Hawaii cannot take advantage of the lower rates provided by foreign vessels for shipment of freight. They are compelled to pay substantially more each year for their essential ocean freight services because of the national policy requiring them to use U.S.-flag vessels than they would be if they were free to use the most economical services regardless of nationality.

Furthermore, this inequitable burden may well increase in the near future. The vessels presently serving Hawaii were constructed for the most part during World War II for the United States and sold at favorable prices after the war to the private carriers. These vessels are now almost all approaching their 20th anniversary in service. They will have to be replaced eventually. If they are replaced at present U.S. ship construction costs, which are almost twice as much as foreign costs, these costs will have to be absorbed by the people of Hawaii through even higher freight rates.

I believe that maintenance of a segment of a strong U.S. merchant marine should not devolve chiefly upon these areas. The problem is national and should be solved on a national basis.

It is my hope that the committee will make a thorough study of these problems and that it will recommend solutions which will be in the best interest of the people and business interests of the offshore areas, recognizing at the same time that the ocean carriers serving these areas must make a reasonable profit if they are to continue in business. With particular respect to Hawaii, orderly development of its economy in the years to come will depend upon the regularity of

ocean transportation and the reasonableness of shipping rates. Finally, national policy with respect to maintenance of the U.S. merchant marine must be reexamined and new determinations made.

Thank you, Mr. Chairman.

Senator BARTLETT. Thank you, Senator Fong. I believe you mentioned that more than two-thirds of the food consumed in Hawaii reaches there by ocean shipping.

Senator FONG. Ninety percent, Mr. Chairman. Ninety percent of all consumer goods, other than food.

Senator BARTLETT. How about food?

Senator FONG. Two-thirds of the food consumed in Hawaii is imported.

Senator BARTLETT. Do you foresee the possibility that at some time in the future a greater percentage of food will be produced in the islands for local consumption or do you believe the land will always be more valuable for sugar and pineapple?

Senator FONG. I believe the land is always more valuable in the type of agricultural pursuits we are now pursuing. We have a very difficult time in Hawaii in getting land for the truck farmer. For example, on the Island of Oahu, where almost 80 percent of our population is situated, on 10 percent of the land, of the State we almost have no land for agricultural pursuits for small farmers, and it is a very, very difficult thing to find land for these truck farmers to produce the things we need. More and more I think we will be dependent on surface transportation to take care of our requirements.

Senator BARTLETT. While your land is most productive, the aggregate acreage available is rather limited in terms of Nebraska or the Dakotas, for example.

Senator FONG. Yes, very much so. Much of our land is mountainous, and I believe we only have around 10 to 15 percent class A land that could be used for good agricultural purposes. Much of our land is class B land and mountainous terrain.

Senator BARTLETT. Now, pursuing that line of inquiry for a moment more, how does the island of Hawaii, for example, or any of the other islands receive its foodstuff? Does it all come to Honolulu and then transshipped, or is there direct service from the mainland?

Senator FONG. We have direct service to the various islands, and we also have transshipping from Oahu. I do not know what the percentages are, but there is quite a lot of transshipment.

Senator BARTLETT. Transshipment is by barge or how?

Senator FONG. By barge mostly.

Senator BARTLETT. My recollection is that Hawaii is the only one of the three offshore areas—Alaska, Hawaii, and Puerto Rico—that now enjoys passenger steamship service. How many carriers serve Hawaii for passenger carriage?

Senator FONG. I believe there are two passenger carriers, Matson and American President Line.

Senator BARTLETT. Are the passenger ships of Matson new, medium aged, or becoming older?

Senator FONG. I think they are more than 20 years old and within a few years they will have to be replaced.

Senator BARTLETT. If they are replaced, if new ships are built for that trade, under existing circumstances, would it not require a very considerable elevation of passenger rates?

Senator FONG. From my understanding, a freight-carrying ship costs around \$10 million. These ships were acquired by the Matson Navigation, I believe, for the sum of approximately a million dollars. Now, there is a difference of \$9 million there not taken into account in computing costs. If you were to make a 6-percent return, there is \$54,000 right there, to be considered in just interest alone on the \$1 million without talking about the cost of amortization or depreciation, say for a period of 20 years. It must necessarily follow these ships are to be replaced by ships that would exceed in cost the sum now being shown on the books, and that the company expects a return of probably 6 or at least 4 percent on their costs. Under those circumstances the rates will materially rise. Passenger ships, I understand, cost at least \$25 million each.

Senator BARTLETT. There is keen competition at this time, is there not, between the passenger steamships and the airlines?

Senator FONG. I am not in a position to answer that question, except that there are not too many trips that have been made by the Matson Navigation with the two ships they have. I think they have the *Matsonia* and the *Lurline*. There is a Matson man here who will be able to give that testimony.

There are only two ships that make the Hawaiian run, and there is some talk one of the ships will be taken off the run in June. I don't know whether that is definite or not.

The Matson Navigation people have representatives here to testify and I presume they will be able to answer that question. But most of our passengers come by airlines rather than by ships.

Senator BARTLETT. Is that on account, would you think—of course, this is all speculative—of a desire to save time, and be able to spend more time in the islands—

Senator FONG. It is cheaper by airplane because it only takes 4½ or 5 hours to get to Hawaii now—whereas by ship it takes around 4½ days, and with all the food and services that must go with 4½ days on a ship, the costs are much higher if you go by ship than if you go by airplane. Most of our passengers come to Hawaii by airplane.

Senator BARTLETT. From some later witness we will seek to elicit information about the comparative rate schedules, in part to point up the possibility that you have suggested—that if the carrier serving Hawaii has to get new ships on run, with the high costs, the trade actually may no longer be competitive.

Senator FONG. Yes.

Senator BARTLETT. Thank you very much, Senator Fong, for a most useful statement.

Senator FONG. Thank you, Mr. Chairman.

Senator BARTLETT. Our next witness will be the former Governor of the then Territory of Hawaii, one-time superintendent of instruction of the territory, and now the Senator from the new State, Senator Oren Long.

We welcome you, Senator, because we know that you always are eminently qualified to speak on this subject.

STATEMENT OF HON. OREN E. LONG, U.S. SENATOR FROM THE STATE OF HAWAII

Senator LONG. Thank you, Mr. Chairman.

It may seem obvious that the questions to be considered in these hearings are important to Hawaii. One need only to consult a map or a globe to see that our island State is totally dependent upon sea transportation as far as all heavy goods are concerned. Yet while transport by rail, motor, and inland waterway has been the subject of many books, extensive inquiries, and considerable legislation, transportation to and from the so-called noncontiguous areas seems largely to have been overlooked. It is even possible that some persons underestimate the interest of the people of Hawaii in a solution of the problems—an illusion that I hope to correct.

I wish to make it unmistakably clear that Hawaii has a deep and permanent interest in sea transportation. Indeed, I know of no domestic issue with a greater impact on my State than that of how best to provide the transportation without which we will suffer irreparable damage. Further, we recognize a community of interest with the people of Alaska, Puerto Rico, and Guam in this regard. For these reasons, we welcome these hearings and stand ready to assist the committee in any way we can.

Some basic facts of island life are involved in this matter. Among these facts are the following: One, we are dependent on sea transportation for our very existence. Two, further integration into the national economy can be fostered only through sea transportation; and, three, this one essential service is beset by economic problems created by established national maritime policies.

We are caught up in a cost spiral that is exacting an ever-increasing toll on our economy and our people. We have no choice but to pay the bill—it is unthinkable that we should be without the service of water carriers—but the bill is getting higher and higher and is approaching the point where severe damage may be done to our economy and our standard of living.

For we are talking here not about trivia or luxuries. We are talking about the cost of importing two-thirds of our food and nine-tenths of our other consumer goods. We are talking about the cost of exporting over half of the production of our economy. And we are also talking about the impact of these costs on a community that already has one of the highest costs of living in the Nation and where production costs are already at a level where foreign commodities are challenging ours in the American market.

I am not one to grieve about the economic integration that these figures disclose. Rather, I feel that the facts are evidence of a desirable division of labor between us and our sister States. But the general freight rate rose 89 percent in 8½ years prior to 1959 and I fear that, if rates continue on the escalator, we may yet be raising our own rice and letting California's versatile farmers try their hands at pineapple culture.

The problem cannot be laid fully at the doors of the carriers or the Federal Maritime Board. True, we have had our differences with both, but the root cause lies much deeper. It lies in two fundamental elements of maritime law; one, restriction of offshore trade to Ameri-

can-flag carriers, and, two, the absence of subsidy for carriers in this protected trade.

These two factors together force our own small community to bear the full burden of the costly American maritime industry as it affects the Hawaiian trade. In the absence of subsidy, shipping revenues must be high enough to meet American wage standards, American shipbuilding costs, and the other American-level expenditures associated with operating an American-flag service. So revenues must rise, and every business, every person in Hawaii feels the impact.

What can we do to improve the situation? The easiest solution would be to open our trade to foreign flags and let rates find their economic level through competition. An unsubsidized lifting of the sabotage restriction would, however, run counter to national policy and would surely put our carriers out of business. This would be an impossible approach.

If, however, carriers to offshore areas were treated the same as carriers in foreign commerce, a favorable rate structure would be possible without causing disaster to American-flag shipping. Again rates would seek their economic level through competition, but carriers would be sustained through subsidy and the national policy of keeping American bottoms on the sea would be reinforced. Consideration of this alternative is clearly merited.

A third possibility would be to award subsidies to our carriers while retaining the cabotage restriction. This would remove some of the present inequities, but would raise major questions in ratemaking and in distributing total costs between artificially constructed rates and subsidies for which standards would be difficult to find.

I feel that I cannot make a definite recommendation today. I, too, am looking forward to what these hearings may reveal. But I would be remiss if I did not urge the need for taking some action to alleviate the present situation. Some change in our maritime laws must be made to accommodate the peculiar problems of noncontiguous areas within the framework of national maritime policy. I am confident that sound legislation will be developed as a result of these hearings. I hope so, because the stakes could hardly be greater for Hawaii.

Senator BARTLETT. An excellent statement, Senator Long, which will be truly helpful to the committee.

I was, perhaps, particularly impressed by the third point you mentioned, on page 1 of your statement, where you said—and I quote:

This one essential service is beset by economic problems created by established national maritime policies.

Your view, then, is, I take it, that what is occurring in Hawaii and these other offshore areas is occurring inadvertently, so far as intention is concerned, by reason of maritime policies adopted by this Government long since, which were not tailored to the situations to which you now address yourself?

Senator LONG. That is correct.

Senator BARTLETT. And your contention is that the time has come for the National Government to take a separate look at the offshore situation?

Senator LONG. Yes. I think it should be carefully studied, evaluated, and these new conditions that have developed be met. It is going to become increasingly more difficult for Hawaii as our population

increases. Of course, it will be the same with your State of Alaska.

Senator BARTLETT. The committee, in the 86th Congress, held many hearings relating to the intra- and inter-coastal shipping trades and learned, among other things, that service along our coasts has virtually disappeared. That, of course, is highly unfortunate so far as our need to have a fleet is concerned, and is unfortunate in other ways.

But in those cases, as we all know, there are other modes of transportation which are available. That will never be true, so far as we can now predict.

Senator LONG. That is true.

Senator BARTLETT. You are going to have to pay the bill under present laws and practices, whatever that bill may be, no matter how much economic and other suffering may take place in the State if this continues—if this cost spiral continues.

Thank you, Senator Long, very much, indeed.

Senator LONG. Thank you, Mr. Chairman.

Senator BARTLETT. The next witness is Chairman Stakem, Federal Maritime Board, and Maritime Administrator.

We greet you in both those capacities, Mr. Chairman.

STATEMENT OF THOMAS E. STAKEM, CHAIRMAN, FEDERAL MARITIME BOARD, MARITIME ADMINISTRATOR

Mr. STAKEM. Thank you, Senator.

Senator BARTLETT. You may proceed.

Mr. STAKEM. Thank you, Senator Bartlett.

The Federal Maritime Board welcomes the opportunity to participate in this study and in the consideration of the problem of shipping in the domestic offshore trades for the Board has been much concerned over the fact that in recent years increasing expenses have forced the carriers in these trades to make rate increases which, although justified from the standpoint of the ship operator, nevertheless have an impact on the residents of the domestic offshore areas which they can ill afford to withstand. The proper solution of these problems makes it necessary to give attention to all pertinent facets.

There can be no doubt that for years to come water transportation will be the principal means for the interchange of goods between Alaska, Hawaii, Puerto Rico, Guam, and the 48 contiguous States of our United States. It is equally clear that the proper development of these offshore components of our Nation will rest in a large measure on the water transportation services which form the essential connecting link. The problem then becomes basically one of, Can these services be provided at a cost which will not inhibit the proper growth of those areas?

Virtually all rate increases made in these trades in recent years have been subjected to formal investigation by the Board. Some of these are still in the progress of hearing and as to these no comment is made—the outcome cannot be foreseen. However, with respect to the completed investigations, the evidence has shown that the increases were justified and necessary if the carriers were to maintain their services.

It is readily apparent that since the ocean transportation costs are not resulting in unreasonable profits to the water carriers, any reduc-

tion in their rates must be compensated for through reductions in their expenses of operations or offsetting income from other sources or the services will not be continued. The question to be resolved by the Congress and the President is whether the national interest dictates as a result of these hearings that the Federal Government provide the necessary funds for such compensation. If it is determined that subsidization of these services is necessary—as to which I am not prepared to make any recommendation at this time—there are a number of possible methods by which varying degrees of reduction in the cost of ocean transportation might be accomplished. They are:

(1) Construction-differential subsidy on new vessels: This might offer some help in the replacement of present fleets. However, it must be borne in mind that present fleets represent purchases of war-built ships at which might be termed bargain prices. Replacement costs, even with construction subsidy, would exceed prices so that the rate base would not be reduced. By itself, this alternative, while it might make possible the ultimate and necessary replacement of ships, would not lead to a reduction in rates unless a new type ship of far greater efficiency could be designed and built with such aid.

A variation of the construction subsidy method might be to build replacement ships for the Government's account, sell them to the operators at minimum downpayments of 5 to 25 percent and payments on a low interest rate mortgage to be made only if earnings exceeded a given profit percentage. This could be termed an "earnings debenture plan."

(2) Operating-differential subsidy: In this method, the absence of foreign competition in the noncontiguous trades, because of the existing cabotage laws, would make it necessary to provide an entirely new basis for establishing the amount of the subsidy payable and be a drastic departure from the principle envisioned by this form of subsidy.

(3) Trade promotion subsidy: In place of an operating differential subsidy, consideration could be given to a direct subsidy to assure service at rates which would be set or affirmatively authorized by the Government. This would be in the nature of a contract between a qualified shipping line and the Government of the United States which would call for the operation of specific service with stated frequencies at freight rates which would be specified by the Government on the basis of the economic needs of the areas to be served regardless of whether the rates were compensatory. The subsidy which would be paid would be designed to offset losses incurred from such an operation.

Several countries already grant aids of this nature to shipping companies to induce them to supply needed services to areas which could not support shipping lines without some such aid. Canada, for example, has paid subsidies to coastal and inland water carriers to provide services to outlying communities where operating expenses are greater than probable revenues. Other countries have done this in order to provide services to small outlying islands and communities where profitable commercial operation is virtually impossible.

In the light of the need for economic development in our noncontiguous States and possessions and their dependence on ocean transportation, the question of establishing a direct subsidy in the nature of a trade promotion or cost of living subsidy to reduce costs would

warrant serious consideration only if a valid case can be made that such development is being stifled by high ocean freight rates.

(4) Government operations: As an alternative method to providing direct subsidy to the carriers in the offshore domestic trade, Government operation of the services would be possible.

Under such Government operation, presumably through general agency arrangements, freight rates could be set at such a level as was deemed consistent with furthering the development of the States and territories. Excess of expenses over revenues would be borne by the Government.

Such an operation is open to criticism on the grounds that it is contrary to the philosophy of fostering private shipping enterprise. Further, there is the practical problem of the manner in which the existing private operators could be integrated into the Government operation, even assuming that such operators are provided priority in the appointment of general agents.

(5) Government charter: The Government could furnish ships to the operator at a low minimum charter hire, graduated upward on the basis of profits, if earned.

In such a plan, the minimum charter hire expense would be used in determining the fair and reasonable carrier rates and any increased profits would be recouped by the Government on a sliding-scale basis.

All of the foregoing suggestions would require legislation and substantial appropriations. In addition to these suggestions, lower rates might be obtained through repeal of the cabotage laws. We strongly urge that this proposal does not merit serious consideration. Such action would be potentially destructive of U.S.-flag operations in these trades with the resulting loss of availability of American vessels and employment of American seamen without assurance of any substantial reduction in freight rates. If trade was dependent in whole or in part on foreign-flag tonnage, any world disturbance could lead to withdrawal of foreign ships with the resulting difficulty of replacement by U.S.-flag services. As to Alaska, due to the high cost of loading and discharging cargo, the seasonal factors, and the character of this trade, there is no assurance that foreign-flag carriers would provide the necessary service to develop the area. They would presumably—as is usual—concentrate on the port or ports through which the greatest amount of cargo flowed and on the port or ports which they could serve most easily in combination with their calls at foreign ports, such as Japan, China, et cetera, with the result that some ports would not receive sufficient service.

Moreover, the repeal of these laws would involve a complete departure from the traditional policy since the early days of American independence of reserving these trades to U.S. ships. Available traffic would be divided with the result that our domestic fleet would be further reduced in number, if not completely eliminated. The continuance of any American operators in the trades would require the payment of construction and operating subsidies. In two world wars the domestic fleet has been an important nucleus which was in immediate operating condition and available to serve military and naval needs. The necessity for their continued existence seems beyond doubt.

There has been some thought that if a certificate of convenience and necessity was required before a water carrier could engage in domestic offshore trades, the result would be that cargo would not be drained away from the regular carriers in the trade by irregular or casual operators and that this would result in a better utilization of the space offered by the regular certificated carriers. With better filled ships the revenues would be improved without substantial increase in operating expenses and this, it is suggested, would enable the certificated carriers to reduce their rates.

This is highly problematical. The effect of a certificate, of course, is to protect existing operators from additional competition. The elimination or reduction of competition rarely leads to better rates or services. For example, it seems doubtful that container operations would have developed as far as they have today in the domestic offshore trades without the spur of competition.

A suggestion that does not require Federal aid, yet offers a hope for decreases in cost of ocean transportation service to the offshore areas, is the development of more efficient service. The handling of unitized freight-containerized cargo via integrated ship, motor, and rail services and possibly air, with through routes, under one bill of lading, through door-to-door service with minimum handling, stowing, packing, and repacking offers an opportunity for less costly transportation. A coordinated joint board of the several regulatory agencies specializing in the various forms of transportation would be a means to accomplish this.

In conclusion, the suggested methods by which rates in the non-contiguous domestic trades might be reduced have been offered in the light of the assumption indicated in the program for study of this problem that a reduction in ocean freight rates by the carriers is required in order for the areas involved to survive and develop their economies, even though the ocean freight rates were reduced below a compensatory level. As you will note, the ready solutions having the earliest and most effective results would call for substantial expenditures by the Federal Government.

It is our understanding that the program for the study of this problem contemplates an exhaustive review to make certain that any action which is undertaken will accomplish its purpose. In this connection, we would like to point out that there are many factors which go to make up the cost of goods to the ultimate consumer. Among these would be the original procurement cost, insurance and financing charges, the cost of moving the commodity to sea-board, sometimes receipt and storage at seaboard and the cost of moving to shipside, ocean transportation, receipt and storage costs at port of unloading, onward transportation to point of final destination, as well as wholesale and retail markup. Many of these cost factors are unregulated.

It is assumed that before any conclusion is reached on the various alternative ways of lowering freight rates, an effort will be made to settle definitively the relationship of the ocean carrier's charges to the ultimate consumer costs. It would be unfortunate if drastic legislative changes were to be made in our shipping laws or a new program of Government subsidization were to be undertaken only to find that the effect of such changes did not provide the desired result because the ocean transportation factor was not as significant a factor

in consumer costs as anticipated or because the savings represented by reduced ocean transportation costs have been partially or wholly absorbed by the unregulated factors.

It may be that this study will indicate the essentiality of an adjustment in freight rates in order to assure the economic stability of the offshore States and possessions but without a thorough study, there will always be an area of doubt and of danger that the steps taken will not achieve their objective.

We will be most happy to assist the committee in any way that we can.

I might add, Senator, that this statement, although it doesn't show here, it has been cleared by the Department of Commerce and the Bureau of the Budget.

Senator BARTLETT. Thank you, Mr. Chairman.

Your words of caution that we should not move perhaps too far too soon will assuredly be heeded by the committee in respect to the hearings which are now underway, because actually our whole purpose is to determine where we are, why, where we may be headed, how our destination will appear to us once we are there; and to arrive at any answers, of course, we must be fortified with all the data which may possibly be accumulated.

Mr. STAKEM. As you know, Senator, the Federal Maritime Board has asked its Deputy General Counsel to be liaison with this committee in this study, so that anything that we can do to assist we will certainly do.

Senator BARTLETT. I am very glad to hear that, because I was just about to make that request of you.

I think that some of the information which you have properly suggested here, the committee not only should desire, but require. Perhaps it can come from the Federal Maritime Board more appropriately and more speedily than from anywhere else.

Now, in your statement, Chairman Stakem, I find these words on page 2, after you had said that if it is discovered that subsidization is necessary, there are a number of alternate approaches which might be taken, and you said you are not prepared to make any recommendations at this time.

May I ask this: Do you foresee that the Federal Maritime Board will, at a later date during these hearings or before the committee makes final determination, present to the committee specific recommendations?

Mr. STAKEM. Yes. I was, before leaving the stand, going to suggest that we will follow the hearings very closely, and as you come down toward the end of the hearings we will be very happy to come back and give you the benefit of what we can.

Senator BARTLETT. Excellent.

On that same page, namely, page 2, you were referring to the alternate of applying a construction differential subsidy for this trade. Actually, would you not agree with me that if that, and that only, were done, the effect might be for even higher rates?

Mr. STAKEM. Yes; that is a fact, Senator.

When you compare the base for the ratemaking purposes of the present ships against what the new ships would be even with construc-

tion subsidy, you would still have a higher rate base, which would not result in reduction.

Senator BARTLETT. It would give the trades fine new ships, but wouldn't go to the heart of the problem that agitates us now: bringing down the cost of living in those places by reason of lower transportation rates.

Mr. STAKEM. I agree.

Senator BARTLETT. On page 3 of your statement you refer to a variation of the construction subsidy method, whereby replacement ships might be built for the Government's account.

May I ask you if this has ever been tried in this country, or elsewhere?

Mr. STAKEM. Yes. We have built ships for Government account and later sold them to the industry. I think a classic example that first comes to mind is the Mariner ships that were built by the Maritime Administration at the time of Korea. Admiral Cochrane was Chairman at that time, and 35 Mariners were constructed for Government account. Several of them were later turned over to the Navy, but the great majority of them were eventually sold to the shipping industry, and all of those are now plying the Pacific Ocean trades.

Senator BARTLETT. How has that program worked, satisfactorily or otherwise?

Mr. STAKEM. It has worked satisfactorily. It requires, initially, the outlay of the complete cost of the vessel by the Government and then a mortgage backed with a small downpayment by the operator. In the last years, the emphasis has been put the other way, for the Government to seek its appropriations for ship construction only on the basis of our participation in the costs with an insurance guarantee on the part of the Government for private financing of the ship-owner's costs.

Senator BARTLETT. May I ask this, in that connection: again, if this program were adopted, this particular one, it would be a means to get ships to the given trades; but it wouldn't necessarily operate to reduce rates, would it—

Mr. STAKEM. No—

Senator BARTLETT. Or to keep them at existing levels?

Mr. STAKEM. No; unless, as I pointed out in the statement, the mortgage payments were tied to the earnings of the ship, and to be collected only after a certain percentage on investment of the company—what we call the earnings debenture plan here.

Senator BARTLETT. This might or might not, then, seek the objective which is the main concern of the committee at this time?

Mr. STAKEM. Yes. It is something to study. Whether it would be a cure-all I am not prepared to say.

Senator BARTLETT. Going to your second presentation, operating differential subsidy, Mr. Chairman, why do we have a shipping subsidy program?

Mr. STAKEM. Because without it the American flag would disappear from the seas in foreign trade.

Senator BARTLETT. If Matson serves, as I believe it does, Australia and other areas in that part of the globe, and a freighter sets out for Australia and has, we'll say, 500 tons for discharge at Honolulu, how, in an accounting manner, do you approach this problem?

Mr. STAKEM. A ship that is operated with operating subsidy, that does engage in some leg of the domestic trade, must repay to the Government a certain cost of the ship—I am talking about a construction subsidy ship now—must pay to the Government a certain amount representing the percentage of the domestic cargo to the total cargo.

I would be very happy to put into the record at this time a complete statement as to how this formula works out.

Senator BARTLETT. Very well. We appreciate that.¹

How about the operating subsidy? Granted that the bulk of the cargo on this particular ship is going to Australia, but some fraction of it is discharged at Honolulu?

Mr. STAKEM. There is no recouping of operating subsidy on the basis of the percentage of the utilization for domestic as against the foreign.

Senator BARTLETT. The company would not, then, be paid for this 500 tons landed in Hawaii?

Mr. STAKEM. Yes. The ship is operating in the domestic trade, or in the foreign trade, and it would be paid a subsidy based upon its competition in that trade, and there would be no reduction in operating subsidy by reason of a small portion of the ship being used in the domestic trade, if it had certain rights given to it by the Board.

Senator BARTLETT. You don't even inquire into the percentage of traffic that might be diverted to domestic areas along the route, because of an understanding that it is always fractional?

Mr. STAKEM. I am subject to correction, Senator. My General Counsel tells me that there is a recouplement on both construction and operating subsidy for that portion that goes in the domestic trade.

Senator BARTLETT. The accounting procedures and techniques must be rather involved in respect to both categories.

Mr. STAKEM. They are. And, as I promised, I would put a statement in the record as to how that works out in actual practice.

Senator BARTLETT. Thank you.

Well, pursuing that same line of inquiry a bit further, the subsidy, as you stated, is provided so that we will have a fleet in being in time of national need.

Mr. STAKEM. Yes.

Senator BARTLETT. And you say that if a subsidy, an operating differential subsidy, were to be applied to the ships serving offshore areas, this would represent a drastic, and I quote: "a drastic departure from the principle envisioned by this subsidy." Insofar as I am concerned, that is a factual statement.

But could it not be said, Mr. Chairman, that with practically all ships having disappeared from the coastal and intercoastal trades, and with many ships having disappeared from the offshore areas, substitution having been made by barges, we fail in whatever measure of need there may be to keep in being an operating fleet that might be just as important, surely, as those American carriers engaged in foreign trades?

Mr. STAKEM. I agree with that, and I think our statement is predicated upon the fact that we think the operations in both the domes-

¹ See supplemental information from Mr. Stakem, p. 76.

tic, coastal, and intercoastal and offshore trades are important, and we should take all means to keep these people in business.

Senator BARTLETT. The subsidies on our foreign trade weren't put into effect to help the carriers; they were put into effect to make contributions, ship contributions to the national defense, when and if the need arose; right.

Mr. STAKEM. Actually, the subsidy is based upon two principles—one, that these ships are necessary for national defense purposes, and also that they are necessary for the economic well-being of the Nation.

I would say there are two bedrocks written into the policy statement of the 1936 act on shipping—that we need them from an economic point of view, as well as national defense.

Senator BARTLETT. Yes.

On page 4 of your statement you referred to subsidization by Canada to coastal and inland water carriers to provide services to outlying communities. We have never done anything of that nature, have we, in our maritime history?

Mr. STAKEM. No, we have not.

Senator BARTLETT. Do you know, from what you may have heard, read, or otherwise learned, how this program works out so far as Canada is concerned?

Mr. STAKEM. I do not have the exact details with me, but it may be that we could expand the statement, perhaps, more on what we know. I would be very happy to take a look at the records, and if we can supplement it in that area we will.²

Senator BARTLETT. There may be nothing useful and comparable that would come out of such a survey, but if anything does, we would appreciate having it.

Mr. STAKEM. Yes.

Senator BARTLETT. On that same page, page 4, you suggested that the proposition of granting a direct subsidy ought to hinge on the validity of the case that could be made that economic development of these several areas is, or will be, hindered by high ocean freight rates. Later on, I believe, you pointed out that many other factors must enter in here.

In your own view, if you care to express it—and perhaps you are not in a position now to do so—do you believe that high ocean freight rates have a material bearing upon the economic prosperity of Puerto Rico, Alaska, and Hawaii?

Mr. STAKEM. The question is broad, Senator, and I don't want to answer it specifically. I do think that the freight rates do have a bearing. Now the extent of the bearing is something that perhaps will be developed in these hearings.

Senator BARTLETT. Well, going back to the subsidy, we all recall that for a time after the war the Government-owned ships were chartered below the regular charter rates to serve Alaska, and this was a form of subsidy, was it not?

Mr. STAKEM. Yes; on a very low charter rate, as I remember.

Senator BARTLETT. And I remember it had a very useful and even necessary effect at that time—necessary so far as the area was concerned.

² See supplemental information from Mr. Stakem, p. 77.

You said on page 5 that another alternative would be furnishing by the Government of ships at minimum charter hire rates, which ties in with that charter arrangement for Alaska some years ago.

May I ask you, Mr. Stakem, if this were deemed appropriate, does the Government have suitable ships for these several trades in readiness, or comparative readiness?

Mr. STAKEM. I have in mind, Senator, that in connection with the total replacement program, that we do receive into the reserve fleets a number of vessels that may be useful for this purpose.

In that connection, it might be of interest to the committee if we gave you a breakdown of what ships there are in the reserve fleets that might possibly be used for that, the better classes of ships—I am not thinking of the Liberties—the better classes of ships.³

Senator BARTLETT. Thank you.

What authority does the Board now possess, if any, to charter such ships at attractively low rates, or attractive rates?

Mr. STAKEM. I believe that we do not have authority to charter without a public hearing to show the nonavailability of vessels suitable—suitable vessels in private hands.

Senator BARTLETT. The authority is in law, though? You have the authority by existing law, after hearings?

Mr. STAKEM. Yes, after certain hearings.

Senator BARTLETT. Now, Mr. Chairman, you urged most seriously and most strongly against any amendment of the cabotage laws which would permit foreign ships to provide these services. I don't know what the general view is regarding this, but I know for my part I agree with you thoroughly. It isn't going to be done, and if it were done, as you suggest here the effects might be adverse rather than beneficial, because there are situations beyond the control of the Federal Maritime Board.

Mr. STAKEM. That is right.

Senator BARTLETT. I have an illustration of this.

We all know that the ocean distance between Alaska and Japan is much less than between Japan and any other American ports. But recently a conference agreement was entered into, solidified, certified, and is effective, whereby freight rates from Japan to Alaska, and vice versa, are much higher than from Japan to other American ports. So the mere entrance of foreign shipping into these areas certainly is not guaranteed to solve any problems, and, as you appropriately stated, they might go only to those ports furnishing the greatest volume of traffic.

Mr. STAKEM. Yes.

I had in mind, Senator, Alaska particularly, where if you did allow foreign liners into the trade, you might find that they would go to one or two ports, but—and I once made a count for my own information as to how many different places in Alaska that Alaska Steam goes, and I think it was somewhere between 70 and 90. I didn't know there were that many places a large oceangoing ship could visit in Alaska.

Senator BARTLETT. In a coastline comprising 34,000 miles, there are many more they could go to. There might not be any people there, but they could go.

³ See supplemental information from Mr. Stakem, p. 80.

Mr. STAKEM. But I don't think there is any doubt about it, if you repeal the cabotage laws and expected to get service to many, many of these ports, you wouldn't; this would not result.

Senator BARTLETT. Now on page 6, these were your words:

In two world wars the domestic fleet has been an important nucleus which was in immediate operating condition and available to serve military and naval needs. The necessity for their continued existence seems beyond doubt.

And yet it is true that in the Alaska trade—about which I know somewhat more than the other trades—ships are being increasingly replaced by barges, and they perform a very useful service. I don't know whether or not similar barges could be used to Hawaii and Puerto Rico; but, to the extent they are in any of these areas, the availability of a merchant fleet in being for national defense decreases; and, of course, that is one of the prime considerations before this committee now, in seeking to make a determination as to what, if anything, should be done concerning the overall problem, because we know that not only intracoastally and intercoastally, but also in these off-shore areas, the number of ships does not compare with the number previously in service.

In respect to certification, Mr. Chairman, is there any way that you could inform the committee whether certification would go only to ships, or would they also be applied to barge operations?

Mr. STAKEM. I had not given much thought to that particular point, Senator, but it would seem to me that it might well be, if the certificate route was decided upon, advantageous to the trade, that there would be certificates for barge operations as well as ship operations.

That is an off-the-cuff statement, without any opportunity to think about it.⁴

Senator BARTLETT. We shall not seek to hold you to that statement.

Now is it not true, Mr. Chairman, that these carriers serving the offshore areas have produced some of the most significant and useful developments in the post-World War II period of the history of U.S. maritime transportation, modernization, container-type operations and the like? Is it not the case that practically all significant advances in those directions have come in these trades?

Mr. STAKEM. It very definitely is true, and we are just beginning to see the expansion of what has developed in the domestic trade, in the foreign trade, and I have in mind the container ships which Grace Line is trying to get into the Venezuela trade as an example of that.

Senator BARTLETT. And it follows automatically, I suppose, that rates would be even much higher than they are if these improvements had not been made?

Mr. STAKEM. I think that is true.

Senator BARTLETT. Now you mention on page 8 that, if subsidies are provided in whatever form they might be, substantial expenditures will be required by the Federal Government, and we must assume that is the case.

The question here will be, will it not, twofold: one the well-being of the people of Puerto Rico, Hawaii, Guam, and Alaska, all of whom are Americans, and, two, national defense needs? The cost has to be contrasted with those two factors.

⁴ See supplemental information from Mr. Stakem, p. 81.

Mr. STAKEM. I agree with that, Senator.

Senator BARTLETT. Now you have mentioned at some length, and appropriately, that what it costs to ship a pound of onions from New York to San Juan, or from San Francisco to Honolulu, or from Seattle to Seward is not the whole cost which the consumer pays, that there are many other elements which enter in here.

I am particularly hopeful, Mr. Stakem, that in the assistance you were good enough to promise the Board will give the committee, we shall enter very directly into that entire situation and see if we can get any approximate breakdown as to the importance of these various elements.

Mr. STAKEM. Yes.

Senator BARTLETT. And we will want to know ultimately, or to decide, on the basis of the information which may be available, how much other costs can rise simply by reason of an ocean freight increase. Sometimes these things mushroom.

Mr. STAKEM. I would like to think, Senator, as the operators in these trades are brought before this committee, that if they have any information along this line, to assist the record they should be asked to supply it.

There has been no cost study, as such, in Alaska or Hawaii or Puerto Rico by the Federal Maritime Board, and it might be quite an undertaking, from a manpower and cost point of view, to go into that deep a study. Certainly you couldn't do it within a week.⁵

Senator BARTLETT. That is why I said we may have to depend upon approximations here, because I don't believe these factors will have been susceptible of precise definition. Our conclusions may have to be somewhat general. However, we have a jesting remark made in Alaska ever since I was a youngster, that the barber charges the price he does for a haircut—which has now reached \$2.50 in some cities—because of the high freight rates. Well, of course, there is a semblance of truth to that. All the elements that enter into the higher cost of living in Alaska hit the barber as well, and he has to get more for clipping hair.

Before Mr. Grinstein proceeds, I note the presence in the room of the junior Senator from Alaska, and if it is agreeable to you—as I know he is so busy with another hearing at the moment—perhaps Chairman Stakem will step aside until Senator Gruening has delivered his statement, and then we will return to you.

STATEMENT OF HON. ERNEST GRUENING, U.S. SENATOR FROM THE STATE OF ALASKA

Senator BARTLETT. Senator Gruening, we are indeed happy to have you.

Senator GRUENING. Mr. Chairman, I am grateful for this opportunity and just to keep the record straight, since the last 10-percent increase was levied, the price of haircuts in Fairbanks has risen from \$2.50 to \$3, so that there is apparently a definite relationship between the high cost of transportation and the cost of haircuts which you pointed out.

⁵ See supplemental information from Mr. Stakem, p. 81.

Senator BARTLETT. You flabbergast me, I had not known of this recent development.

Senator GRUENING. I wish to thank you, Mr. Chairman, and this committee for giving me the opportunity to present once again, a case for the State of Alaska in connection with the very useful study of offshore shipping in which you are now engaged.

Mr. Chairman, during the last decade, waterborne freight rates to Alaska have increased 56.4 percent. The cost of operation, the legitimate costs, had increased by that percentage. The State is, even now, fighting a 10-percent increase allowed by the Federal Maritime Board to go into effect more than a year ago over the opposition of the State. Even if this increase should ultimately be denied by the Board, its inflationary effects have already been imbedded in the economy of Alaska, and, even should shippers be refunded the excess costs they may have been charged there is nothing that can effectively roll back the higher costs which are now a part of every commodity purchased in the State. For the consuming public will have paid the higher cost on every commodity as a result of the freight rate increase even if the refund is made to the shippers.

The State of Alaska must find a solution to this problem of intolerable freight rates. The unbelievably high costs of living in Alaska have been an economic phenomenon recognized and made the subject of comment by one study after another. That the unduly high cost of living is a direct result of the high costs of waterborne transportation is unquestioned.

Within the last week the freakish effects of high living costs resulting from high transportation costs have been manifested in yet another blow to the Alaska economy. For many years we had looked forward to the enactment of Federal legislation which would provide assistance to our sorely pressed public schools—as much in need of Federal help in Alaska as anywhere in the United States. Imagine our dismay to find that, when the funds would be apportioned under the plan proposed for Federal aid to education by the President, Alaska would receive the minimum amount available to a State. The reason lies in that the plan of distribution is calculated to provide the largest amount of help to the poorest States. But, because in Alaska wages have to be high to provide a living wage because of the high cost of everything, it appears as though Alaska were a wealthy State. This is, of course, a distortion of the facts concerning the economy of the State, and one we hope to remedy before the education bill is finally enacted. However, this is one more occasion on which the desperate need to reduce transportation costs is once again brought to the fore.

The plight Alaska suffers results from the nature of the Alaska water commerce. This is an abnormal kind of trade which is, in reality, interstate commerce, but lacks the controls of an effective regulatory agency and/or the existence of other, competitive forms of transportation available to other States of the continental United States.

While it is interstate commerce, the nature of the trade is, in reality, that of foreign shipping. This gives rise to an anomalous situation in which the Alaska trade is limited to domestic carriers with the same problems of operation as carriers in the foreign trades, but who have none of the advantages accruing from construction and operat-

ing subsidies which might make possible a saving to shippers and consumers, if such subsidies should be granted in combination with adequate regulation. While this is a situation shared in common with the other offshore areas of Hawaii and Puerto Rico, it is exaggerated in Alaska by the lack of any subsidized carrier for which Alaska is an intermediate point, thus providing the advantage which might be obtained by the availability of transportation at costs competitive with foreign shipping.

The result of this is that the application of national defense policies designed to strengthen the American merchant marine by the exclusion of foreign carriers from domestic trade causes the citizens of the offshore areas to subsidize this policy by paying increased transportation costs, thus bearing an unequal burden of national defense not shared by other citizens of other parts of the United States.

This, then, is our problem. It is to find solutions for the problems of Alaska, as well as for the other offshore areas that this committee has undertaken the study with which we are now concerned.

It is my belief that it is, first of all, necessary to establish a new attitude on the part of the carriers that serve my State of Alaska and on the part of the Federal Maritime Board which presides over their rate increase applications. It is necessary that the carriers and the Board adopt an attitude of concern for the public welfare which at least matches the zeal for improving the financial position of the carriers. At present there is no policy of the carriers or the Board which clearly recognizes the interests of the public. At least, the effects upon Alaska of the operations of the carriers and the administration of shipping affairs by the present Federal Maritime Board and its predecessors have not given indications that consideration of the public interest is of concern to either.

While this is a generalized objective, I would like to suggest some specific approaches which might be followed to obtain regulatory policies for the offshore areas which would take account of the needs of the people served.

A. Changes in statutory standards of ratesetting: Much of the difficulty we face can be remedied by enactment of statutes which would insure the regulation of rates charged by carriers on a basis which would not only provide a fair return to them, but, also, a fair break to the consumer.

(1) Articulation of standards: The present statutory requirement that rates set for the offshore trades must be "just and reasonable," is, of course, the definition supplied for other forms of transportation regulation. For the water transportation trade, however, the Federal Maritime Board and its predecessors have never developed progressive standards and procedures for ratesetting which other agencies have applied and which can make a very great difference in determining whether the rates paid by the public are truly "just and reasonable" or otherwise. A precise statutory definition of the standards to be applied in determining the rates to which carriers are entitled would eliminate many of the difficulties faced by areas they serve.

(2) Realistic accounting of assets, investments, and costs: The public is entitled to an honest analysis of carrier earnings in the determination of rates to be assessed. The ratepaying public should not be charged for the acquisition by stockholders of profitable items of property not used in the trade and from which it derives no benefit.

That is the case with the principal maritime carrier from the 48 States to the 49th, namely, the Alaska Steamship Co. The facts which will be brought out in due course reveal financial practices which cannot be justified as part of a service affected with public interest.

B. Responsibility of carriers for maintenance of efficient fleets: In connection with the general need for the development of an attitude of responsibility to the ratepaying public, the carriers should be required—as much in their own interests as that of the public—to maintain an efficient fleet, constantly reconditioned through construction of new vessels and repair of the old so that service can be maintained on as economical a basis as possible. Certainly, carriers should not be allowed to charge unrealistic depreciation costs to the ratepayer while siphoning off the depreciation funds for profitmaking operations of stockholders to the neglect of the fleet.

C. Reformation of the organization and procedures of the Federal Maritime Board: A basic cause of difficulties faced by the public served by the offshore carriers has been the organizational structure and procedures of regulation followed by the Federal Maritime Board and its predecessor agencies.

(1) Schizophrenic organization: An organizational malady of the Federal Maritime Board to which attention has been repeatedly called, and to which reference was made in the recent report to the President by Dean James M. Landis, is the schizophrenic nature of its organization. The Federal Maritime Board and the Maritime Administration, both located within the Department of Commerce, are both agencies concerned with oceangoing shipping. But the nature of their functions is—or should be—quite different.

In theory, it would appear that the function of the Federal Maritime Board is to regulate and control rates, services, practices, and agreements of oceangoing common carriers by water. However, as the current Government organization manual states:

The Federal Maritime Board and Administration foster the development and encourage the maintenance of a merchant marine.

In other words, the Federal Maritime Board must promote and encourage development of the same industry it is expected to regulate at the same time.

Moreover, the schizophrenia here is intensified by the fact that the Maritime Administrator, whose clear duty is to promote the growth of the merchant marine, is also Chairman of the Federal Maritime Board that regulates operations of the very same merchant marine.

It is therefore virtually impossible for the same agency to both promote development of an industry and, at the same time, regulate it, if the regulating is to be of any effect, and in the public interest.

Regulation, by its very terms, involves restriction of some aspects of carrier operations. Almost inevitably, a case can be made that regulation—for example, failure to allow rate increases—inhibits growth of the industry.

With the best intentions in the world it seems impossible that the Maritime Administration can, on the one hand, work to strengthen and promote the merchant marine, and on the other hand, act to restrict it.

As noted in the Landis report, a related and important factor in the organizational problem of the Federal Maritime Board is that

it is organizationally located within the Department of Commerce. While recognizing that the Board operates independently of the Secretary of Commerce—except that it is guided by policies of the Secretary in awarding subsidies—it is, nevertheless, dependent on the Department for assignment and payment of personnel, for budgetary allocations, for office space, and other housekeeping services. The effect of this relationship must tend to exert controls over the operation of the Board.

2. Failure of the Maritime Board and Administration to take positive action for improvement of American merchant marine: Although, as noted above, it is a responsibility of the Maritime Administration to promote the welfare of the American merchant marine, it is apparent from the well-publicized plight of domestic shipping that the agency has not carried it out. Imaginative solutions to problems of dwindling business, overage fleets, and costly operations are demanded, but have been disastrously lacking.

It is not sufficient that the only remedy apparently known to the Maritime Board and Administration for increasingly difficult problems of maritime carriers is the application of the balm of higher rates. While this remedy gives momentary relief to carriers it does nothing to cure basic ills of the industry and it is disastrous to the people of Alaska overburdened with steadily mounting living costs. The higher rate remedy to all ills also obviously wreaks serious damage on an economy chiefly dependent on water transportation as is Alaska's.

The plight of Alaska—saddled with ever-increasing freight rates of the water carriers on which it is totally dependent—has been known for generations. Yet there have never come from Board, the Maritime Administration, or its predecessors any suggestions whatever as to solutions for this problem.

Aside from the general public interest in a healthy merchant marine, aside from the interest of Alaska in securing an economical means of water transportation, the water carriers themselves have long suffered from this lack of imaginative, dynamic programs for improvement of the merchant marine.

3. Inordinate length of hearings: The inordinate length of time required to complete adjudicatory proceedings before the Maritime Board is a procedural defect the Board has in common with other regulatory agencies. Recommendations of the recent Landis report on this to President-elect Kennedy are, with distinctions as to specialized aspects of maritime regulation, applicable to the Federal Maritime Board.

4. Regulation of reporting procedures of carriers: Associated with the need for shortening the time of proceedings before the Board is the recommendation that the Board be empowered to require the carriers to submit reports containing specified information necessary to determine rates.

At this time one reason for the exceptional length of time required for hearings lies in the fact that masses of data concerning the economic status of a carrier must be elicited during the course of the hearings. The data needed are not available in the form of published documents or records readily available at the Board. Months of time required to compile the facts needed to show the true financial status of a carrier could be eliminated if carriers were required to file periodic

reports of information of the character now sought by time consuming discovery processes.

5. Need to extend time of rate increase suspension: At present the Maritime Board may suspend the effective date of a rate increase for a period of 4 months. As noted above, the existing procedural delays and the need for extensive discovery of facts to prepare a case make it impossible to obtain a decision from the Board during the suspension period. If the time during which rates may be suspended is lengthened and the adjudicatory process is shortened, it could be possible to achieve a decision by the Board within the period of rate suspension. This would, of course, be of exceptional benefit to carriers and consumers alike in view of savings in money that would accrue and numerous other advantages flowing from an early determination of issues in dispute. I am pleased to point out that the Senate has now passed the bill, S. 804, which would extend the time during which rate increases may be suspended from 4 to 7 months. I hope this measure will soon pass the House and be enacted into law.

In conclusion, I might suggest that it would be useful to extend to the offshore carriers the provisions of the national transportation policy adopted by Congress in 1940 to apply to transportation subject to the regulation of the Interstate Commerce Act. To the carriers with which we are here concerned could equally well be applied the policy to—

provide for fair and impartial regulation * * * to promote safe, adequate, economical, and efficient service and foster sound economic conditions in transportation * * * to cooperate with the several States * * * all to the end of developing, coordinating, and preserving a national transportation system adequate to meet the needs of the United States, of the postal service, and the national defense.

Senator BARTLETT. Thank you, Senator Gruening. I hope you have an ample supply of mimeographed copies of this statement, because I suspect there will be an extraordinary demand.

Senator GRUENING. There is an ample supply, Mr. Chairman, and they are available to the press and public and the other members of the committees, as well as to the carriers.

I thank you, Mr. Chairman.

Senator BARTLETT. Thank you very much.

FURTHER STATEMENT OF HON. THOMAS E. STAKEM, CHAIRMAN, FEDERAL MARITIME BOARD AND MARITIME ADMINISTRATOR

Senator BARTLETT. Chairman Stakem, I want to ask you a question or two, based upon Senator Gruening's statement.

Mr. STAKEM. Yes, sir.

Senator BARTLETT. What regulatory requirements and/or privileges does the Federal Maritime Board have under the law, if that question is comprehensible?

Mr. STAKEM. The Federal Maritime Board has authority under the law to regulate in the foreign trade and also to regulate in the offshore domestic trade.

We have authority to set the measure of rates in the domestic trade. We do not have that same authority in the foreign trade. We can only knock down the rate if we find it to be detrimental to the commerce of the United States.

Senator BARTLETT. What standards, under the law, guide the Federal Maritime Board in its determinations?

Let me be a little clearer on that. Does the chief requirement have to do with the financial solvency of the particular carrier, or are you required to inquire constantly into the public interest as well?

Mr. STAKEM. I think that we are required to do both, to take the financial position of the carrier into consideration as well as the economic impact of the rates themselves, and I am thinking of the domestic trade.

Senator BARTLETT. As a matter of practice, would you say that these two goals have had equal consideration historically by the Federal Maritime Board and its predecessors?

Mr. STAKEM. Let me speak only for myself. I believe that I have tried to, in the decisions since I have been on the Board, weigh both factors in our ratemaking proceedings.

Senator BARTLETT. Would you care to comment, Mr. Chairman, upon the statement made in the Landis report in these words, and I quote:

But in its quasi-judicial aspects it (Federal Maritime Board) suffers from a lack of settled public procedures and standards of decision, thus resulting in the exercise frequently of arbitrary powers by the staff. It places too much emphasis on bureaucratic details to the disregard of matters of large public importance. A fog of secrecy also surrounds many actions of the Board and no articulate standards seem to have developed with respect to ex parte presentations. Each agency, however, requires separate consideration and individual remedial action.

Mr. STAKEM. Far be it from me to criticize the Coordinator for the lack of settled public procedures and standards of decision. I do believe that it is intended that a fuller and broader review of the agencies is intended by Mr. Landis.

Certainly, as to the reference to secrecy, I think the Federal Maritime Board operates in a kind of a glass bowl. I am not aware of any secrecy in connection with our proceedings. I have personally talked to Mr. Landis since he assumed office, and we have promised him the fullest cooperation in endeavoring to bring about more expeditious proceedings before the Board and to conduct whatever inquiry toward better management is necessary. And I believe that Mr. Landis is satisfied that we are straightening out our procedures and that we have more timely decisions, and less problems in this area in the future.

Senator BARTLETT. Are we to infer, then, that they weren't timely before, and needed straightening out?

Mr. STAKEM. I think there were considerable delays in proceedings before that with a little more push we could have done a quicker job.

Senator BARTLETT. Yesterday's papers, I believe, had a story that came as a surprise to me, which they carried from Washington that the Atomic Energy Commission had captured or recaptured control from the staff. The story went on to say that the Commission has been operated under staff jurisdiction for goodness knows how long, and a great victory was won, because the men who were appointed to run the Commission are, according to the paper, going to run it instead of the staff.

This quotation, to which I have referred from the Landis report, makes an allegation regarding the staff powers of the Federal Maritime Board. Do you have any comment on that?

Mr. STAKEM. My only comment is that the staff of the Federal Maritime Board does not run it; it is run by the three Board members.

Senator BARTLETT. You deny this?

Mr. STAKEM. Yes.

Senator BARTLETT. In Senator Gruening's statement it was said that the Secretary of Commerce guides the Federal Maritime Board in respect to the award of subsidies. To what degree does his control run in that area?

Mr. STAKEM. The Secretary of Commerce has policy guidance in the area of subsidy, that is, the construction and operating subsidy. The Federal Maritime Board is completely independent in the matter of regulation under the 1916 act. But the language of plan 21, adopted by the Congress in 1950, does give the Secretary of Commerce authority to give policy guidance in the area of subsidy.

Senator BARTLETT. Do you have to follow his recommendations?

Mr. STAKEM. The law is not clear on that point. Lawyers will differ on it. It has been frequently argued that the Secretary of Commerce could state a position but it would not necessarily be binding on the Board. I can only say that in this area of policy guidance in the 5 years that I have been on the Board that we have had no difficulties with the Department of Commerce.

Senator BARTLETT. An associated comment made by Senator Gruening ties in with this. What if the Secretary of Commerce would make a recommendation regarding a subsidy and you would disregard it; could he cut your paycheck off?

Mr. STAKEM. That I doubt, since it is a term appointment. He probably could—again, we are speculating. The designation of the Chairman can be made by the President, at his pleasure, and there are certain areas in which a Cabinet officer could operate, if we reached a point of ultimate disagreement on major points.

Senator BARTLETT. But, more seriously, the Secretary of Commerce does have budgetary control over your operations?

Mr. STAKEM. Yes. The budget for the Maritime Administration, which is the policing arm of the Board, in the subsidy field, as well as the Board's budget with respect to personnel, goes through the Department of Commerce, is cleared there, before it goes to the Bureau of the Budget.

Senator BARTLETT. Senator Gruening said, and I quote:

The plight of Alaska—saddled with ever-increasing freight rates of the water carriers on which it is totally dependent—has been known for generations. Yet there have never come from the Board, the Maritime Administration or its predecessors any suggestions whatever as to solutions for this problem.

Now, my question is not intended to be a goading one. I want information.

What are the responsibilities in this field of the Maritime Board and the Maritime Administration?

Mr. STAKEM. First, let me say that I think Senator Gruening overstated his case. I don't agree that the Maritime Administration and the Federal Maritime Board have not offered suggestions in the domestic shipping. I feel that under the law that it is our responsibility to foster an American merchant marine in the domestic area. And I would be very happy to list chapter and verse of the number of recommendations and areas of action that we have taken over the years.

Senator BARTLETT. I wish you would do that and concentrate exclusively perhaps upon the so-called offshore areas.

Mr. STAKEM. Yes. I would also like, with the Senator's permission, to submit a letter from the Board in reply to at least certain parts of Senator Gruening's statement. I think it was most critical of the Federal Maritime Board and I am sure that we would like to make a supplementary statement for the record on a number of points raised.⁶

Senator BARTLETT. Permission granted.

Mr. Grinstein?

Mr. GRINSTEIN. Mr. Chairman, I take it it is your view the cabotage restriction is supported mainly on national defense reasons?

Mr. STAKEM. Yes, sir.

Mr. GRINSTEIN. Has the Department of Defense ever made a determination as to how many ships are required in the domestic offshore trade—Alaska, Hawaii, Puerto Rico?

Mr. STAKEM. This is a continuing study on the part of the Department of Defense with Maritime as to the need of ships, pointed to national defense. It has been a long time since I have looked at that study and I don't recall whether it is broken down into the foreign and domestic. We would be very happy to submit something for the record on that.⁷

Mr. GRINSTEIN. In other words, though, it is your recollection that the Board does have some directive from the Department of Defense setting up certain levels of ships required in this trade?

Mr. STAKEM. Yes, and this is a continuing thing, and we constantly consult with the Department of Defense in this area. I don't believe, if I were to take a guess, that it is broken down into domestic as against foreign, but we will look at it from that point of view.

Mr. GRINSTEIN. When I said ships, I meant American-flag ships.

Mr. STAKEM. Yes, sir.

Mr. GRINSTEIN. In response to a question from Senator Bartlett, you said the Federal Maritime Board in a rate proceeding looks both to the needs of the carrier, as well as the economic impact on the area concerned. On page 4 of your statement you said that trade promotion or cost-of-living subsidy to reduce costs would warrant serious consideration only if a valid case can be made that such development is being stifled by high ocean freight rates.

Has the Board made any such determination along these lines?

Mr. STAKEM. I don't think I get the thrust of your question.

Mr. GRINSTEIN. Well, when the Board is balancing these two considerations, the needs of the carrier and the impact of increased rates on the area concerned, let's say Hawaii, has the Board made a determination that development in Hawaii is being stifled by Hawaiian ocean freight rates?

Mr. STAKEM. No, I don't think so, in just those terms. I think that, however, with a review of the Board's reports, it will show that the economic impact of the rates were taken into consideration in the ultimate decision made.

Mr. GRINSTEIN. Have you made any determination as to approximately how far rates could go without too great a burden on the offshore area?

⁶ See supplemental information from Mr. Stakem, p. 81.

⁷ See supplemental information from Mr. Stakem, p. 82.

Mr. STAKEM. Not specifically.

Mr. GRINSTEIN. Has the Board ever made a general investigation of domestic offshore shipping, both with respect to increasing rates and a projection or the burden it would impose on the economy generally?

Mr. STAKEM. There was a transportation study several years back on the domestic trade. I would be very happy to furnish a copy of that to the committee.⁸

Senator BARTLETT. That will be accepted, Mr. Stakem, and will be incorporated in the committee's file.

Mr. GRINSTEIN. Mr. Chairman, what is the Federal Maritime Board permitting as a fair return to the carriers involved in these trades? Is there any percentage level, 5 or 7 percent?

Mr. STAKEM. I don't want to get too deeply into the allowance because of the cases that are pending now that will come to the Board for decision, but I can say this, that the Board in the most recent Puerto Rican case, docket 807, attempted a complete reevaluation, and to restate a rate basis in that case that would be meaningful in this trade. We would be very happy to submit for the record the elements considered by the Board in this case.

Mr. GRINSTEIN. Would it be your view, Mr. Chairman, for costs, both operating and replacement costs, will stabilize or continue to mount over a 5-year period?

Mr. STAKEM. It is a fact that—you are talking of replacement cost of ships?

Mr. GRINSTEIN. Yes.

Mr. STAKEM. The Board has been very happy to see the reduced costs of ship construction in this country. We have had two bids that have gone even lower than the staff estimate of what the cost would be. I think the answer is hungry shipyards.

From the standpoint of the replacement of ships, we like to see this trend and we would like to build a lot more at the present going prices.

Mr. GRINSTEIN. What about operating costs? Is it anticipated they will stay on an even keel or decrease or mount?

Mr. STAKEM. I don't see any immediate hope for a decrease in the operating costs of vessels under the American flag. As to the guess of increasing, I would rather pass that.

Mr. GRINSTEIN. Are there any foreign ports a comparable distance from the United States as Hawaii, say, served by subsidized carriers?

Mr. STAKEM. You are contrasting the distance between, say, California and Hawaii with some of the foreign areas that would be in the Caribbean area?

Mr. GRINSTEIN. That is correct.

Mr. STAKEM. I should think the answer to your question is yes, there are foreign areas served, in the foreign trade, that are closer to the United States than Hawaii is.

Mr. GRINSTEIN. Has there ever been a comparison of the rates between these areas of comparable distance?

Mr. STAKEM. I am sure we have, within the Regulatory Office of the Board, rate information of this kind.

Senator BARTLETT. Could you supply that for the record?⁹

⁸ See supplemental information from Mr. Stakem, p. 82.

⁹ See supplemental information from Mr. Stakem, p. 83.

Mr. STAKEM. Yes, what we have I will supply.

Mr. GRINSTEIN. Mr. Chairman, do carriers in the domestic offshore trade benefit from the same treatment as all subsidized carriers, with the exception of subsidy? I have in mind here nontaxable reserve fund.

Mr. STAKEM. They do not have the same privilege as the subsidized operators have under the 1936 act. They have some privileges, but not all. If it will help the committee, we can give a contrast as between the domestic operators and the offshore operators.¹⁰

Senator BARTLETT. It will be helpful and we shall appreciate your doing that.

Mr. GRINSTEIN. Along this line, would such benefits as they have that are not presently available to domestic offshore shipping, if these were extended to the carriers in the domestic offshore trades, do you think they would have a significant effect?

Mr. STAKEM. They would have some effect, Mr. Grinstein. How significant it will be, I couldn't venture an opinion at the moment. But anything helps, that is for sure.

Mr. GRINSTEIN. Has the Board made any determination on the likelihood or possibility there might develop a shift, both from American ships and U.S. mainland, for services, supplies, and market outlets? I was thinking there instead of United States and American-flag carriers serving Alaska, perhaps Japan and Japanese-flag carriers would become the main source of supply.

Mr. STAKEM. It would be hard for me to answer that question, Mr. Grinstein. The question fundamentally as I understand it, are the offshore areas, like Puerto Rico and Alaska, and Hawaii, buying more from, increasing their purchases from foreign markets as against their purchases in this country.

I would say that there is an increase, but I think by a great majority the most of this trade is with this country.

Mr. GRINSTEIN. I understand that. Some of the testimony, as I recall, testimony already presented, is that rates are apparently, in the domestic offshore trades, reaching what might be called a peril point, a point of too great a burden. It seems to me it would be material to know whether this is true and, two, if it is true, where these domestic offshore areas will begin to look for services, as well as market outlets and supply?

Mr. STAKEM. We will give you the best we can on that, Mr. Grinstein.¹¹

Senator BARTLETT. Mr. Bourbon?

Mr. BOURBON. I have no questions, Senator.

Senator BARTLETT. Mr. Goding has been with the committee for some months studying this very problem. Do you have any questions?

Mr. GODING. I have a question as to your statement on certification. In your prepared statement you questioned the value of certification, insofar as its having any economic impact. You stated that certification, in effect, protects the carriers. The question really is, does certification as we know it not also establish an obligation to serve, and provide a greater control over the type and degree of service

¹⁰ See supplemental information from Mr. Stakem, p. 83.

¹¹ See supplemental information from Mr. Stakem, p. 84.

that is subject to certification? Also is certification or the equivalent not implicit in most of the alternative suggestions—I won't say recommendations—that you have made as to things that might be done. In the foreign trades, you have your designated essential trade routes?

Mr. STAKEM. I have never been one that feels that a certification in the domestic offshore trade has been necessary. It seems to me that—and I have made this point in my statement—that the domestic offshore trade and the intercoastalwise trade, are in the forefront on new inventions in shipping operations. I am thinking of the containerization. I have the feeling that if we had not had the spark of competition in those trades which might not be present with certificates that we would not have made the advances in these trades that we have.

There is no question as to your point that a certificate of convenience and necessity has somewhat the marks of the essential trade route concept. But up to this point, we have never felt it was necessary to go that far in the domestic trade.

Mr. GODING. Would you agree that some such form would be required, if action were to be taken on any alternative that you discussed?

Mr. STAKEM. I think the objectives could be met without the certificate, the necessity for the certification. But if, as the result of these hearings, it was found that this was a necessary element in the aid that might come out of the hearings, yes, we would be glad to take a second look at our position on it.

Mr. GODING. If I recall correctly, and I am depending on memory, I think former Chairman Morse changed his position to some extent on that. I think the testimony in 1959 indicated basically the position you take today and last year, if I recall correctly. Chairman Morse indicated that he thought certification and some changes in the form of economic regulation might be desirable. Do you recall that?¹²

Mr. STAKEM. No, I don't recall that. But I do say this, that a change in position would have to be made by the Federal Maritime Board, and this has not been specifically studied beyond the fact, as I stated today, that we see no immediate necessity of changeover.

Mr. GODING. I have one suggestion here, in terms of material for the record. I think it would be helpful if we had specific data in the form of a table or tabulary presentation of the tonnage, number of vessels involved in the noncontiguous services set up against the number in other domestic operations. I am speaking of common-carrier dry cargo vessels.

Mr. STAKEM. Yes, we will be happy to furnish that for the record.¹³

Senator BARTLETT. Competition is not necessarily denied, Mr. Stakem, by reason of certification, is it?

Mr. STAKEM. No, you can certificate as many as you feel are necessary in the trade to do the proper job.

Senator BARTLETT. Right, Mr. Grinstein?

Mr. GRINSTEIN. Mr. Chairman, you mentioned before in your brief before the court of appeals, I believe, in docket 807, you set out the standards you applied in the ratemaking case. I have been informed by note that docket 807 was reversed by the court of appeals and va-

¹² See supplemental information from Mr. Stakem, p. 84.

¹³ See supplemental information from Mr. Stakem, p. 85.

ated. Was it based on the fact they felt your standards were inadequate?

Mr. STAKEM. No, let me change your word from "reversed" to "remanded." It was remanded on, I think, a very narrow point. I haven't got the remand direction with me, but it seemed to me there were two points made by the court. One was, in going for the domestic market value, or the market value of the vessels, in the rate base, it was felt that the discussion and reasons were not properly set forth in the opinion.

Then there was, I think, a question of what happens when the depreciation is eliminated and you have perhaps a resale of ships, at a new rate base. So I would consider that the court's action is not a reversal of the elements of the rate base, but merely a remand on these two points which must now be considered by the Board.

Mr. GRINSTEIN. When you supply for the record your brief, could you also supply the court of appeals' decision, and what new determinations are made?

Mr. STAKEM. Yes.¹⁴

Mr. GRINSTEIN. In your brief before the court of appeals, in docket 807, did you also set out what considerations you give to the effect of rates on the local economy?

Mr. STAKEM. I would have to reread the presentation, Mr. Grinstein.

Mr. GRINSTEIN. If you do have some statement as to how much investigation you make and how this evidence is weighted in a determination, I think it would be helpful to the committee.

Mr. STAKEM. Yes, sir.¹⁵

Senator BARTLETT. Mr. Chairman, Mr. Grinstein tried to tie you down and make you an economic prophet in advancing 5-year projects and you were probably wise in not making any direct commitment, but can we not say this, that if the future is as the past, the costs of operating ships and the costs of constructing ships, even if temporarily they are down, will advance as will everything else in our economic structure?

Mr. STAKEM. Yes. I can say this, that the Office of Ship Construction which keeps a running record of the costs, has used a measure, shall we say a measure of thumb, that about 5 percent a year has been the indication of the cost rise, except as I say for this last period where we are getting much better prices than we had expected.

Senator BARTLETT. Decreases tend to be temporary in nature.

Mr. STAKEM. Yes, sir.

Senator BARTLETT. The whole economic pressure in the Western World is on the inflationary side and it may apply to other parts of the world, as far as I know, and I suspect it does.

Mr. STAKEM. It probably does.

Senator BARTLETT. Now Mr. Grinstein also asked you what I thought was a very worthwhile question. What, if any, evidence is there that high freight rates may be inducing foreign carriers to come to these offshore areas? I wonder if you will be good enough, if it is possible for you, to present a statement to the committee on that very point.

¹⁴ See supplemental information from Mr. Stakem, p. 85.

¹⁵ See supplemental information from Mr. Stakem, p. 169.

For example, in Alaska I know that within the last year many, or at least several, Japanese ships have put in with steel cargoes and with other construction materials, to the loss of American carriers, and American steel mills, and American labor. I don't know what bearing the freight rates had on this, if any, but if you could supply information on that point, it might be helpful, because that which has been started may expand and multiply unless we take appropriate steps.

Mr. STAKEM. Yes. I think it is common knowledge that the Japanese are very active in soliciting business in Alaska. They do carry considerable pulp out of the mill at Sitka, and I know in trying to get a haul both ways they are actively soliciting merchants for Japanese goods.¹⁶

Senator BARTLETT. And will you not agree with me, Mr. Chairman, that in these instances, and others which may arise, or may already have arisen, it is an obligation on our part to see to it that, insofar as possible, American goods, built by American labor and carried by American carriers, are employed?

Mr. STAKEM. I think that is our responsibility, Senator.

Senator BARTLETT. Thank you very much, Mr. Chairman, for an informative statement which we will study and restudy.

Mr. STAKEM. Thank you, sir.

Senator BARTLETT. And we shall depend very largely, I might add, upon the Federal Maritime Board to give us on a continuing basis the data so essential to this inquiry.

Mr. STAKEM. We will do our best, Senator.

Senator BARTLETT. Now the committee is going to stand in recess, but we are not going to wait until tomorrow morning before we resume because we are going to run out of time if we do that. If it is not a burden upon those who are to testify also this morning, we are going to ask them to return at 2 o'clock this afternoon, at which time the hearings will be resumed.

The attorney general of Hawaii is to be heard next and Mr. Oshiro, a member of the Hawaiian Legislature, the Governor of the Virgin Islands, and Mr. Edwards, secretary of Guam. We would hope at least to conclude their testimony during the afternoon session.

(Thereupon, at 12:10 p.m., the subcommittee recessed, to reconvene at 2 p.m. the same day.)

AFTERNOON SESSION

Senator BARTLETT. The committee will be in order.

The acting chairman of the subcommittee wants to express the hope and belief that tomorrow the able and distinguished Senator from California, Mr. Engle, shall have returned from the Golden State, on schedule, and will be here to preside over the hearing. And next week also we hope to give, if possible, even more objective attention to this problem than the chairman who is before you now.

The committee is honored to have as the next witness Mr. Kashiwa, attorney general of the State of Hawaii.

For the record it might be stated that the attorney general of Hawaii is accompanied by Mr. William Rogers, attorney, of Washington, D.C.,

¹⁶ See supplemental information from Mr. Stakem, p. 169.

special deputy attorney. You identify, if you care to, Mr. Rogers more particularly, will you?

STATEMENT OF SHIRO KASHIWA, ATTORNEY GENERAL OF THE STATE OF HAWAII, ACCOMPANIED BY WILLIAM ROGERS, OF WASHINGTON, D.C.

Mr. KASHIWA. Mr. Rogers, of Washington, D.C., is associated with my office as special deputy attorney general in all the Hawaiian maritime matters.

Senator BARTLETT. We are glad to have him here, too.

Now you may proceed, Mr. Kashiwa.

Mr. KASHIWA. For the record, my name is Shiro Kashiwa. I am the attorney general of the State of Hawaii.

Gov. William F. Quinn has asked me to appear on behalf of the State during these hearings. The Governor deeply and sincerely regrets that he could not himself come to Washington. Our legislature is presently in session. As you may imagine, it is difficult for him to leave Honolulu at this time. He has asked me to convey his sincere regrets for his inability to be here.

He has especially asked me to state to you his profound appreciation for the institution of this investigation. The State, for reasons which I shall attempt to develop, believes that the problem of high and continually increasing maritime rates for its essential shipping to and from the mainland is one of the most serious economic problems Hawaii faces today. The Governor was gratified to have the opportunity to meet with the Governors, Senators, and congressional officials of Alaska and Puerto Rico on this problem during inauguration week while he was here in Washington, and wants me to reaffirm his vital concern with this problem. He has asked me to say again for him that the State is anxious to continue its cooperation and aid in this committee's search for an equitable remedy.

A word or two about the economy of Hawaii will demonstrate the overwhelmingly crucial importance of maritime rates and service to our people, and the vital need for remedial Federal legislation. I have set forth some of the general economic indicators in attachment I of this statement.

The Hawaiian island chain is some 2,400 miles off the coast of California. It consists of eight major islands: Oahu, the Island of Hawaii (the "Big Island"), Maui, Kauai, Niihau, Molokai, Lanai, and Kahoolawe. The chain extends over some 400 miles of ocean.

The land area in the State is 6,435 square miles. This makes Hawaii roughly the same area as the States of Connecticut and Rhode Island combined.

Our population is something over 600,000, to which should be added about 50,000 or 60,000 Armed Forces personnel. This population is greater than the population of Alaska, Nevada, Wyoming, Vermont, Delaware, or New Hampshire. The bulk of these people, over 500,000 of them, live in the city and county of Honolulu, which includes the principal metropolitan center of Honolulu, our major business community, the seat of the State government, and, of course, the Island's major shipping port.

The economy of Hawaii is tied to the economy of the mainland. Hawaii is far from self-sufficient. We are, in broad terms, specialists,

selling goods and services to the mainland and purchasing the bulk of what we consume from mainland producers and suppliers. Naturally, such an economy is totally dependent upon transportation.

Governor Quinn, testifying at recent Maritime Board rate hearings, described the importance of our transportation services to and from the mainland as follows (Pacific Coast-Hawaii and Atlantic/Gulf-Hawaii General Increase in Rates, Federal Maritime Board docket 869 (hereinafter docket 869), transcript, p. 2203):

Hawaii is vitally dependent upon its ocean shipping services. More than half of everything produced in Hawaii is shipped out over the seas to the mainland. More than half of everything that the people of Hawaii consume—more than half of their foods, their clothing, their automobiles, most of the products that go into their houses—are imported from the mainland.

Aside from military spending, two major industries support our economy: agriculture and tourism.

Hawaiian agriculture has a long history. Throughout that history it has been geared to production of specialized products for shipment to the markets of the mainland.

Sugar is the most important. At the present time, Hawaii produces approximately 1 million tons of sugar per year for shipment to the mainland. About 800,000 tons move to California in bulk under tariff terms for refining. The remainder is shipped to Atlantic coast refineries. The value of this export crop to the Hawaiian economy in 1959 was roughly \$131 million (exhibit 107, docket 869, preliminary data).

Our second major crop for export to the mainland is pineapples. Twenty-seven million cases were produced during the fiscal year ending May 31, 1958. The value of the pineapple crop was \$122 million (*ibid.*—preliminary data).

These two major products, as I have indicated, are in large part marketed on the mainland; the economy of the islands, the incomes of our people and their employment opportunities depend to a marked degree upon the continued success of these two sectors of the agricultural industry.

The second major nondefense pillar of the Hawaiian economy is the tourist industry. Tourism in Hawaii has shown remarkable growth in the last few years. There are now almost 200,000 visitors to the islands each year. The tourist industry, as a form of invisible export, has recently become almost as significant to the State's economy as the visible exports of agricultural products.

These two major industries, along with defense spending, constitute the major sources of dollar earnings for Hawaii. These earnings become payments for the enormous volume of goods which we import from the mainland each year. There are few manufacturing industries in Hawaii. We import into the State almost all of the products which are part of mid-20th century life in the United States. Thus, in 1958, Hawaii bought from the mainland \$426 million of various goods—food, clothing, construction materials, appliances, drugs (exhibit 34, p. 29, docket 869). Purchases from the mainland currently are running at about half a billion dollars per year.

The dependence upon transportation is particularly marked in the area of consumer goods. Responsible economists have estimated, for example, that 90 percent of our consumer items—shoes, television sets, and refrigerators, construction materials—which make up the bulk

of personal expenditures of our people, are imported from the mainland. Almost two-thirds of our food is brought over the oceans as well. (Dr. James H. Shoemaker, docket 869, transcript, pp. 1750-1751). These commodities are indispensable to Hawaii.

In short, we depend in vital ways upon transportation. As a specialized economy, we produce for sale to the mainland, and we use our earnings on the mainland to import the essentials of life into Hawaii. Some indication of the vast catalog of goods we import and export can be seen from attachments II and III to this brief. It lists westbound and eastbound cargo, to the Pacific coast, as well as to the east coast and it is listed in four different pages, quite a long list of commodities. Hawaii could not live without transportation.

However, we have but one form of transportation to turn to: ocean shipping. The other States of the United States can call on a variety of competitive services, including truck, rail, and highway transportation. In Hawaii, aside from a negligible amount of air freight, however, all our essential exports and imports move by ship. Ocean transportation has a monopoly over our vital transportation needs. Steamship service is the lifeline of the Hawaiian economy.

Thus we stand on a different footing than the States of the mainland. We are wholly unable to avoid the impact of increases in ocean shipping costs. Every cost increase for our essential ocean shipping services immediately affects the economy and people of Hawaii. We have no other service to turn to.

High shipping costs for our exports affect the competitive position of these exports in the mainland market, and hence the incomes and employment opportunities in Hawaii. We have noticed this particularly in recent years in the case of our pineapple industry which is now finding its ability to compete substantially affected by increases in ocean freight rates, and is losing mainland markets to foreign pineapple. In fact, one of our large canneries has recently announced that it will cease operations.

On the other hand, every increase in freight rates on inbound commodities, such as cars, refrigerators and food, shoes and construction materials, also has several serious consequences. On major consumer items, purchase of which cannot be postponed or avoided, we have no alternative but to pay the higher price. The transportation cost increase is passed on to the consumer and adds to the inflationary drain on the purchasing power of the consumer dollar in Hawaii. Some measure of the high cost of living in Hawaii, occasioned in part by the burden of high transportation rates, may be seen from attachments II and IV, attached to this brief, which compare our food prices with those on the mainland.

For other items, consumption can be postponed or there are alternative sources of supply. For these, transportation cost increases can have the effect of depressing sales of mainland manufactured goods. This is because the diluted value of the dollar may compel the consumers to forgo expenditures, or alternative products manufactured in foreign countries and shipped in at foreign-flag freight rates can be sold at lower prices.

Note, for example, automobile sales. Foreign cars have penetrated the Hawaiian market much more deeply than the mainland market. As attachment V shows, in 1958 more than one out of every three cars sold in Hawaii were manufactured in foreign countries and im-

ported into Hawaii at foreign-flag rates. On the mainland foreign car sales were less than 1 in 10. There is no doubt that a part of the move to foreign cars in Hawaii is the result of the simple fact that the ocean freight on cars all the way from England is roughly identical with the freight on U.S. cars moving only the 2,400 miles from California (docket 869, transcript, p. 2536).

We are now also importing increasing amounts of meat products from Australia and New Zealand, textiles from Japan, and lumber and newsprint from Canada. This trend to foreign sources of supply and manufacture has meant that U.S. suppliers and shippers as a whole are finding themselves more and more shut off from the growth of the Hawaiian economy. Although our imports from the mainland still vastly exceed our imports from foreign countries, imports from foreign countries are growing at a more rapid rate than shipments from the mainland, as shown in attachment VI.

To give you some idea of the overall magnitude of the importance to our economy of the freight movement between the mainland and Hawaii, I have set out in attachment VIII a schedule of tonnage and revenue in recent years. Note that our personal income in 1958 was only \$1,154 million. Ocean freight charges, that is to say, charges solely for moving our imports and exports between the mainland and Hawaii, were almost \$80 million. This is 6 percent of all our income.

It is therefore a matter of fundamental importance that the cost of ocean shipping to the people of Hawaii be kept as low as is economically possible. The people of Hawaii are prepared to pay for the commercial cost of their service, but they should not be called upon to bear alone, by themselves, some higher cost imposed by a national policy.

Hawaii has gained statehood. As a matter of equity its admission as a State must be on an equal footing with all other States. If it is to grow, if its economic ties with the other States are to develop, it must also have transportation rates which reflect commercial considerations.

The cost of Hawaii's essential maritime services to and from the mainland is already higher than it should be; is increasing at an alarming rate; and may shortly spurt upward to a level beyond our ability to pay. This is in considerable part due to Federal maritime policy.

Federal law restricts trade between the mainland and Hawaii to U.S.-flag vessels. U.S.-flag vessels are more expensive to operate than foreign-flag vessels. Vessel replacement in U.S. yards is substantially more costly than replacement in foreign yards. Costs of operating U.S.-flag vessels have increased more rapidly in recent years than costs of foreign-flag lines.

This higher cost of U.S.-flag service is borne by the people of Hawaii alone. In the Merchant Marine Act of 1936, of course, Congress authorized the Maritime Administration to absorb up to one-half the cost of construction of vessels to be used by American shipping companies in the foreign trades. Similar relief, however, was not afforded to American-flag operators in the domestic offshore trades. In fact, these trades were expressly excluded from the subsidy provisions of the Merchant Marine Act.

The 1936 act also provided for the subsidizing by the United States of the differential in operating costs of American-flag vessels over

comparable operations of foreign-flag operators. Again, this effort to assist the U.S. merchant marine to match the lower costs of foreign carriers was not extended to the domestic trades.

As a result of this national policy, the increasingly high cost of U.S.-flag services between the mainland and Hawaii must be borne by the people of Hawaii alone. Rates in mainland-Hawaii trade have nearly doubled in a decade. The history of these rate increases is reflected in attachment VIII. It shows between the years of 1951 to 1959 rates have gone up 88 percent. It is hardly surprising, therefore, that the cost of living in Hawaii has gone up much more rapidly than elsewhere in the Nation, as shown in attachment IX. It shows that on the mainland, U.S. consumer index jumped—this is between 1950 and 1959—U.S. consumer index jumped from 102 to 124 while the Hawaiian index jumped from 120 to 151.

Had Honolulu been a foreign port during this same period, our annual freight bill would have been consistently lower and would not have reflected the inflationary spiral which is now having such a vital effect on our economy.

The policy of the Merchant Marine Act of 1936 was geared from all appearances to national considerations of defense. It was thought essential to insure a modern fleet-in-being under the American flag, and to continue a nucleus of commercial shipbuilding, against the hazard of war.

Thus the Federal Government in 1936 encouraged domestic shipyards and the development of a more modern merchant marine by the use of construction-differential subsidy and enabled the continuation of U.S.-flag foreign services by an operating-differential subsidy. The wisdom of this policy became apparent in the dark days of World War II.

Perhaps there were valid reasons why Congress did not extend these same benefits to the carriers in the Hawaiian trade in 1936, while at the same time continuing to require, through longstanding restrictions, that Hawaii be served only by U.S.-flag carriers in American-built ships. Hawaii was then a territory. And the cost differential between U.S.-flag carriers and foreign-flag carriers perhaps was not so drastic then as it is today.

But as this committee knows, since World War II economic conditions of the ocean steamship industry have changed markedly. The bar against use of foreign-flag vessels now has the effect of thrusting upon Hawaii the full burden of costly American shipping services. I would like to repeat that. The bar against the use of foreign-flag vessels now has the effect of thrusting upon Hawaii the full burden of costly American shipping service.

Perhaps this is essential from the standpoint of the national interest. It may well be a vital national policy to preserve the fleet used in the mainland-Hawaii service under our flag in the event of a national emergency. We would not question such a policy decision. But we feel that to require the people of Hawaii to bear the entire cost of this national policy decision is unjust and inequitable.

I would like to repeat that. We feel to require the people of Hawaii to bear the entire cost of this national policy decision is unjust and inequitable.

This burden apparently will increase to even more severe proportions in the near future. The majority of the vessels in the Hawaii-mainland service were purchased by the carriers from the Government shortly after World War II at favorable prices of \$1 million to \$2 million each. Thus, Matson's total investment for its large fleet, much of it already recovered through depreciation, was only \$36 million. But the useful life of these vessels is soon to expire. It is now estimated that the cost of construction of a replacement for each vessel, with the necessary technological improvements, will cost up to 10 times the investment in the present vessels. Matson, for example, has estimated that to replace its World War II fleet with modern vessels, it will require upwards of \$300 million, as shown in attachment X.

I will not repeat the list because it is a very long list, but the vessels are named in that attachment.

There are several possibilities—all disastrous. Either the carriers will find themselves unable to gather the breath-taking capital sums required for new vessels—which will mean that Hawaii will be served by obsolete, deteriorating vessels, or the replacement vessels will be built and their cost passed on to the people of Hawaii in the form of astronomical freight charges. These higher freight charges could well be beyond our ability to pay.

Some remedy for this inequity, some relief from this approaching crisis, must be forthcoming. Measures must be taken to insure that the cost of ocean transportation to the people of Hawaii be pegged at the lowest feasible level. This could be accomplished either directly—by opening up the trade to the lowest cost foreign-flag operator, a remedy the States does not recommend, or indirectly, by arranging for a system of Federal assistance, to be passed on to the consumers as lower or more stable rates, which would offset the higher construction and operating costs of U.S.-flag carriers.

The State has given a great deal of thought to the precise form which this remedial legislation should take. We have not, however, proposed any specific terms for a bill for your consideration, primarily because we recognize that its final form must be based on considerations of national policy with respect to which you are much more qualified to speak than we. We are, however, anxious to continue to aid and cooperate with your search for a solution. We have a wealth of information which might be relevant to your considerations, much of it gathered in the course of the recent Maritime Board's investigation of the 1959 Hawaii rate increase. We would like to make this available to you. My office and our representatives here in Washington are prepared to work with your staff at any time.

It is not the position of the State that its people should escape the payment of just rates for ocean shipping services. Hawaii does not want the Federal Government to provide ocean transportation at the expense of its fellow citizens on the mainland. We will pay our own way. The State feels, however, that it should not have to bear alone the costs of a national program. In order that the United States might have vessels readily available in the event of a national emergency, Hawaii is now compelled by national law to pay an artificially high price for its shipping. If this national defense policy is valid, its cost, we think, should be borne by the people of all the States of the Union.

(The attachments to Mr. Kashiwa's statement follow.)

ATTACHMENT I

Selected economic indicators

I. GROSS PRODUCT OF STATE

Year	Amount	Average annual percent increase
	<i>Thousands</i>	
1939.....	\$562,500	
1952.....	1,141,304	1939-52..... 8.6
1958.....	1,400,000	1952-58..... 4.5

II. TOTAL PERSONAL INCOME

Period or year	Amount	Index
	<i>Thousands</i>	
1946-50.....	\$708,000	100
1951-55.....	876,000	124
1956.....	1,024,000	145
1957.....	1,098,000	155
1958.....	1,154,000	163

III. AVERAGE PER CAPITA INCOME

Period or year	Amount	Index
	<i>Thousands</i>	
1946-50.....	\$1,373	100
1951-55.....	1,694	123
1956.....	1,787	130
1957.....	1,821	133
1958.....	1,862	135

Source: Exhibit No. 33, F.M.B. docket No. 869, "The Hawaiian Market", compiled and published by J. Walter Thompson Co.

ATTACHMENT II

Commodity Cargo carried by Matson Navigation Co., Pacific Coast to Hawaii, 1959

Commercial:	Short tons
Merchandise, general, not otherwise specified	227, 033
Asphalt, liquid in bulk	5, 242
Autos and trucks	16, 034
Beer	14, 375
Boxes, fiberboard	15, 073
Canned goods	39, 627
Feed and grain:	
In bags	63, 110
In bulk	1, 153
Fertilizer:	
In packages	23, 410
In bulk	48, 869
In liquid	39, 832
Flour	20, 981
Fuel oil, bulk	232, 336
Furniture	3, 579
Household appliances	5, 513
Iron, steel, and machinery	69, 283
Lumber:	
Loose	11, 861
Strapped	117, 336
Paper, newsprint in rolls	8, 850
Petroleum products	12, 350
Plywood, strapped	4, 288
Refrigerator cargo	45, 946
Rice	16, 540
Tinplate	16, 499
Ventilated cargo	19, 693
Total commercial	1, 078, 813
Sea vans (military household goods moving on Government bill of lading)	13, 347
MSTS	80, 316
Total westbound	1, 172, 426

Source: Exhibit No. 29, FMB docket 869.

Commodity Cargo carried by Matson Navigation Co., Hawaii to Pacific Coast, 1959

	Short tons
Merchandise, general	9, 726
Autos and trucks	726
Coffee, green	3, 186
Containers, empty, returned	1, 352
Hides, green	1, 155
Household goods	589
Iron, steel, and machinery	5, 385
Molasses, in bulk	215, 839
Pineapple, canned (unitized)	63, 864
Pineapple, canned (loose)	126, 681
Refrigerator cargo	20, 690
Sugar, raw, in bulk	781, 084
Sugar, refined, in sacks	20, 426
Wallboard	20, 824
Sea vans, empty	2, 266
Total commercial	1, 273, 793
Sea vans (military household good moving on Government bill of lading)	9, 859
MSTS	21, 207
Total eastbound	1, 304, 859

Source: Exhibit No. 29, FMB docket 869.

Cargo carried by Matson Navigation Co., United States Lines Co., and Isthmian Lines, Inc., Atlantic-Gulf to Hawaii, 1959

<i>Commodity</i>	<i>Short tons</i>
Commercial:	
Merchandise, general, n.o.s.	53, 023
Autos and trucks	2, 090
Canned goods	3, 759
Chemicals	259
Clay	157
Cotton piece goods	1, 160
Feed and grain	30, 231
Fertilizer	8, 469
Floor covering	884
Furniture	539
Glass and glassware	862
Household appliances	332
Household effects (vans)	1, 340
Insecticide	977
Iron and steel	26, 725
Liquors and beer	2, 994
Machinery	767
Meats, reefer	362
Paperboard	547
Paper products	502
Peanuts	314
Sulphur	2, 912
Textiles	990
Tinplate	37, 961
Total commercial	178, 756
Sea vans (military household goods moving on Government bill of lading)	1, 377
MSTS	15, 773
Total westbound	194, 599

Sources: Exhibits 2, 8, and 29, FMB docket 869.

Cargo carried by Matson Navigation Co., United States Lines Co., and Isthmian Lines, Inc., Hawaii to Atlantic-Gulf, 1959

<i>Commodity</i>	<i>Short tons</i>
Commercial:	
Merchandise, general, n.o.s.	7, 253
Household goods	417
Iron and steel (scrap)	1, 385
Pineapples and juice	290, 751
Refrigerator cargo	66
Sugar, raw, in bulk	82, 981
Tinplate	485
Total commercial	383, 938
Sea vans (military household goods moving on Government bill of lading)	2, 291
MSTS	19, 672
Total eastbound	405, 901

Sources: Exhibits 2, 8, and 29, FMB docket 869.

ATTACHMENT III

Comparison of annual average retail prices for major food items in U.S. mainland cities and Honolulu

Item	1959 average price	
	U.S. cities	Honolulu
Bacon (sliced, per pound)	\$0. 651	\$0. 849
Salmon (pink, per pound) .....	. 622	. 663
Butter (per pound) .....	. 759	. 835
Cheese (per pound) .....	. 581	. 674
Milk (evaporated, 14½ ounces) .....	. 153	. 176
Potatoes (per pound) .....	. 066	. 116
Onions (per pound) .....	. 112	. 125
Peaches (can, No. 2½) .....	. 353	. 409
Corn (can, No. 2) .....	. 192	. 243
Peas (can, No. 2) .....	. 202	. 254
Flour, wheat (5 pounds) .....	. 544	. 742
Coffee (per pound) .....	. 774	. 986
Lunch meat (can, 12 ounces) .....	. 512	. 558

Sources: Mainland cities, U.S. Department of Labor, Bureau of Labor Statistics. Honolulu, State department of labor and industrial relations, bureau of research and statistics. Exhibit No. 61, FMB docket 869.

ATTACHMENT IV

Comparison of annual average retail prices for food items listed in attachment III, 5 mainland cities and Honolulu

City	1959 average
Honolulu	\$6. 630
U.S. city average	5. 521
Los Angeles	5. 698
Portland	5. 560
San Francisco	5. 970
Seattle	5. 502
New York	5. 546

Sources: Mainland cities, U.S. Department of Labor, Bureau of Labor Statistics. Honolulu, State department of labor and industrial relations, bureau of research and statistics. Exhibit No. 61, FMB docket 869.

ATTACHMENT V

Comparison of foreign automobile sales, Hawaii and the mainland

	Percent of total sales	
	Mainland	Hawaii
1957	3. 8	14. 7
1958	8. 6	35. 7
1959	9. 8	30. 8

Source: FMB docket 869, tr. pp. 2535-2536.

ATTACHMENT VI

*Growth rates of Hawaiian purchases from mainland and foreign countries—
Purchases from mainland and imports from foreign countries*

[In thousands of dollars]

Year or average period	Hawaii, mainland	Index	Hawaii, foreign	Index
1946-50 ¹	\$304,000	100	\$12,154	100
1952-55	365,000	120	19,714	162
1956	407,000	134	22,779	187
1957	464,000	153	26,695	220
1958 ²	426,000	140	33,244	274

¹ 1948 and 1951 not available.² Year of sugar strike.

Source: Exhibit No. 33, FMB docket 869, "The Hawaiian Market," compiled and published by J. Walter Thompson Co.

ATTACHMENT VII

Annual freight movement between Hawaii and the mainland liner services

TONNAGE

[In short tons of 2,000 pounds]

	1957	1958	1959
Pacific coast-Hawaii service	2,710,806	2,107,187	¹ 2,477,335
Atlantic/gulf-Hawaii service	658,807	612,010	600,500

REVENUES

[In thousands of dollars]

Pacific coast-Hawaii service	52,290	48,820	55,667
Atlantic/gulf-Hawaii service	² 18,187	² 17,857	² 17,043
Total	70,477	66,677	72,710

¹ Weight tons carried by Hawaiian Marine Freightways unavailable.² Revenues of United States Lines unavailable (1957, 25,338 tons; 1958, 31,877 tons; 1959, 36,637 tons).

Sources: Exhibits 1, 2, 8, 10, and 29, FMB docket 869.

ATTACHMENT VIII

Pacific coast-Hawaii rate increases

[In percent]

Effective date of increase	Amount	Increase over 1950 base	Effective date of increase	Amount	Increase over 1950 base
Feb. 1, 1951	10.0	10	July 15, 1957	13.2	53.95
Jan. 14, 1952	7.5	18.25	Jan. 20, 1958	9.0	67.81
Mar. 1, 1953	8.5	28.30	Sept. 14, 1959	12.5	88.79
Mar. 1, 1955	6.0	36			

ATTACHMENT IX

Comparison of rates of increase of Hawaii and U.S. consumer prices indexes

[1943=100]

Year	U.S. consumer price index	Hawaii consumer price index
1950	102.8	120.1
1955	114.5	135.9
1959	124.6	151.7

Sources: Business research department of the Bank of Hawaii, exhibit No. 118, FMB docket 869.

ATTACHMENT X

Replacement cost of Matson Navigation Co.'s 1960 cargo fleet

Vessel	Year built	Original cost plus improvements	Cost of replacing fleet with modern high-speed cargo ships and special ships
Hawaiian Rancher	1944	\$2,333,210	\$14,655,000
Hawaiian Farmer	1944	2,077,960	14,655,000
Hawaiian Craftsman	1945	1,718,707	14,655,000
Hawaiian Planter	1945	1,689,608	14,655,000
Hawaiian Educator	1945	1,563,616	14,655,000
Hawaiian Fisherman	1945	1,629,505	14,655,000
Hawaiian Merchant	1945	2,329,259	14,655,000
Hawaiian Builder	1945	2,349,726	14,655,000
Hawaiian Packer	1943	2,407,118	14,655,000
Hawaiian Retailer	1944	1,331,427	14,655,000
Hawaiian Refiner	1944	2,390,550	14,655,000
Hawaiian Lumberman	1944	628,501	14,655,000
Hawaiian Trader	1945	910,918	14,655,000
Hawaiian Tourist	1945	994,779	14,655,000
Hawaiian Traveler	1945	993,528	14,655,000
Hawaiian citizen ¹	1960	4,050,000	14,615,000
Californian ¹	1960	3,300,000	14,615,000
Hawaiian ¹	1960	3,300,000	14,615,000
Total		35,998,343	278,325,000

¹ Remodeled.

Source: Matson Navigation Co., exhibits 25 and 29, FMB docket 869.

Senator BARTLETT. Thank you, Mr. Attorney General.

The rate increases to which you have referred apply equally and in equal measure to eastbound traffic?

Mr. KASHIWA. No. I don't like to go into a detailed discussion of our last rate, but as you know in ocean shipping—by the way, the last rate case was 12.5 percent, generally speaking, but in certain areas that was not applied.

Senator BARTLETT. Over the years, over the last decade, for example, would you say that the increases that have been applied to the transportation of eastbound cargo have been identical or closely so with westbound cargo?

Mr. KASHIWA. I would not say so, because there were certain reductions made in certain areas on eastbound cargo.

Senator BARTLETT. Applying to pineapple in many instances?

Mr. KASHIWA. More to sugar.

Senator BARTLETT. More to sugar. Do you have any explanation of that?

Mr. KASHIWA. Now, Senator, this is an area which is now being discussed in our rate case before the Maritime examiner, and it will be before the Board. I am, personally, counsel of record. Of course, the briefs will be available to your staff, if the staff wants to discuss the problems, but it is a field where I do not wish to go into a lengthy discussion about it.

Senator BARTLETT. We have no desire or intention to try a case here, but let me persist for a moment.

Is this situation to which you refer historically true? To use a word which may not be accurate, has there always been favoritism for sugar as compared with pineapple?

Mr. KASHIWA. In one of the earlier cases, case 808, there was an instance of favoring pineapple, and a correction was made.

Senator BARTLETT. Well, we will let that be.

Are you now contesting a proposed freight rate increase?

Mr. KASHIWA. Oh, yes. Yes, the 12.5-percent rate case was heard. We started out in New York, San Francisco, Hawaii, back in Washington, and is now before the examiner.

Senator BARTLETT. When was the request for that increase made?

Mr. KASHIWA. In September 1959.

Senator BARTLETT. All right. That is the one I have in mind.

Now, it is true, is it not, Mr. Attorney General, that the cost of living in Hawaii is materially higher than in any of the original 48 States?

Mr. KASHIWA. It is.

Senator BARTLETT. Why should that be so, in your opinion?

Mr. KASHIWA. Well, it is our opinion that one of the contributing causes is higher freight rates. Everything must be shipped out there.

Senator BARTLETT. You heard Mr. Stakem make his statement this morning, I know. He very correctly, in my opinion, said ocean freight rates in and by themselves aren't the sole reasons for increases in the prices of commodities when they reach the public. And he named several other factors that might and I suppose always do apply. Have you any personal view as to whether ocean freight rates are the principal factor?

Mr. KASHIWA. Now, this I would like to say: On certain specific items what the chairman said may be true. But where there is a generally high level, and the State is located 2,000 miles away from the mainland and here these rates are going up and up, there is a corresponding rise in the index. We can point our finger and say, well, this certainly should materially contribute to this rise.

Now, I think that there is no exact way of determining to the *n*th degree whether a certain raise is all due to a certain thing, but as a general rule we can point to the difference between the mainland and Hawaii, that we are separated by this body of water and we have this higher living cost index, and I think that is attributable to the freight rates.

Senator BARTLETT. Well, it is true, is it not, Mr. Kashiwa, that the Federal Government itself recognizes the markedly higher cost of living in Hawaii by granting its own employees a cost of living allowance?

Mr. KASHIWA. That is true.

Senator BARTLETT. What is the order of that allowance now in Hawaii?

Mr. KASHIWA. I don't know. I am a State employee. But it runs about 25 percent, doesn't it? I am not so certain about it. I can get that differential for you and submit it to you.

Senator BARTLETT. It is my recollection it is 20 percent in Hawaii now, but I would appreciate your doing that, as indicative of the higher costs of living there.

Mr. Attorney General, to your knowledge is any freight transported from the U.S. mainland to Hawaii by barge?

Mr. KASHIWA. Yes.

Senator BARTLETT. When did that start?

Mr. KASHIWA. Many years ago there was a steamship strike, and there were some barge shipments to Hawaii, but lately it has been revived from the Pacific Northwest area, just very lately.

Senator BARTLETT. Are the barges important in the transportation scheme of things as of now?

Mr. KASHIWA. No, it has been only very recently these barges have come in and, as I understand, they handle lumber and it is significant to this extent that lately Matson has announced that with respect to its Northwest trade, certain of its shipping schedules are going to be materially disrupted.

Senator BARTLETT. From which of the U.S. ports does the greatest Hawaii tonnage come?

Mr. KASHIWA. San Francisco and Los Angeles.

Senator BARTLETT. What would be the percentage from Portland and Seattle—small, medium?

Mr. KASHIWA. Portland, Seattle, I would say it is small compared to San Francisco and Los Angeles tonnage. But I could get those figures for you.

Senator BARTLETT. Don't trouble. I don't think that will be necessary.

Is San Francisco the nearest port on the mainland to Honolulu?

Mr. KASHIWA. That is true.

Senator BARTLETT. In Senator Long's statement this morning, confirmed by you, he said that in the 8½ years last past freight rates have witnessed a cumulative rise of 89 percent. Do you have any readily available information as to the situation in the comparable period before then?

Mr. KASHIWA. Yes. We don't have it here, but we can get the raises before 1951 for you and we can submit that in tabular form.

Senator BARTLETT. Ocean freight rates have gone up; trucks rates have gone up; and if anything hasn't gone up in the last decade, I don't know offhand what it might be. However, do you have any information which you might make available to the committee as to these increases of 89 percent compared with general rail increases, truck-rate boosts, and increases which might have been experienced on intracoastal or intercoastal shipping routes?

Mr. KASHIWA. We don't have the figures here now, but certainly we can work this out for you.

Senator BARTLETT. I don't know if I should call upon you to supply that information. Perhaps we could get it. I think we will save you the labor of going into that, because that really is not your proper function. But I think we must have from the ICC or some other Fed-

eral agency some kind of yardstick here by which to make comparisons.

Mr. KASHIWA. I wanted to point out, even though these percentages may be high, on the mainland here you have an alternative, where something goes up you don't necessarily have to use that service, you can use some other service, like trucking, for example. In Hawaii you don't have this alternative. You either have to use steamship or nothing.

Senator BARTLETT. Or it doesn't get there.

Mr. KASHIWA. That is right.

Senator BARTLETT. How is tourism faring in the State to the westward?

Mr. KASHIWA. Very well, Senator. We have been spending a lot of money on destination centers on the other islands. Waikiki is just booming. In that business everything looks very good at the present time. Of course, it looks as though, on the face of things, because they all fly there, that shipping doesn't affect this business too much, but at the same time, when they come there, they must be fed, they buy materials and goods there, and this all comes by steamship.

Senator BARTLETT. Mr. Attorney General, it is true, in all probability, that all of us in this room are quite adapted to the proposition of boarding an airplane and going from where we are to where we want to go. But is it not likewise true that the majority, in numbers and percentages, of Americans have never been aboard a plane? Lots of people will not take an airplane for vacation trips or for any other purpose, and if they don't have passenger service to Hawaii, for example, as they do not to Alaska, they won't go to Hawaii?

Would you agree with that?

Mr. KASHIWA. Are you talking about steamship—I didn't get your question.

Senator BARTLETT. My question is this: If you did not have passenger steamship service to Hawaii, would you not deny many people the opportunity of going there, because they are not willing to fly?

Mr. KASHIWA. That is true. There are many, many people—I am still surprised—many who are not willing to fly. They would rather sail down there and come back on a boat. Fortunately we do have them still traveling out there and also on the *Matsonia*.

Senator BARTLETT. Mr. Grinstein fortifies my vague recollection on this subject by saying 78 percent of the people in the United States have never flown, and I suppose a substantial percentage of the 78 percent have no intention of flying, or they would have done so before now.

Mr. KASHIWA. What I want to bring before the committee is this: this rise in costs, when people hear about the prices of things in Hawaii, the tourists, instead of being encouraged to go out there, it has a deterring effect. For example, this morning we heard about your \$3 haircut in Alaska. When a tourist hears about this, he says, well, it must be pretty high cost out there, just that index alone. And it does have a deterring effect. And I think that, although tourists don't go down there on ships, still this economy there should be as attractive to them as much as possible.

Senator BARTLETT. Well, I think we ought to have available not only by way of attachment, but we ought to read into the record, a few of the food price differentials which you noted in your attach-

ment 3. These figures come from the Bureau of Labor Statistics of the U.S. Department of Labor, and I note, Mr. Attorney General, that you inform us that the 1959 average price of bacon, sliced, per pound, on the mainland was 65 cents—or approximately that, and in Hawaii it was 84 cents, 85 cents almost. And salmon—we must get that in the record, of course—pink, 62 cents, and in Hawaii it was 66 cents. The differential is not so high there, thank goodness, because we want you to eat lots of Alaska salmon.

Mr. Grinstein just gave me a horrible thought. He said you might be getting some of that salmon from Japan. If you are, don't.

Butter costs 79 cents on the mainland, and in Hawaii 83 cents. Potatoes were 6.066 cents a pound on the mainland and 11.6 in Hawaii.

These are important considerations, and if the higher prices in Hawaii don't arise on account of the transportation system, I don't know what the reasons would be.

I think that two items especially that you refer to are of great importance. You said that you are discovering that the competition with your pineapple industry has reached the point where one large factory is going to have to close down, and that the small foreign cars are proving so popular that increasing numbers are brought in on foreign ships.

Would you agree with me, Mr. Attorney General, when I say that I have a conviction that it is just as important in respect to maintaining a fleet in being to have them serving in these offshore areas as in the foreign trade and the ships might, and even could, be more readily available in time of need?

Mr. KASHIWA. I think it is just as important; I agree, Senator.

By the way, Senator, there is a very interesting aspect of this lumber shipments out of Canada coming to Hawaii.

Senator BARTLETT. Increasing?

Mr. KASHIWA. Increasing; yes.

Senator BARTLETT. You mentioned, as I recall, that transportation costs amount to 6 percent of the total cost of a product in Hawaii.

Mr. KASHIWA. That is not the exact statement I made.

Senator BARTLETT. I didn't think it was. What did you say there?

Mr. KASHIWA. This is 6 percent of all of our income.

Senator BARTLETT. Oh, yes; that's much different.

Do you have any comparative figures for any of the other states, in respect to transportation?

Mr. KASHIWA. No, we don't, Senator. This again, if it is really necessary, we can furnish.

Senator BARTLETT. It seems very, very high to me. I think we will seek that information from another source. We will try the ICC.

Mr. KASHIWA. By the way, this is both ways, eastbound and westbound put together.

Senator BARTLETT. I understand.

Now, your attachment 8 shows that a rate increase in the Hawaii trade of 10 percent went into effect on February 1, 1951?

Mr. KASHIWA. Yes.

Senator BARTLETT. And then again, January 1952, an additional 7½ percent; March 1, 1953, 8½ percent; March 1, 1955, 8 percent; July 15, 1957, 13.2 percent; January 20, 1958, 9 percent; and September 14, 1959, 12½ percent; adding up to a grand total of 88.79 percent.

Mr. KASHIWA. That is right.

Senator BARTLETT. Now you say the State is objecting to the latest increase?

Mr. KASHIWA. That is right, the September 14, 1958, 12.5 percent. We have filed a protest and it is in litigation now as to whether that is just or not. It is now before the examiner.

Senator BARTLETT. In the meantime, are these higher rates being collected?

Mr. KASHIWA. Yes.

Senator BARTLETT. Is the money thereby taken by the carriers being segregated for possible refund?

Mr. KASHIWA. No, it is not.

Senator BARTLETT. So what does that mean? If the Federal Maritime Board were later to determine that the increase was not warranted, the shippers and/or consumers would not be reimbursed?

Mr. KASHIWA. They will be.

Senator BARTLETT. It is being segregated, then, held in escrow?

Mr. KASHIWA. Well, even though it is not held in escrow, my understanding is there will be a reimbursement to the shippers.

Senator BARTLETT. There is a reimbursement provided in any case?

Mr. KASHIWA. Yes.

Of course, the difficulty would be turning that over to the consumer. This would be a very, very difficult problem.

Senator BARTLETT. Now on page 13 of your statement you said that Matson, for example, has estimated that to replace its World War II fleet with modern vessels would require the expenditure of \$300 million. Have you learned whether Matson is ready, able, or even willing to put up any such sum of money for replacement?

Mr. KASHIWA. I do not know. But this is actually taken from our case, FMB docket No. 769. These figures are taken from the docket.

Senator BARTLETT. A company, with every good intention in the world, might not be able to do this.

Mr. KASHIWA. It is a very large figure.

Senator BARTLETT. Then going one step further on that—or one further league on that sea, or that metaphor, maybe—what, aside from national defense considerations, in your opinion, is going to occur if something is not done in this situation, and these ships were out and the inflationary process continues?

Mr. KASHIWA. Well, either these ships will be remodeled, remodeled, remodeled, and at the end I am sure that they will not have any use as ships for defense, but we will have to get along with very old unsatisfactory ships, because \$300 million is rather prohibitive, and unless some Federal aid comes in, whether by shipbuilding subsidy or something of that nature, the future is very, very dark.

In fact, this last 12½ rate case, where the State protested—there is a great deal of interest in the State; everybody is interested about this—in fact, the case was started after a joint resolution by the House and the Senate, the State legislature, and the whole project is being fought and financed by the State government; in other words, the State is fully interested in the entire picture, and this is one of the phases—who is going to rebuild the ships hereafter.

Senator BARTLETT. Would it be fair to say in the opinion of the people of the State of Hawaii, without trying to blame or praise the carriers concerned, this 12½ percent increase coming after so many

others in the last 8½ years before this, had caused the people to become alarmed as to their economic future?

Mr. KASHIWA. That is right.

Senator BARTLETT. Mr. Grinstein?

Mr. GRINSTEIN. Mr. Kashiwa, when Chairman Stakem was testifying, on page 8 of his testimony he said the following:

It is assumed that before any conclusion is reached on the various alternative ways of lowering freight rates an effort will be made to settle definitively the relationship of the ocean carrier's charges to the ultimate consumer costs.

I take it he had reference to the possibility there might be a higher markup by the retailer or distributor in Hawaii. Has there ever been a study made of this to find out whether there is a higher markup?

Mr. KASHIWA. No, we haven't. But it is definite that before the goods go to Hawaii it has to pay that freight rate. I mean a certain freight bill, and certainly where the figures definitely show in Hawaii the cost of living is much higher, this freight bill has some influence in that area. Now as to exactly how much, this I cannot put my finger on. It would be very difficult to trace back. But definitely there is a direct relationship.

Mr. GRINSTEIN. But there hasn't been any study that would allocate so much of the cost to the freight rate?

Mr. KASHIWA. No.

Mr. GRINSTEIN. In a rate proceeding before the Federal Maritime Board, has the State of Hawaii contested these rates at least in part on the grounds of economic impact or the needs of a developing economy, or has it been mainly on the rate formula?

Mr. KASHIWA. The entire group, including all the attorneys, took a trip out to Hawaii, and we had a 5-day session there, and people from the various islands, people in business in Honolulu, all appeared before the examiner and there was quite a lengthy hearing on the impact on various industries, for example, the vegetable men, and the dairy industry, and there was quite a great deal of expert testimony put on by the University of Hawaii Economics Department.

That phase of the case I would say was most fully explored.

Mr. GRINSTEIN. Has that material appeared in the Federal Maritime Board opinions, or the examiner's report, written?

Mr. KASHIWA. Well, there has been no examiner's report; but this is all in the transcript. It covers hundreds and hundreds of pages. The case has not been decided as yet.

Mr. GRINSTEIN. I understand that.

You were talking just about the last case; I was thinking of more. There have been seven of these, and over the period of seven—

Mr. KASHIWA. I want to point this out. It is only in the last 12½ percent raise that there was a real contest of any nature whatsoever.

Senator BARTLETT. Did the State ever protest before then, in these 8½ years, that you know of?

Mr. KASHIWA. No.

Mr. GRINSTEIN. This is the first time?

Mr. KASHIWA. Yes.

Senator BARTLETT. Mr. Bourbon?

Mr. KASHIWA. I think this is the first raise that came after we became a State.

Mr. BOURBON. Just one thought occurs to me: Do you think some of your people are taking advantage of this situation, some of the people that are not affected by it at all, for instance, to the point where a Hawaiian shirt costs 20, 22, or 25 cents here, and it cost 45 cents in Hawaii, to have ironed? Do you think a lot of people who are really not bothered by it at all are taking advantage of the situation and putting their little bite on things, too?

Mr. KASHIWA. This is an area where it is very difficult to say. A rise in a basic thing like freight rates has an indirect impact all over, and it has a tendency to spiral the rest of the things. As to how much, for example, the barber is affected, or how much the clothes are affected, to bring this down to a close mathematical formula is very difficult; but there is, I would say, an impact which is indirect. But it does have an effect.

Mr. BOURBON. That is all.

Senator BARTLETT. Off the record.

(Discussion off the record.)

Senator BARTLETT. On the record.

Mr. KASHIWA. For example, a laundry delivery truck, the price for a delivery truck in the islands is added on and this runs into \$200 or \$300 per car. This is an area which he must earn extra to pay for that truck. And these things cumulate. That is my point.

Of course, the person who has a shirt washed, it costs him a little more, so he charges a little more. That is the effect of it.

Senator BARTLETT. Do you have adequate service frequency?

Mr. KASHIWA. Right now?

Senator BARTLETT. Yes.

Mr. KASHIWA. As far as I know, yes.

Now, there is one thing I would like to say, that we have four islands, and in between these islands, as I have stated, there are barge services. Now on the outer islands, like Kauai, Hilo, and Nawiliwili, some of the merchants there may want more service, naturally, but that is tied—as far as Matson is concerned—with the sugar, the pineapple loading, so whatever they may not be able to get on Matson shipping directly at those ports will come to Honolulu and will be barged over to the outer islands.

Now, this is as far as the outer island inadequacies—I wouldn't call it an inadequacy, but it is a situation which is there.

Senator BARTLETT. But you have no complaint to make about frequency of service between your principal ports and the mainland?

Mr. KASHIWA. No.

Senator BARTLETT. How many carriers serve Hawaii from the U.S. west coast?

Mr. KASHIWA. The U.S. west coast only?

Senator BARTLETT. Yes.

Mr. KASHIWA. This would be appropriate for the Matson people. I have the list of ships here.

Senator BARTLETT. I mean as to the number of companies, rather than ships of a given company?

Mr. KASHIWA. Matson is the main one. Of course, we have some tramp—in the rate case, for example, it was apparent there are some tramps that pick up scrap tin and bring tin down. Now, that is on non-Matson ships.

Senator BARTLETT. Does American President Lines serve Hawaii?

Mr. KASHIWA. Yes.

Senator BARTLETT. With freight?

Mr. KASHIWA. No.

Senator BARTLETT. Just passenger service?

Mr. KASHIWA. Well, very small freight, if any. It is mostly passenger.

Senator BARTLETT. How about States?

Mr. KASHIWA. No. They have an application pending at this time, as I understand it.

Senator BARTLETT. But Matson carries the majority of the freight?

Mr. KASHIWA. Yes.

Senator BARTLETT. Do you have any questions, Mr. Goding?

Mr. GODING. What about other contract or industrial carriers? You mentioned some tramps carrying tin and scrap. Does industrial, contract, or other shipping enter the picture very appreciably?

Mr. KASHIWA. In our rate case it appeared that this tin deal is a very special contract service. The other areas, there are very few other products brought in on a similar basis as tin.

Mr. GODING. I wondered whether fertilizer or bulk cement—

Mr. KASHIWA. Bulk cement; yes. They used to have their own ship. But lately we manufacture our own cement out there. Of course, there is a lot of oil, gasoline, and that type—tankers—that come out there. Standard Oil.

Mr. GRINSTEIN. On page 8 of your testimony you mentioned foreign products coming in on foreign-flag vessels to Hawaii. Is it your opinion that if the rates continue to increase in the trade that the Hawaiian people will begin to look to other countries for their sources of supply and the foreign-flag vessels for the source of their services?

Mr. KASHIWA. Well, we don't necessarily look to them. For example, the Australian or New Zealand meat comes in in refrigerated ships and the meat is dropped in Honolulu and cut up and sold, and it is cheaper than the mainland meat, and this causes problems.

Mr. GRINSTEIN. I wasn't referring necessarily to the present time. I take it there are some foreign products presently competing with mainland products in Hawaii. But is it your opinion that in the future if the rates continue to increase, the ocean freight rates between the mainland and Hawaii, that Hawaii will have to look to foreign sources for their services and supplies?

Mr. KASHIWA. We don't look to it, but it is kind of a forced situation there.

Senator BARTLETT. In that connection, I note by your attachment 6—and that was a very good reply you just made, Mr. Kashiwa—that this trend toward foreign importations has been very pronounced since 1946. Using the period 1946-50 with an index figure of 100, we discover that in 1958 the index for imports from the mainland, according to this attachment, was at 140.

Mr. KASHIWA. Yes.

Senator BARTLETT. But the index for foreign importations in the 1946-50 period, was, in 1958, 274, so there is a gain of only 40 points on Hawaii's importations from the U.S. mainland, but 174 points on importations from foreign lands.

I think that that goes to the heart of what we are discussing here today—that we may be pricing ourselves out of some mighty valuable and important markets.

MR. KASHIWA. This is especially so in pineapples. Of course, it is on the reverse; we are the suppliers of the pineapples, but as I understand, it is cheaper to ship pineapples from Formosa to San Francisco than from Hawaii to San Francisco, and, therefore, we have a very, very difficult situation there. Foreign pineapple is underselling our pineapple.

Senator BARTLETT. When the pineapple from Formosa travels to San Francisco either on foreign-flag carriers or U.S.-flag carriers, that operation is subsidized, and yours is not.

MR. KASHIWA. That is correct. And it is a very serious situation on the island of Kauai. That is the extreme northernmost island. The sole economy there is sugar and pineapple. The town of Kapaa which, I would say, is about—I don't know the exact population there, but it used to be a very thriving town. The owners of the cannery there have announced that they are not going to continue that cannery, and it is creating quite an economic problem there.

Senator BARTLETT. How many people will that throw out of work, do you judge, in the fields and cannery?

MR. KASHIWA. Right now it has not been closed, but I don't know the exact figures. But I can give you the exact economy of that Kapaa situation from the economic development section of our State government.

Senator BARTLETT. I wish you would furnish a statement on this particular subject and this particular place.

(See letter from Mr. Kashiwa, p. 319.)

MR. BOURBON. With regard to the pineapple from Formosa, do you have any figures as to the cost of the pineapples at Formosa, before put on the ship, as compared to the cost of yours?

MR. KASHIWA. No, I don't have them, but I can get those for you from the pineapple people.

MR. BOURBON. That might be quite a factor in the lower cost from Formosa.

MR. KASHIWA. Yes. I would like to state this: in this 12½ percent rate case, the pineapple people hired special counsel from San Francisco, and he was right beside us and right from the very beginning to the end, protesting this raise, as far as they are concerned. Of course, there is an eastbound business, but they were right in there pitching with us.

Senator BARTLETT. I am going to ask the committee staff, in line with your inquiry, Mr. Bourbon, to see what we can discover about the production of pineapple on Formosa, when they started the export, and what their production costs are compared to those in Hawaii.

MR. BOURBON. Yes, sir.

Senator BARTLETT. Thank you very much, Mr. Kashiwa. You have given us much useful information.

Senator BARTLETT. The next witness will be the Honorable Robert Oshiro, member of the House, Hawaii Legislature. He has testified before this committee previously on allied subjects, and we are glad to have him once more in a different setting.

STATEMENT OF ROBERT OSHIRO, MEMBER OF THE HOUSE, HAWAII
LEGISLATURE

Mr. OSHIRO. Thank you, Mr. Senator.

Senator BARTLETT. You get your shirts done cheaper here, too.

Mr. OSHIRO. I would like to inform the committee, as well as the press, that my oral presentation will be a condensation of my written statement and there may be a slight variation in regard to emphasis.

Mr. Chairman, members of the Merchant Marine and Fisheries Subcommittee of the Senate Committee on Interstate and Foreign Commerce, my name is Robert C. Oshiro, member of the House of Representatives, first State Legislature of the State of Hawaii.

Thank you very much for this opportunity to speak at this hearing on a matter which so vitally concerns us in Hawaii, as well as the people of Alaska and Puerto Rico, and is, in our opinion, vitally important to the national economy and defense.

We are extremely happy that you have chosen to examine the effect of the Federal maritime laws on the economies of the domestic off-shore areas. Although I am not prepared to give detailed remarks, inasmuch as I was asked to testify on very short notice, nevertheless I sincerely hope that whatever I may say will be of some small help to you in better understanding our situation in Hawaii.

Mr. Chairman, before I proceed any further, I would like to request that my written statement and Resolution No. 33 adopted by the House of Representatives of the first Legislature of the State of Hawaii, general session of 1961, be entered in the record of this hearing with your approval and with the approval of the members of this committee.

Senator BARTLETT. That will be done. Without reading it, will you give us the general sense of that resolution?

Mr. OSHIRO. Mr. Chairman, I will go into the matter of the resolution at the end of my remarks.

Senator BARTLETT. All right.

Mr. OSHIRO. Gentlemen, because of the geographical location of the State of Hawaii, we are dependent upon ocean transportation for survival. We depend on ocean transportation for our basic necessities—our food, shelter, and clothing. Literally, ocean transportation is our lifeline.

Freight rates and freight rate increases are not directly the subject of this hearing, but I believe they are of critical significance when considering the effects of the present maritime laws on Hawaii, Alaska, and Puerto Rico.

As far as we can see, freight rates will continue to rise in order to meet the American wage standards, ship construction and operational costs, unless the present maritime laws are modified. The larger the bill we must pay for ocean transport, the less we have to spend on the goods we need and to invest in the businesses which will contribute to our growth. As an illustration, today in Hawaii it costs \$275 to ship an item which could have been shipped for \$100 in 1946.

Gentlemen, we recognize that it is the national policy to sustain that portion of the merchant marine which competes with foreign car-

riers through operating and construction subsidies, and to protect the coast trade from foreign competitors by excluding foreign ships from such trade. This policy is now incorporated into our laws pertaining to our merchant marine.

1. With the use of subsidies to sustain that portion of the merchant marine, which competes with foreign carriers, we have no argument.

2. But in regard to the domestic carriers which serve Hawaii, Alaska, and Puerto Rico, we would like to emphasize that because subsidies are not available to them, they must maintain shipping revenues high enough to meet wage standards, operating and construction costs, which means that freight rates will continue to rise.

This means that in maintaining our national policy, the domestic carriers and their customers pay the full cost of supporting one portion of the merchant marine, while the general taxpayers pay a substantial part of the cost of the other portion of the merchant marine.

Not only do I and my fellow citizens of Hawaii as general taxpayers support that portion of the merchant marine in foreign trade, as we should, but in addition we pay a special kind of tax in the form of higher prices for consumer goods and in the form of lower sales or return on our exported goods in order to support the nonsubsidized portion of the merchant marine. It is this second kind of tax which we believe is unfair.

Briefly, I have stated the problem as it affects our people. Now, in regard to solutions, I am of the opinion that the wisdom of the members of this committee and Congress will develop solutions acceptable to the consumers and the ocean carriers within the framework of the concept of the national policy now embodied in the maritime laws.

However, as a member of the House of Representatives of the State of Hawaii, may I direct your attention to the resolution which suggests that an inquiry be made as to the feasibility of granting financial assistance to domestic carriers so that the cost of sustaining this portion of the American merchant marine will not fall entirely upon the people of Hawaii; and should such subsidies be granted, in regard to Hawaii, that the Federal Maritime Board be requested to insure the admission of other subsidized carriers to the Hawaii-mainland trade so that competitive and comparable rates can be established.

It is my humble opinion that a policy of subsidizing domestic carriers would foster and maintain the national policy of maintaining a strong merchant marine for the Nation's welfare and national defense. It is vital to our national security and to our defense that the United States have immediately available adequate ships for use in transporting troops and materials in case of war, as I believe that this is one of the most important reasons for subsidizing American-flag vessels engaged in foreign commerce. I believe ships in the domestic trade are much more readily available in time of war, as experienced in World War II, in which Hawaii was one of U.S. bastions of defense in the Pacific.

Thank you very much for your kind and considerate attention. I will be most happy to answer any questions you may have.

(Statement follows:)

STATEMENT OF MR. ROBERT OSHIRO, MEMBER OF THE HOUSE OF REPRESENTATIVES, STATE OF HAWAII

Mr. Chairman, thank you very much for inviting me to speak at this hearing on a matter which so vitally concerns us in Hawaii. We are extremely pleased that you have chosen to examine the effect of the Federal maritime laws on the economies of the domestic offshore areas. We are also very appreciative of the work performed by Puerto Rico and Alaska, the two areas which share so many of our problems, in investigating this problem and in submitting the results of their studies to you for your consideration. I sincerely hope that my remarks will be of some small help to you in better understanding our situation in Hawaii.

Sometimes even we in Hawaii forget for a moment how completely dependent we are on water transportation. It is our economic lifeline in every sense of the word. The cars on our roads, the paper in our offices, the furniture in our homes, the equipment in our factories—for all these and hundreds of other items we depend on water transportation. Two-thirds of our food and 90 percent of our consumer goods come from the mainland over the oceans. We, of course, produce in the islands some of the things we need, but we are in no sense of the word self-sufficient nor should we be.

Our insular economy is built in large measure on exchange—we export sugar and pineapple and import goods. The primary market for the sugar and pineapple which we grow, harvest, and process lies not in the islands but again over the ocean on the mainland. Thus our lifeline works in both directions—we are dependent on sea transportation to bring us the goods we consume and to move the products we must sell, which in turn earn for us the income we need to purchase the goods we require.

Not only are we utterly dependent on sea transport but we pay a high price for this dependency. Of every dollar we spend outside of Hawaii, 5 cents is paid to mainland and foreign concerns for ocean and air freight. And since only a small portion of our goods are moved by foreign firms and only a minute portion by air freight, almost all of the 5 cents is paid to mainland concerns for ocean transport. And this 5 cents is in addition to what we, like the citizens of any mainland State, must pay as our share of the cost of transporting goods from the farm or factory to the point of use, or in our case the port of departure or what our sugar and pineapple companies must pay for rail freight on the mainland. This cost of sea transport then is for us a cost over and above that which you would expect a mainland consumer or producer to pay.

Study after study has demonstrated the impact which these costs have on our insular economy. Staple goods, for example, are priced measurably higher in Hawaii than on the mainland, a result of the fact that a distributor pays more for food landed in Hawaii. Milk costs more in Hawaii than almost anywhere on the mainland. This higher cost is a result of paying from $3\frac{1}{2}$ to 4 cents per quart for bringing items to Hawaii which are necessary for milk production. The story with respect to nonfood products is similar. A large percentage of the cost of everything we use and consume in our homes, offices, schools, farms, and factories is for shipping. And while this is a cost we shall have with us always in Hawaii, it is the magnitude of that cost and its effect on our cost of living, our standard of living, and our rate of economic growth that is of such concern to us.

Not only is our dependence on sea transport both complete and costly, but in addition we must rely on a single company—Matson Navigation—to move 90 percent of the ocean freight between Hawaii and the mainland. Freight rates and freight rate increases are not directly the subject of this hearing, but I believe they are of critical significance when considering the effects of the present maritime laws on the State of Hawaii. Frankly, as far as we can see, domestic tariffs will continue to rise unless the present laws are modified, and such increases will continue to hamper our economic growth and depress many of our local business activities. The larger the bill we must pay for ocean transport, the less we have to spend on the goods we need and the less we have to invest in the businesses which will contribute to our growth. The cost of transporting freight has increased tremendously since 1946. Today, it costs \$275 to ship an item which could be shipped for \$100 in 1946. This 175 percent increase in the cost of shipping general cargo compares to a 63 percent increase in the Honolulu consumer price

index since the year 1943. And while admittedly our local price index has a number of limitations, it is doubtful that such limitations are sufficient to explain away all of this difference.

We also recognize that some of the modern freight handling methods adopted by Matson should tend to reduce the cost of shipping some items and thus to lessen a little the cumulative effect of these increases. In spite of these allowances, the fact remains that we live on islands utterly and completely dependent on a single shipping line, the costs of whose services have increased drastically in a period of only 15 years. And we know who pays this bill when we buy cereal, machines, lumber, equipment, and the other items that are essential to the functioning of our modern economy.

We recognize that it is national policy to maintain a strong merchant marine and to sustain that portion of the merchant marine which competes with foreign carriers through operating and construction subsidies. With the use of these means to achieve the national policy, we have no argument.

However, as you know, subsidies are not available to the merchant marine which serves offshore areas such as Hawaii, Alaska, and Puerto Rico. Rather, this portion of the merchant marine is sustained by forbidding lower cost, foreign competitors to carry domestic traffic, and thus permitting the domestic lines to pay their costs and earn a profit out of shipping revenues.

This means that to achieve and maintain the national policy, the domestic shippers and their customers pay the full cost of supporting one portion of the merchant marine, while the general taxpayers pay a substantial part of the cost of the other portion of the merchant marine. Not only do I and my fellow citizens in Hawaii as general taxpayers support that portion of the merchant marine in foreign trade, as we should, but in addition we pay a special kind of tax in the form of higher prices for consumer goods and in the form of lower sales or return on our exported goods in order to support the nonsubsidized portion of the merchant marine. It is this second kind of tax which we believe is unfair.

We respectfully request that the matter as to the feasibility of granting subsidies to our domestic carriers, similar to those granted to other American-flag lines, be considered by this committee so that the cost of sustaining the portion of the American merchant marine serving domestic areas will not fall entirely upon the people of Hawaii, Alaska, or Puerto Rico.

In regard to Hawaii, should such subsidies be allowed, we further respectfully request that Hawaii-mainland trade be opened to other carriers so that competitive and comparable rates will be established, thus assuring to the people of Hawaii a share in the benefits which would result from granting subsidies.

I have been authorized by the Hawaii House of Representatives to transmit to President Kennedy, to Senator Magnuson, and to the members of the Senate Committee on Interstate and Foreign Commerce and its Subcommittee on Merchant Marine and Fisheries the resolution adopted by the House requesting your assistance in this matter of properly placing the burden for sustaining that portion of the merchant marine which serves Hawaii and other similar areas.

Gentlemen, we are very pleased that you are so seriously and exhaustively investigating this problem which has plagued us so long that sometimes we have even tended to ignore it. But ocean transport is so vital to our very existence, and the cost of that transport such a significant factor in the cost of the things we buy and in the amount of income we receive from the items we sell that one cannot either understand the Hawaii of today or discuss the Hawaii of tomorrow without considering the problem of ocean transport. I know, gentlemen, that you are as cognizant as I of the opportunity you have to rectify an inequity and of the tremendous beneficial impact your actions may have on the future of our State and our people.

Thank you.

(Resolution 33 follows:)

RESOLUTION

Whereas, because of their geographical location, the people of Hawaii are greatly dependent upon the ocean carriers of Matson Navigation Co. for their exporting and importing trade; and

Whereas the ocean carriers of Matson Navigation Co., although considered a part of the American merchant marine, are classified as domestic carriers or "common carriers by water in interstate commerce" and are not qualified to receive any financial assistance from the Federal Government but are expected

to pay their cost and earn a profit out of shipping revenues, which means that the people of Hawaii are required to assume the great burden of cost and profit of Matson's ocean carriers; and

Whereas it is the policy of the United States to sustain the American merchant marine through operating and construction subsidies amounting to as much as 70 percent of wages and 50 percent of construction costs in order to enable American-flag lines to operate successfully with tariffs and other charges similar to those charged by foreign ocean carriers; and

Whereas such a policy to sustain the American merchant marine is beneficial to all of the people of the United States of America and it is just as appropriate that the Nation as a whole pay for the maintenance of such a policy so that the cost will not disproportionately fall upon the people of Hawaii and other domestic shippers and their customers who pay general taxes to sustain foreign shippers of the American merchant marine: Now, therefore, be it

Resolved by the House of Representatives of the First Legislature of the State of Hawaii, general session of 1961, That the Honorable John F. Kennedy, President of the United States of America, the Honorable Warren G. Magnuson, chairman, and all members of the Senate Committee on Interstate and Foreign Commerce and its Subcommittee on Merchant Marine and Fisheries are hereby respectfully requested to investigate the possibility of and give serious consideration to granting financial assistance to Matson Navigation Co. similar to subsidies granted to other American-flag lines in order that the cost of sustaining this portion of the American merchant marine will not fall entirely upon the people of Hawaii; and be it further

Resolved, That, if such subsidies are granted, the Federal Maritime Board be requested to insure the admission of other subsidized carriers to the Hawaii-mainland trade so that competitive and comparable rates can be established; and be it finally

Resolved, That copies of this resolution be transmitted to the Honorable John F. Kennedy, President of the United States of America, the Honorable Warren G. Magnuson, chairman, and all members of the Senate Committee on Interstate and Foreign Commerce and its Subcommittee on Merchant Marine and Fisheries, the Federal Maritime Board, and the Honorable Oren E. Long and the Honorable Hiram L. Fong, U.S. Senators from Hawaii, and the Honorable Daniel K. Inouye, U.S. Representative from Hawaii, by the Honorable Robert C. Oshiro, representative of the First Legislature of the State of Hawaii.

Senator BARTLETT. It was good of you to make the trip clear from Honolulu to Washington to present your views before this committee. That which you had to say, which you incorporated in your written statement, and which you abbreviated in your presentation will be carefully considered, I assure you, by the committee.

Let me ask you: When was that resolution adopted?

Mr. OSHIRO. Mr. Chairman, that resolution was adopted on Thursday, last week, the day I left for Washington.

Senator BARTLETT. It is brandnew, then?

Mr. OSHIRO. Yes, Mr. Chairman.

Senator BARTLETT. Should we interpret this by the Hawaii House of Representatives as reflecting an especially keen interest in this problem?

Mr. OSHIRO. Mr. Chairman, I think the resolution and my presence here indicates that as far as the house of representatives is concerned we are very much interested in the entire problem and we intend to keep close contact with your office and with this committee as to the future costs, and wherever we can help we would like to do so.

Senator BARTLETT. Then you were directed or requested by the house of representatives to come here to testify?

Mr. OSHIRO. Yes, Mr. Chairman.

Senator BARTLETT. And the legislature is now in session?

Mr. OSHIRO. Yes, Mr. Chairman.

Senator BARTLETT. Notwithstanding the fact that your presence there would otherwise be taken for granted, you thought it important enough to leave for several days to come here?

Mr. OSHIRO. Yes, Mr. Chairman.

Senator BARTLETT. Now, you mentioned subsidies. That is a word not unheard of in these Halls. There are subsidies of one kind or another, I guess. But the word is not too popular in all quarters yet; certainly not, I suspect, with you or with me. We prefer some other means of making suitable arrangements, if they are to be found. Do you have any alternate ideas as to how this problem could be resolved?

Mr. OSHIRO. Mr. Chairman, I arrived earlier in Washington than I expected, because I had short notice and I was not familiar with the problems. But, like many other things, the more you look into the problems, the more you find that the solutions create problems also. Frankly, I do not have the experience, nor the knowledge, nor the background to contemplate any specific suggestions.

The only suggestion that we thought of back in Honolulu, at the time the resolution was drafted, was on the basis of what meager information we had. We felt that if the carriers in the foreign commerce could be subsidized that we saw no reason why the domestic carriers could not also be subsidized. But as far as the other solutions are concerned, we would rather leave it up to the wisdom of the committee.

Senator BARTLETT. We assuredly would not ask you to appear here before the committee as an expert on maritime transportation.

Do you have the feeling that these repeated freight rate increases are bearing down hard upon the individual citizen of Hawaii?

Mr. OSHIRO. Yes, Mr. Chairman, for this reason: The figures quoted by Senator Long, as well as the attorney general, are correct. But those figures, I believe, take into consideration the years from 1950 to 1959. Just for curiosity, before I left Hawaii, I had a reference bureau check into the rates since 1946 and the astounding thing is what we could have shipped in 1946 for a hundred dollars would cost today, in terms of freight alone, \$275. That means that we have less money to buy other consumer goods or to buy other products from the west coast or any other place; and that is the reason why I would like to emphasize the factor of national economy, because Hawaii is a good market for a lot of the west coast industries. But if the tariffs keep on rising, it is going to get to a point where we may have to turn to other sources for our products, like the attorney general indicated. We buy a lot of lumber from Canada, whereas we used to buy it from Washington State and Oregon and California.

Senator BARTLETT. Of course, these figures you produced, to which you just referred, are startling that it costs \$275 now to ship an item which could have been shipped for \$100 in 1946. But I don't suppose anyone would contend that this represents an average of the inflationary process to which this country has been subjected since then. It is extraordinary, is it not?

Mr. OSHIRO. Yes, Mr. Chairman.

Senator BARTLETT. Mr. Grinstein?

Mr. GRINSTEIN. I have no questions.

Mr. BOURBON. I have none.

Mr. GODING. I have none.

Senator BARTLETT. I want to thank you very much. And I would deem it a personal favor, Mr. Oshiro, if you would thank your colleagues in the house of representatives for having made it possible for you to come here to testify before the committee, because you have given us some data that otherwise would not have been available. But, more importantly, you have contributed by informing us of the concern of the people of Hawaii in respect to this problem. I personally am deeply appreciative.

Mr. OSHIRO. Thank you, Mr. Chairman.

Senator BARTLETT. Mr. Goding just informs me that the next scheduled witness, Governor Merwin of the Virgin Islands, will not appear before the committee.

Incidentally, it might be mentioned that the Virgin Islands do not fall within the provisions of the cabotage laws which apply to these other areas.

Let's go into recess for 10 minutes.

(A short recess was taken.)

Senator BARTLETT. The subcommittee will be in order.

It is our pleasure now to hear from the former Associate Solicitor of the Department of the Interior and the present secretary of Guam, Mr. A. M. Edwards.

STATEMENT OF A. M. EDWARDS, SECRETARY OF GUAM

Mr. EDWARDS. Thank you, Mr. Chairman.

I wish to take this opportunity on behalf of the people of Guam to say how deeply appreciative we are of this opportunity to appear before you and express our views on this matter, which is of vital importance to the island of Guam. Governor Flores asked I express his regrets he was unable to be present and he asked that I appear and present his views.

As you know, Guam is the most distant of the U.S. territories from the mainland, being some 3,200 miles west of Hawaii. In fact, Guam is the gateway to the United States from the Far East, being approximately 1,500 miles east of the Philippines. It is the largest and the greatest populated of the Marianas Islands, having a land area of 221 square miles, with a population of about 70,000 persons, of which about 30,000 are natives of Guam and the rest composing the personnel of the Armed Forces, their departments and civilian personnel connected with the various activities of the military and other Federal and territorial activities.

Our present economy is based on furnishing services to the Armed Forces. We have very little industry, although effort is being made at the present time to revitalize the use of coconuts, which before World War II was one of the main sources of income for the territory. While we are attempting to do this, we have discovered that a large number of our coconut trees are diseased and we are having a survey made now by a doctor who was formerly of the University of the Philippines to determine whether or not we can utilize our coconuts.

Senator BARTLETT. If he can't do it, remember the Bartlett tree surgeons.

Mr. EDWARDS. I certainly will.

We understand and we have had information that there is a new machine that will produce not only coconut oil but also coconut flour, and utilize the fiber of the coconuts and, if this would develop, if this machine is practical, and can be economically operated, feasible for operation on Guam, it would give us some industry.

There is little agricultural activity, although efforts are being made to increase the production of food. We are working now in developing some poultry, but as to agriculture we are still confined more or less to truck gardening, and we do not begin to serve anywheres close to 10 percent. It is confined to mostly the use of bananas; we have a few pineapples, which are used for the local market; but nothing is exported and in fact we have to import all of our fresh fruits and vegetables.

As I have said, we import over 90 percent of all of our food products, and 100 percent of all other consumer items needed for the civilian economy. Therefore, transportation is a vital connecting link to our lifeline. In other words, Guam cannot survive without sea transportation.

Guam, too, has been and is being affected by general rate increases. We have had two recent rate increases, with the second coming prior to the final determination of the first. And these cases are still pending before the Maritime Board.

We are also in a similar position as is Hawaii, since coastwise laws which protect American maritime industry in the shipment of goods between the coastal cities on the mainland likewise apply to Guam. And at this point we recognize that since coastwise laws applied to Guam, the shipper of merchandise in an American-flag vessel from the States—say it is shipped to Japan, that carrier gets a subsidy, whereas if it is shipped to Guam, which lies practically due south of Tokyo, being the same distance from the same city, the carrier gets no subsidy. And thus the people of Guam have to pay full rate, plus reasonable rate of return on their investment, in having all of our commodities transported and all the cargo transported to Guam.

In addition, we have, because of our location, and because of the nearness to the Far East, we are a vital link in our national defense and by reason thereof Guam does not enjoy the same privileges as the coastal cities on the mainland or in other areas under the United States flag, with regard to competition from foreign vessels.

By Executive Order No. 86-83, dated February 14, 1941, Guam was declared and reserved as a naval defense sea area and all foreign vessels are prohibited, unless their entry is authorized by the Secretary of the Navy.

Since this is a matter of our national defense, naturally we in Guam are not in a position to comment thereon. We only wish to call this matter to your attention so that the committee might be cognizant of this matter.

I should like to file with the committee an exhibit which shows the commercial inbound and outbound cargo broken down to show whether originating in the continental United States, Hawaii, or foreign countries, and this is broken down between two commercial carriers serving the area and it covers the years 1955 through the first half of 1956. It also shows the dollar value of this cargo, on the commercial cargo.

We also have here the military cargo, that is, carried by these civilian vessels, of the two carriers who serve that area. This does not include the cargo that is transported by the Navy.

In conclusion, I would like to say that the people of Guam feel that we should have some relief because as you can readily understand, since over half of our population is tied in with the military and have what we on Guam call "commissary privileges," the other half being the natives and the people connected with the civilian economy do not enjoy those privileges.

We get all of our products, food, consumer durables, through commercial lines. For example, it costs us, to buy a roll of toilet tissue, more for freight than the cost of the item itself. In fact, I think I was told that a box of toilet tissue runs around \$8 and the freight on it is \$11. So you can see how our economy is tied in to the shipping and when you realize that our carriers get no subsidy because we are within the confines of the coastwise laws, it makes it a rather hard and difficult situation to put upon our civilian economy, the high rate of transportation that we have out there.

That concludes my statement. I would be delighted to answer any questions.

Senator BARTLETT. Thank you, Mr. Edwards.

First, let me say the exhibit to which you referred will be accepted.

(The above-mentioned material follows:)

Report of cargo inbound-outbound, Guam, M.I.

Pacific Far East Line	1955 (58 vessels)	1956 (58 vessels)	1957 (55 vessels)	1958 (38 vessels)	1959 (36 vessels)	1st 6 months of 1960 (18 vessels)
INBOUND CARGO						
Originating in United States.....	29,633	50,952	81,109	51,232	94,806	42,686
Originating Hawaii.....	425	1,196	1,084	910	1,633	456
Originating foreign.....	11,484	12,488	11,574	16,188	9,487	5,988
Total commercial (short tons ¹).....	41,542	64,636	93,767	68,330	105,926	49,130
Total commercial (revenue tons ²).....	100,532	108,522	115,114	103,457	120,604	58,241
Military ex-United States.....	(³)	(³)	(³)	42,148	55,573	18,119
Military ex-Hawaii.....	(³)	(³)	(³)			
Military ex-foreign.....	(³)	(³)	(³)	22,821	2,840	2,005
Total military.....				64,969	58,413	20,124
OUTBOUND CARGO						
Destined United States.....	3,759	4,963	3,832	5,925	5,392	3,006
Destined foreign.....	40,705	38,768	19,294	4,907	26,486	14,605
Destined Honolulu.....	47	371	105	229	203	124
Total commercial (short tons ¹).....	44,511	44,102	23,231	11,061	32,081	17,735
Military destined United States.....	(³)	(³)	(³)	1,451	4,070	2,060
Military, foreign.....	(³)	(³)	(³)	2,162	1,783	1,227
Total military.....				3,613	5,853	3,287
American President Lines						
	(16 ves-sels)	(12 ves-sels)	(13 ves-sels)	(16 ves-sels)	(15 ves-sels)	(8 ves-sels)
INBOUND CARGO						
Originating in United States.....	12,351	9,427	12,200	18,559	12,467	6,887
Originating foreign.....	29	None	None	None	None	None
Total commercial (short tons ¹).....	12,380	9,427	12,200	18,559	12,467	6,887
Total commercial (revenue tons ²).....	20,441	17,280	21,950	29,834	23,295	14,611
Military ex-United States.....	(³)	(³)	(³)	13,148	19,846	8,749
Military ex-foreign.....	(³)	(³)	(³)	None	None	None
Total military.....				13,148	19,846	8,749
OUTBOUND CARGO						
Destined United States.....	150	71	169	471	390	50
Destined foreign.....	2,033	5,056	3,252	1,718	1,170	1,234
Total commercial (short tons ¹).....	2,183	5,127	3,421	2,189	1,580	1,286
Total commercial (revenue tons ²).....	3,590	10,533	7,987	7,252	6,024	4,557
Military destined United States.....	(³)	(³)	(³)	None	None	None
Military, foreign.....	(³)	(³)	(³)	158	85	35
Total military.....				158	85	35

¹ Short tons of 2,000 pounds.² Revenue tons of 2,000 pounds or 40 cubic feet.³ Not available.⁴ Honolulu, Hawaii.

Sources: Commercial manifests and bills of lading on file at commercial port. Military manifests on file at Naval Supply Depot, Guam. Compiled by employees of the commercial port of Guam and government of Guam.

Senator BARTLETT. What was the value of the imports for the last year for which there is a record, civilian?

Mr. EDWARDS. That is total import?

Senator BARTLETT. Yes.

Mr. EDWARDS. For 1959 it was approximately—we had \$24,180,179 imported from the United States; \$404,322 from Honolulu, Hawaii; and the foreign imports were \$3,734,310.

Senator BARTLETT. The goods thus imported were exclusively for the use of the civilian population?

Mr. EDWARDS. Yes.

Mr. BARTLETT. You told us, as I recall, that about half the civilian population is connected with our Military Establishment in one way or another?

Mr. EDWARDS. A little over half.

Senator BARTLETT. What do the remainder of the people do?

Mr. EDWARDS. Primarily serve military establishments.

Senator BARTLETT. But those who are not connected, I mean?

Mr. EDWARDS. Still servicing the establishments, like our civilian laundries service the people who take and work for the Government; private industry, as you know, the military buys quite a bit from local firms, whatever they buy locally, that is, things that are coming in, and really the principal function is serving the military and servicing them.

Senator BARTLETT. Do you know if the U.S. cabotage laws have been in effect ever since we have had jurisdiction over Guam?

Mr. EDWARDS. I am not certain just when they went into effect. We took jurisdiction over Guam in 1898, the Treaty of Paris. Is my memory right? Did it start in 1916 or when? I am not familiar enough with it.

Senator BARTLETT. We will allow you to consult your sources and furnish this information for the committee files and include the answer to the question I asked, which you couldn't be expected to answer offhand.

As a matter of practice, does the Navy permit many, or any, foreign ships to put in to Guam and deliver cargo?

Mr. EDWARDS. No, sir; none.

Senator BARTLETT. What U.S. carriers serve Guam?

Mr. EDWARDS. Pacific Far East and American President Lines.

Senator BARTLETT. You spoke about two recent rate increases. Of what order were they?

Mr. EDWARDS. I don't have the numbers of them. From the Maritime Commission.

Senator BARTLETT. Will you please also supply for the files at your convenience the dates and percentage increases applied. And it might be well to go back for a period of 10 years before the first of these rate increases and give us information as to what happened during that time.

Mr. EDWARDS. All right.

I would like to say in this connection that we have a local counsel in the government of Guam which was handling those rate cases, and he would be available to give any information to your staff on any of the background here on these specific items.

Senator BARTLETT. Very good. Thank you. What is his name?

Mr. EDWARDS. Eugene Stewart, of Hume & Stewart.

Senator BARTLETT. Here in town?

Mr. EDWARDS. Yes.

While his commitments precluded him from being here today, tomorrow he will be available any time that your staff might wish to contact him and will be delighted to cooperate and give you any information as to all of these finer points on these cases which are still pending.

Senator BARTLETT. How do you account for the fact that there has been such a slight development of agriculture there?

Mr. EDWARDS. Well, as you know, the minimum wage laws, Fair Labor Standards Act, applies to Guam.

Senator BARTLETT. Does that apply the same way as to Iowa, for example?

Mr. EDWARDS. The same way exactly. It is \$1 minimum now. So everybody who can get a job with the military gets a job with the military. As you know, our land is volcanic and coral. We have a terrific amount of insects that just devour crops as fast as you can put them in and the net result is it is extremely difficult to produce them and in the tropical climate it just keeps you busy trying to keep the undergrowth down. It grows faster than your crops. Being terrifically small areas, maybe 2- and 3-acre tracts, and that is a sizable tract, it keeps you busy trying to keep everything but the crops from growing and you cannot use mechanical equipment, it is not large enough, the areas are not large enough, the farmers are not sufficiently established that will permit them to do it.

Senator BARTLETT. Do the homestead laws of the United States apply to Guam?

Mr. EDWARDS. Well, no, they don't. No public land laws of the United States apply to Guam. And that is another situation. A large number of acres were used during the war, after Japanese occupation was ended, and the military came in, we just have acre upon acre of airfields under concrete strips. Our best and most productive land is there now. And it is truly amazing when you go onto that island and see the terrific buildup we had to have, which was so essential and such an important point in the war, but still they have removed a lot of the buildings and you just see acres of roads, tar roads, water-bound roads, concrete runways, and a lot of that land has not been returned to production and it would cost a terrific amount to get it back.

The Navy and the Armed Forces are trying as they determine, in their wise judgment, they don't need any land, they are turning it back, that is, some of it goes to the government of Guam and some of it was on lease, they acquired some of it, and in that way they dispose of it under our regular disposal laws.

But the conditions are such that people cannot take and make enough or get enough capital to start out and try to clear the land where there isn't concrete and still at the same time produce a crop and make enough, because they can live, as I say, they get our minimum wage, \$1, and our civilian economy is—our civilian workers try to get a job with the military.

That is the reason why, before World War II, copra was one of the main stabilized crops they had, very productive. But you cannot use coconut trees and generate copra with labor at \$1 and \$1.25 an hour.

Senator BARTLETT. It won't work out.

Mr. EDWARDS. It just won't.

Senator BARTLETT. Is the land fertile?

Mr. EDWARDS. Some of it is and some is not. The southern half of the island is very hilly and in fact that part will not produce very much of anything, because after you pass up 100 or 150 feet above sea level it becomes very arid and very hilly, very little arable land there. It is the northern half, and that is where we have all our air-fields.

Senator BARTLETT. What is the highest point on Guam?

Mr. EDWARDS. About 1,850 feet, I think.

Senator BARTLETT. How far south from Tokyo is it?

Mr. EDWARDS. It is about 1,600, I think.

Senator BARTLETT. In case you are curious, I am only asking you to educate me. I don't know this will be useful.

Mr. EDWARDS. Well, I think your colleague, Senator Gruening, and Senator Long, they made a trip out there, and I would strongly urge that every Senator, every Senator, should see Guam. Having served in Washington a number of years, working in these things, as you well know, for the last 6 or 7 years, you just don't realize the problems that you face when you go out there and see it. They are terrifically loyal people. It is truly a wonderful sight to watch these small Guamanian children all line up in the front of the school and make the pledge of allegiance to the flag in the morning. They are patriotic, very loyal, and energetic.

Senator BARTLETT. Are the services and facilities of the Farmers Home Administration available to people there?

Mr. EDWARDS. No. There is no Federal agricultural activity being done in Guam today.

Senator BARTLETT. How many Guamanians are there?

Mr. EDWARDS. A little over 29,000. That is the 1960 census.

Senator BARTLETT. How large did you say Guam is?

Mr. EDWARDS. 221 square miles. It is approximately 30 by 8, 30 miles long by 8 miles wide.

Senator BARTLETT. I don't know that when the witness from Alaska appears he will be able to give, if he so desires, situations comparable to that which you cited. I don't know he will deal specifically with toilet tissue, but situations where the freight is much higher than the original cost.

But let me say what you already well know: in other ways there are startling contrasts. You said the land area of Guam was 221 square miles and the Department of Interior recently created in Alaska a wildlife range of over 14,000 square miles of land with, perhaps, not much more agricultural activity there.

Now, Mr. Edwards, you are appearing here on behalf of the people of Guam, and you suggested that they need and they are entitled to some relief from the present situation relating to maritime transportation. Are you in a position officially or otherwise to inform the committee as to what you believe the nature of that relief ought to be?

Mr. EDWARDS. Well, naturally I cannot speak for the administration or the Department of Interior under which we all serve. I cannot speak officially, except I can say it was the idea of Governor Flores that we have to be put in a comparable position as the man who is shipping cargo from the United States to a foreign country, because

we are so far away. The coastwise laws were to protect the American maritime industry, going from New York, say, to New Orleans, around to San Francisco. But when you are approximately 6,500 miles from the mainland, which is much farther than a lot of foreign areas are, and whenever American carriers carry cargo to a foreign area, the people of the United States subsidize so he can compete with foreign carriers. The people of Guam don't have that. We don't get the benefit of that. And still we are much farther away and our rates, as you can recognize, because of the distance, we have to pay the straight out and out rate that the carrier has to demand for his rate of return, which makes it rather a high rate.

Senator BARTLETT. Out of your long experience in territorial matters, do you have any present recollection of why it is that the cabotage laws are not applied to the Virgin Islands and are to Guam?

Mr. EDWARDS. Well, when they wrote the Virgin Islands Organic Act they left it up to the President to determine. That was in 1936. It was left up to the determination of the President whether or not they should be applicable and he issued an Executive order determining they should not be applicable. The only other area, as I understand it—I am not an expert on coastwise or any maritime laws, because, as you know, in the Department our experience or my experience has just been with other laws which would come before us on various matters—but, as I understand, American Samoa is the only other area in which coastwise laws are inapplicable, and since the President made the Virgin Islands inapplicable, we, Puerto Rico, Alaska, and Hawaii were the only ones that were made applicable to it.

Senator BARTLETT. The President couldn't change the situation regarding Guam. That would have to be done by law.

Mr. EDWARDS. That has to come within—it would require legislation, yes.

Senator BARTLETT. Thank you very much.

Mr. Grinstein?

Mr. GRINSTEIN. Mr. Edwards, you said Pacific Far East Lines and American President Lines serve Guam. Do they have any obligations to serve Guam, or do they do it because they think it is good business?

Mr. EDWARDS. Well, really I am not in a position to say absolutely whether they are under an obligation or not. I don't know if steamships have something like a certificate of convenience that is required of bus lines or something like that. The airlines have; they get scheduled airlines and they have to have a certificate. I am not familiar enough with it to determine whether or not Maritime issues those certificates or not.

Mr. GRINSTEIN. Well, let me ask this: We will say Pacific Far East Lines serves Guam. Does it serve it with a subsidized vessel and repay back to the Treasury the amount they are subsidized?

Mr. EDWARDS. Again, I am not familiar enough. That is why I suggested that you might get all of these answers from Mr. Stewart, who is fully familiar. He is a maritime specialist here in Washington and would be familiar with that. I am not familiar enough with it to determine just what the situation is on those technical aspects.

Mr. GRINSTEIN. The main source of supply, then, for the civilians in Guam would be the U.S. mainland, including Hawaai, and the main source of supply would be the U.S. vessels?

Mr. EDWARDS. Oh, yes; it is the only source.

Mr. GRINSTEIN. Thank you.

Senator BARTLETT. Mr. Bourbon?

Mr. BOURBON. Did those two lines make application to Maritime to serve you by more frequent calls?

Mr. EDWARDS. I beg your pardon?

Mr. BOURBON. Did Pacific Far East and APL request permission from Maritime to make more frequent calls at Guam? It seems to me I read that recently.

Mr. EDWARDS. Well, I don't recall whether they made application or not. I can tell you that in 1955 there were 58 vessels of PFE, 58 in 1956, 55 in 1957, 38 in 1958, 36 in 1959, and 18 in the first 6 months of 1960.

Mr. BOURBON. Do you have adequate service from them now?

Mr. EDWARDS. Yes, I would say we have adequate service. Naturally all our passengers come in by air and all of our mail is by air. We have mail service by Pan American three times a week and we have two flights a week out of Guam to the mainland. But all of our produce comes in, all of our supplies, food products and consumer durables, automobiles and hard and soft goods, by ship and the average, as I say, is about once a week.

But here recently, the first 6 months of 1960, we had 18 vessels out of 26 weeks. And APL had only eight vessels. So really, the first 6 months we had 26 vessels and there were 26 weeks. Now sometimes they land within a day of each other.

Mr. BOURBON. Doesn't it seem strange, that if I recall properly, you said you brought \$24 million in imports from the United States and only about \$3 million from the Far East? They get a subsidy on anything that is shipped from the Far East, don't they, to Guam, because that is foreign trade? I would think you would be able to buy a whole lot of things a lot cheaper in the Far East than in the United States and yet you buy eight times as much from the United States.

Mr. EDWARDS. Well, the only imports we get from foreign countries is some food products and some soft durables and a few automobiles, but that is about the extent of it. These people mostly buy stateside products. Now I am not certain whether they are subsidized on their foreign merchandise that is brought in from Japan or Hong Kong or Manila; I am not familiar enough with that to say.

Mr. BOURBON. They must be, because they are bringing it into the United States.

Mr. EDWARDS. I would imagine it would be, too, subsidized foreign merchandise. I would imagine it would be, but I am not certain of it.

Mr. BOURBON. That is all.

Senator BARTLETT. Mr. Goding?

Mr. GODING. In an area you are probably very familiar with, you recall the Commission on the Application of Federal Laws to Guam that made a report following the enactment of the organic act and pursuant to the terms of that act?

Mr. EDWARDS. Yes, sir.

Mr. GODING. If I recall, that Commission recommended that Guam be removed from the protection of the coastwise laws.

Mr. EDWARDS. That is correct, sir.

Mr. GODING. Do you recall what happened subsequently? I can see that in view of the security problem that you might not get service, but there might be other reasons.

Mr. EDWARDS. Well, no; no action has ever been taken on it. We went through this application, this Commission's recommendations on the application of Federal laws to Guam and put in everything, but because of the defense sea area nothing was done on that.

Mr. GODING. My understanding is, and it may not be correct, if Guam were removed from the protection of the cabotage laws, the subsidized lines operating there could then serve the area without rebating the subsidy on that.

Mr. BOURBON. That would seem to be so.

Mr. GODING. I wondered if that possibility had been considered.

Mr. EDWARDS. Well, you could keep it a Navy defense sea area and keep out the foreign vessels and still make an exception to the coastwise laws and permit a subsidy.

Mr. GODING. In other words, Guam would then have the benefits of a subsidy?

Mr. EDWARDS. Yes, and still there would be no foreign vessels coming in.

Senator BARTLETT. Mr. Edwards, do you have an adequate harbor or harbors at Guam?

Mr. EDWARDS. A very good harbor. It is naval, but very good.

Senator BARTLETT. The commercial carriers use that harbor?

Mr. EDWARDS. Oh, yes. They come in and one side is set off for the Navy, and the Government of Guam operates the commercial port. These figures I am giving you are taken from our Department of Commerce, which the commercial port is one of its bureaus.

Senator BARTLETT. Thank you very much. We are grateful for your appearing here.

Mr. EDWARDS. It was a pleasure.

I wish, on behalf of the people of Guam, to express our appreciation for you giving us this opportunity to present this problem to you, because it is most timely in Guam right now.

Senator BARTLETT. It ties in with the problem we have under consideration, most assuredly.

The final witness today will be Mr. Fitch, of the Department of the Interior.

STATEMENT OF EDWIN M. FITCH, ASSISTANT TO THE GENERAL MANAGER, THE ALASKA RAILROAD, DEPARTMENT OF THE INTERIOR, WASHINGTON, D.C.

Mr. FITCH. Mr. Chairman, I will try and speak somewhat more to the point and more rapidly than our last Alaska Railroad trains used to run in the old days.

When I first got off the train at Seward in 1947, I recall being met by a resident who said, "Good old Alaska Railroad, on time to the day." We now are on time usually to the minute.

Senator BARTLETT. Now Mr. Fitch, I take that as a matter of gospel, but before others may be willing to do so, you had better identify yourself.

Mr. FITCH. My name is Edwin M. Fitch, Assistant to the General Manager of the Alaska Railroad. I have worked for the Railroad since 1947 and my headquarters are in Washington, D.C.

Senator BARTLETT. And the Federal Government owns the Alaska Railroad and it is operated under the jurisdiction of the Interior Department.

Mr. FITCH. That is correct, sir.

Senator BARTLETT. Thank you.

Mr. FITCH. May I give just a brief history of the Railroad. We have been operating in one form or another for more than half a century. The Railroad goes back to the private railroad constructed from Seward which eventually the Government took over. We run from the port of Seward to Fairbanks, 471 miles. We also operate out of the port of Whittier, which used to be a military port, but is now deactivated. We still run there because there are two or three large industries in Whittier which we must serve.

The financial characteristics of the Railroad can be described briefly. Our freight income is about \$12 million a year. Our total income is perhaps a couple of million dollars more. About half our revenue is from coal and oil. We try to keep our heads above water in terms of breaking even, as far as our costs are concerned, and those costs include \$1,900,000 a year depreciation. As of this time, this year, this fiscal year, we are \$130,000 ahead of the game. Since we were in the red last year at this time, we are \$630,000 better off, in terms of our net now, than we were last year in spite of an increase in our depreciation charges.

Senator BARTLETT. Do you care to start a steamship company then out of the profits?

Mr. FITCH. I am a railroad man and I don't know anything about steamship companies, except this, the Alaska Railroad is in partnership with the steamship companies. Their health is important to us, as ours is to them.

We are also in partnership with the trucklines. We would rather work with them than fight them, though sometimes they are a little more ready to compete strongly with us than we are with them. We have, I think, been very successful in winning the cooperation of the truckers. We have done it through piggyback and containerization, and I think the only excuse for your having me testify on behalf of the Railroad is to secure added emphasis on the subject of containerized freight.

The Alaska Railroad, Alaska Steamship Co., and some of the barge-lines have pioneered in containerized freight in the Alaska trade.

If you had looked at our Anchorage yard on a sunny day in January—if I had been in Anchorage in January, I would have escaped the rigors of the Washington winter—you would have seen flatcars loaded with containers and piggyback trailers all over the place. Every time I go down past the Potomac yard I look for piggyback and containers and rarely see them.

In my judgment, and if you will allow me a bit of bragging, the Alaska Railroad is the No. 1 container railroad in the whole United

States in terms of the percentage of its traffic which is shipped via containers. The reason it is so economical for us to do this is important, I think, to this committee in considering water transportation, because we have an advantage in terms of saving through containers that a railroad that does not cross a dock does not have.

Our goods must come largely via Seattle, or Portland, or San Francisco, over a dock. They are taken to Seward by ship or barge, again transferred over a dock and placed on Alaska Railroad trains to go into the interior to Anchorage and Fairbanks. It has been savings due to that kind of transportation which has been responsible for the fact that the Alaska Railroad is probably the only carrier in the world that is paying 1961 prices, and is charging just about what it charged in 1937 for transportation. That is not true in some particular commodities, but by and large we are making about the same per hundred pounds of freight as we made in 1937 for our line haul over the Alaska Railroad.

Senator BARTLETT. May I interrupt at that point?

You said you are making about the same amount. Are you also charging about the same amount?

Mr. FITCH. I beg your pardon, sir, I meant charge, not make. We are charging about the same amounts as we charged in 1937. One obvious example is our passenger rate which was 6 cents per mile in 1937 and is 6 cents per mile in 1961.

I am happy to report that our longshoremen—these longshoremen, by the way, are the employees of a contractor of the Alaska Railroad, not ours—they are cooperating with us in this endeavor. They are not resisting containerization. They realize that containerization means a great deal to the maintenance of the port of Seward as a successful port, and we are extremely pleased with the way the ILWU officers and members in Seward are cooperating to be certain that we have an efficient containerized operation at that point.

We also, of course, run piggyback, and we have done so for many years. The largest truckers, some of them, in Alaska, may have 80 to 90 percent of their cargo going over our railroad piggyback. I am told that there are one or two lines that have never sent a pound of freight over the highway, but have used us for the over-the-road transportation and have themselves then been the delivery carrier.

We on the Alaska Railroad regard piggyback as old fashioned, however, and expect containerization will increase, and piggyback will decline as far as we are concerned.

I would like to call the attention of the committee to the fact that the Alaska Railroad has a very profound and deep interest in through rates to Alaska. We would like to look forward to the day when a container could be loaded at the manufacturer's warehouse in Chicago, or Pittsburgh, or wherever the origin of the goods is, and that container could go via rail through the ports to Anchorage or Fairbanks, the only handling being the physical handling or placing the goods inside the container at the manufacturer's warehouse, and the taking of the goods out of that container when it arrives at the merchant's warehouse.

Senator BARTLETT. This is not now possible?

Mr. FITCH. No, sir.

Senator BARTLETT. Why?

Mr. FIRCH. In the first place, the Alaska Railroad is not in a position to allow its own containers to move very far out of Seattle. There are no arrangements for pooled containers in this country as yet to compare with the pooling of freight cars, which is done as you know under the guidance of the Association of American Railroad's Car Service Division.

There is developing, through the freight forwarders, what would amount to a pool of containers, and in the future perhaps this will develop as far as the railroads are concerned. But there are obstacles to it now. One, there are no physical arrangements for keeping track of these containers, and I would be the first to admit this is a difficult problem, if they should be shipped all over the United States and to some extent all over the world.

In the second place, we have no way of establishing a through rate, even if we did have pooled containers at this time. As you know, the situation there is due to the fact there is one kind of regulatory board, ICC, for the traffic to the port, and another, the Maritime Board for the water carrier, and another, the Secretary of the Interior, for the Alaska Railroad, or if it moves by truck, it goes back to ICC.

I should like to report to this committee that although some members may have been disappointed at the action by the President in vetoing a bill to place the Alaska Railroad under the ICC last year, that the General Manager has recommended to the Department of Interior that we be placed under the Interstate Commerce Commission for purposes of rate regulation only, and while that has not been adopted as official policy by the Department, the General Manager is recommending that be done.

I would like to close, sir, with one little statement about the future of railroading. We on the Alaska Railroad do not feel defeated about railroads. We operate under a good many handicaps, and also with some financial advantages, that is true, in terms of comparison with Class I railroads. We are a one-way railroad, a short-line railroad, a thin traffic railroad, but we have kept our heads above water. In terms of the meaning of the railroad to Alaska, can I call your attention to the fact that two-thirds of the population lives along the rail belt area.

I would also like to ask you to imagine what would have happened to Anchorage if the Alaska Railroad had gone through Valdez or Cordova. In my opinion the development of Alaska would have occurred some place else. I suspect Anchorage would have been little more than a village beside a salmon cannery, except as the railroad moved through there. True, with the coming of the highways more development is possible, but I doubt very strongly if the highways would have come in the rail belt area except as the Alaska Railroad had developed the area first.

I think there is a great future for railroads in terms of furnishing economical and good and fast transportation. I would like to wind up this brief statement by saying that it is very important to the railroad that we get along with our partners, the shipping companies, with our partners the truckers, and we hope that we can continue to work with them as cooperatively as has been possible in the past.

The general manager of the railroad, Mr. D. N. Smith, may wish to file a statement with the committee, and I would like permission to do so, if he wishes.

Senator BARTLETT. Granted.

Mr. Fitch, if these joint through rates could be established, is it your opinion that substantial savings might be made possible to the ultimate consumer?

Mr. FITCH. That is always theoretically so and I think in practice it often is so. This, of course, could happen with or without containers. The reason for it is that almost invariably the fixing of rates for the long through route means lower rates per ton-mile than for the short route. For example, the rate from Seattle to Seward, for delivery in the city of Seward, for the water haul, is normally somewhat higher than the proportional rate which applies if the through rate is applied going on through to Anchorage or Fairbanks, and in terms of rate history, that has been almost always the case. It takes men's decisions to make it so, but I think that this history means that there would be some likelihood of the same thing happening on through rates to interior Alaska.

Senator BARTLETT. You spoke about the innovations and improvements made in respect to use of containers, both at sea and ashore. Is it not the case, as was suggested this morning, that if this had not occurred, the rate increases for Alaska, and I must assume for the other offshore communities, would have been much larger than actually has been the case during the post-World War II period?

Mr. FITCH. I can speak only for the Alaska Railroad directly, of course, but if it had not been for containers, either we would be losing several hundred thousand dollars every year or our rates would be higher than they are now.

Senator BARTLETT. This then has been a highly significant development in the transportation industry.

Mr. FITCH. It has, sir, and I think it has lessons for the whole of the transportation industry, not just for the Alaska trade.

May I point out in that connection that the military now has in use 85,000 containers for oversea trade. Those are the so-called Conex boxes.

Senator BARTLETT. What kind?

Mr. FITCH. Conex boxes. A small container, as I recall, about 7 by 8 by 12 or 13; something like that.

Senator BARTLETT. There is no standard size for these containers?

Mr. FITCH. Yes; these are all the same.

Senator BARTLETT. Those, but others have different sizes?

Mr. FITCH. Yes; and that is one of the big obstacles to successful containerization throughout the country. There are several committees working on that. I happen to be alternate to the general manager as a member of two of them, one maintained by the American Standards Association and the National Defense Transportation Association. They have agreed to a modular standard, in units of 10 feet, 10, 20, and so forth, and I regret to say that since we were in the container business a long time before these standards were thought of, our containers are all 24 feet long.

Senator BARTLETT. You were first?

Mr. FITCH. We were in there first.

Senator BARTLETT. And biggest?

Mr. FITCH. With the steamship companies, and there has been a tendency for the steamship companies to use the 24 to 37 foot boxes.

Senator BARTLETT. Now you mentioned that the longshoremen in the Alaska ports are of particular interest to you as a member of the Alaska Railroad, and that they have accepted this change in circumstances. Was that acceptance readily given or did it come after tumult and toil and trouble?

Mr. FITCH. Remember I said that the contract—we have a longshore contractor who made the arrangements with the union. I was not in Alaska at the time, but I am informed the acceptance was readily given, and that the longshoremen not only caused no turmoil and trouble, but they have recognized that their future in Seward depends to a great extent upon the success of containerization.

Senator BARTLETT. I am going to suggest in this connection that it will be useful to have in the file, although not in the record, an article on this very subject which appeared in a recent issue of either Harper's or the Atlantic Monthly—Harper's, I believe—by William Glazier upon the subject of automation, and an agreement between industry on the Pacific coast and the longshoremen relating to this. It bears out your declaration, Mr. Fitch, that longshoremen have been willing to accede to that which at first blush would seem to mean a diminution of work opportunities for them.

Mr. BOURBON. Could I ask a question, Senator?

Senator BARTLETT. Yes; of course.

Mr. BOURBON. Do your longshoremen up there share in the \$5,500,000 fund the Pacific coast people have set up to compensate them for the less work?

Mr. FITCH. The contractor's longshoremen—they are not railroad employees—have their own agreement with the contractor, and I am quite sure this is a separate agreement, applicable to the port of Seward, and so that I am almost certain they do not share in that.

Mr. BOURBON. But there is a special bonus for acceptance of the containers?

Mr. FITCH. I would like to check that point. It is my understanding, though, that there is a wage rate only for our longshoremen. I am not aware of any special bonus for handling containers. But that is subject to check, sir, and I will check that.

Senator BARTLETT. I think you will probably discover that the situation is otherwise, and that these longshoremen at Seward, who make up a unit of the international union, are included within the agreement. I don't know this to be a fact, but I would think so because I think they would have this protection from their national director.

Mr. FITCH. I regret I am not more expert on that point.

Senator BARTLETT. If you are not, it is about the only thing relating to this you are not.

Mr. FITCH. Thank you, sir.

Senator BARTLETT. Mr. Grinstein?

Mr. GRINSTEIN. You mentioned a lot of traffic is coming in by barge. Is this increasing? Is more traffic coming into Alaskan ports by barge?

Mr. FITCH. Yes.

Mr. GRINSTEIN. And they are bringing containers in by barge?

Mr. FITCH. That is correct.

Mr. GRINSTEIN. Are these regulated by the Federal Maritime Board?

Mr. FITCH. I so understand, yes.

Senator BARTLETT. Mr. Goding.

Mr. GODING. To supplement that, do you have railroad figures over a period of years or could you supply them on the relative proportion of ship and barge container traffic?

Mr. FITCH. Over how long a period?

Mr. GODING. Over the last 4 or 5 years?

Mr. FITCH. Five years. All right. I am sure Alaska Steamship Co. will forgive me if I point out one of the problems here has been the provision of deck space for containers and the conventional ship doesn't have a great deal of deck space for containers. It is possible to modify it and provide more.

We have had problems of getting the type of deck space which will permit the maximum of containers in the trade. That has been one reason for the increase in barges in the Alaska trade, though not the only reason.

Senator BARTLETT. Thank you, Mr. Fitch, very much. We may be calling on you at a later date for further contributions in the way of information.

The committee will stand in recess until tomorrow morning at 10 o'clock.

(Whereupon the subcommittee recessed at 4:33 p.m., to reconvene at 10 a.m., March 7, 1961.)

(Supplemental information from Administrator Thos. E. Stakem, Jr., previously requested, follows:)

U.S. DEPARTMENT OF COMMERCE,
MARITIME ADMINISTRATION,
Washington, D.C. April 28, 1961.

HON. E. L. BARTLETT,
Chairman, Subcommittee on Merchant Marine and Fisheries, Committee on Interstate and Foreign Commerce, U.S. Senate, Washington, D.C.

DEAR SENATOR BARTLETT: During my testimony on March 6, 1961, at the hearing of your subcommittee inquiring into the problems of domestic offshore shipping, I was requested to furnish certain information for the record.

It occurs to me that it would be most convenient to you and your staff to have the inquiries directed to me identified by the page numbers of the transcript of the hearing.

Accordingly, there is attached a series of pages on which we have identified the requests by the transcript page numbers involved, followed by the responses thereto.

We will be happy to furnish any additional information available to us which you may desire.

Sincerely yours,

THOS. E. STAKEM, *Maritime Administrator.*

Item 1—Pages 36-38

Furnish a statement on the formula used for recoupment of operating-differential and construction-differential subsidies when a subsidized vessel makes a call to a domestic offshore area.

Cases involving questions of reduction of operating-differential subsidy where a subsidized vessel makes a domestic call to an offshore area fall into two categories, namely, (1) those areas which are subject to our coastwise laws, in which case abatement of subsidy is required, such as Hawaii, Puerto Rico, Guam, Midway, Wake, and Alaska; and (2) those areas which are not subject to our coastwise laws, in which case abatement of subsidy is not required,

such as the Virgin Islands and Samoan Islands. There is a separate category involving U.S. trusteeships such as the Marshall Islands, but these areas are not territories of the United States, are not subject to our coastwise laws (even though foreign-flag carriers are excluded from serving such areas), and abatement of subsidy is not required.

In all cases requiring operating-differential subsidy reduction, the formula for such reduction is spelled out in section 605(a), as follows:

"* * * if the subsidized vessel earns any gross revenue on the carriage of mail, passengers, or cargo by reason of such coastal or intercoastal trade the subsidy payment for the entire voyage shall be reduced by an amount which bears the same ratio to the subsidy otherwise payable as such gross revenue bears to the gross revenue derived from the entire voyage."

For example, where a subsidized vessel makes a voyage in the mixed foreign and domestic commerce of the United States earning a gross revenue of \$200,000 of which \$20,000 was earned from the cargo carried in the domestic trade, the amount of subsidy accrued for the entire voyage would be reduced by 10 percent.

Additionally, if the subsidized vessel regarding which operating subsidy must be reduced had also received construction-differential subsidy aid, section 506 requires the annual repayment to Maritime of "that proportion of [one-twentieth or] one twenty-fifth [depending upon the statutory life of the vessel] of the construction-differential subsidy paid [by the Government] for such vessel as the gross revenue derived from the entire voyages completed during the preceding year." For example, assume that a vessel on which a construction-differential subsidy of \$5 million was paid earned \$2 million gross revenue during the year, of which \$400,000 or 20 percent was earned from cargo carried in the domestic trade. Twenty percent of one twenty-fifth of \$5 million (20 percent of \$200,000) or \$40,000 would be required to be paid to the Maritime Administration.

Item 2—Pages 39-40

Furnish whatever is available as to how the subsidization program by Canada to its coastal and inland water carriers to provide services to outlying communities works out.

Bill 336, passed by the House of Commons of Canada on June 23, 1947, established the Canadian Maritime Commission. The Commission is responsible for administering, in accordance with regulations of the Governor in Council, any steamship subventions voted by Parliament and makes an annual report to the Minister of Transport of its affairs and operations.

In response to an inquiry to the Canadian Embassy in Washington, D.C., the Maritime Administration was furnished information on maritime subsidies by letter dated November 17, 1958, copy attached.

In the Commission's latest annual report, dated June 28, 1960, the following is the full information reported on "Subsidized Steamship Services":

"In accordance with the terms of the Canadian Maritime Commission Act, the Commission continued to administer subventions voted by Parliament.

"During the fiscal year 1959-60 subventions were paid for coastal and inland services only. Thirty services received assistance, 2 on the west coast, to on the Great Lakes, and 26 on the east coast; these included the river and Gulf of St. Lawrence and the Canadian National Railways, Newfoundland coastal services, comprising 9 different routes and 11 vessels. A strike of seamen on the west coast resulted in a 2-week stoppage on subsidized steamship services. One new service is included—the Trois-Pistoles and Les Escoumains service—in which the Federal and Provincial Governments share equally.

"A new vessel has been built for the Department of Transport to be operated on the Pelee Island and the mainland services. Tenders were called for the operation of this vessel, to be submitted by February 15, 1960. The previous contractor, the Pelee Shipping Co., Ltd., submitted the lowest tender and was consequently awarded the contract to operate the service.

"The Commission's inspectors examined all services and carried out surveys to ascertain the need for the continuance of existing services. The Commission is represented on the standing committee of explosives in connection with the dangerous goods shipping regulations in the Canada Shipping Act. It has also been represented on several interdepartmental committees investigating transportation problems, in various parts of the country.

Statistics of steamship subventions

	Paid 1959-60	Main estimates
Interprovincial services between—		
Quebec, Prince Edward Island, and Nova Scotia.....	\$174,000	\$174,000
Nova Scotia and Prince Edward Island.....	558,784	617,000
Nova Scotia and New Brunswick.....	33,000	33,000
New Brunswick and Quebec.....	67,500	62,500
Prince Edward Island and Newfoundland.....	72,000	72,000
Provincial services:		
British Columbia.....	277,736	294,500
New Brunswick.....	104,600	104,600
Newfoundland.....	3,707,654	3,317,000
Nova Scotia.....	196,900	196,900
Ontario.....	164,000	157,500
Quebec.....	1,225,200	1,059,200
Total steamship subventions.....	6,581,374	6,088,200

Passenger, freight, and mail traffic on subsidized coastal services

	1958	1959
Passengers.....	1,834,447	1,827,282
Cargo (tons).....	201,239	224,579
Mail (bags).....	252,731	285,217
Vehicles.....	555,752	578,645

"The sum of \$6,581,374 shown as paid in 1959-60 is the net sum after recovering the undermentioned amounts by way of recapture of subsidy:

Prince Edward Island and Nova Scotia service.....	\$58,216
Prescott, Ontario, and Ogdensburg, N.Y., service ¹	15,000
Vancouver and west coast of Vancouver Island service.....	7,334
Total recaptured.....	80,550

¹ Since the contract was negotiated in 1951, the total subsidies paid for the Prescott and Ogdensburg service have been fully refunded.

CANADIAN EMBASSY,

Washington, D.C., November 17, 1958.

IRWIN M. HEINE, Esq.,
Chief, Statistics and Special Studies Office,
Maritime Administration, Washington, D.C.

DEAR MR. HEINE: With reference to your telephone conversation a short while ago with Mr. Broadbridge of this Embassy on the matter of maritime subsidies as it concerns Canada, we now have received fairly complete information from the Canadian Maritime Commission in Ottawa.

Prior to the establishment of the Canadian Maritime Commission in 1947 steamship subsidies were administered by the Department of Trade and Commerce. The Canadian Maritime Commission Act 1947, section 8b, states that "the Commission shall administer, in accordance with regulations of the Governor in Council, any steamship subventions voted by Parliament." Administration of steamship subventions involves the duty of advising the Minister (of Transport) the amount of subsidy which should be placed in the estimates upon which Parliament votes.

At the present time there are 29 subsidized services operating on the east and west coasts of Canada. The attached list taken from the estimates of 1958-59 gives details; 27 of the services are purely domestic and 2 involve a call at a U.S. port.

Many of these services have been established for some considerable time; in most cases there is no choice but to continue them as communities have grown up which are dependent on the service afforded and have no other means of communication. For each subsidized service a careful check is made of current expenditures and the contractor is required to submit yearly financial state-

ments. One of the difficulties which faces the Commission in this administration is the steady increase in contractor's operating costs particularly in regard to fuel and labour. As far as it is possible to do so the Commission allows increases in costs to be offset by reasonable increases in freight rates, dependent upon the ability of the communities involved to pay higher rates. However, even though rates are increased as much as the traffic will bear there remain a number of cases where without subsidy contractors would suffer operating losses.

Before recommending any increase in subsidy the Commission makes a complete investigation into the facts and satisfies itself that the services are essential to the communities involved. A careful study is made of the applicant's financial statements and, where necessary, an independent audit is ordered.

Similar investigations are made in regard to applications for new subsidies. These are only recommended on the grounds of public convenience and necessity or in cases where the Commission is satisfied that the communications involved in the new service will promote trade and be of economic service to the community or the country at large.

In assessing the amount of subsidy that will be required a profit of not more than 10 percent of the capital employed is allowed. Where the reliability of the estimates of revenues and expenditures used for this purpose is in doubt, and it is possible that the actual earnings may be in excess of the 10 percent allowance for return on capital, a recapture clause is included in the subsidy contract whereby the Government recovers, in whole or in part, the subsidy which has contributed to such excess.

The following factors are taken into account before recommending the payment of a subsidy and assessing its amount.

1. ESSENTIALITY OF SERVICE

- (a) Examination of alternatives, if any.
- (b) Consequences of cessation of an existing service.
- (c) Adequacy of service to needs of area served—
 - (i) consideration of freight requirements;
 - (ii) consideration of passenger requirements.
- (d) Development or maintenance of area served.
- (e) Relation of proposed service to industry and to imports and exports of the community concerned.
- (f) Postal requirements.
- (g) Link with other transportation services.
- (h) Assistance to domestic or international trade.

2. FINANCIAL ASPECTS OF SUBSIDY REQUESTED

- (a) Analysis of award in relation to—
 - (i) type and frequency of service;
 - (ii) number of passengers to be carried;
 - (iii) type and amount of freight to be carried;
 - (iv) suitability of vessel employed or to be required—
 - (A) cost of acquisition;
 - (B) cost of operation.
- (b) Analysis of ancillary government costs; public works expenditures on terminals, post office expenditures on carriage of mails, etc.
- (c) Analysis of balance sheets and profit and loss statements.
- (d) Scrutiny of accounts in relation to costs, expenditures, capitalization, dividends, profits, and depreciation, to ensure that service will be operated on an efficient and economic basis.
- (e) Study of competitive services, if any, to prevent abuse of subsidies for competitive purposes.
- (f) Study of passenger and freight rates to ensure that the immediate area is bearing its fair share of the total and to prevent unfair effect on other rates in the area.
- (g) Consideration of corporate or personal status and financial ability of contractor to perform service.
- (h) Consideration of length of contract.

Yours sincerely,

A. B. RITCHIE,
Chargé d'Affaires, ad interim.

Canadian Maritime Commission—Steamship subventions for coastal services

	1958-59
Vancouver and northern British Columbia ports, service between-----	\$194,500
Vancouver and west coast of Vancouver Island, service between-----	100,000

EASTERN LOCAL SERVICES

Baddeck and Iona, Nova Scotia, service between-----	17,500
Campobello, New Brunswick, and Lubec, Maine, service between-----	8,600
Cross Point, Quebec, and Campbellton, New Brunswick, service between-----	50,000
Dalhousie, New Brunswick, and Miguasha, Quebec, service between-----	27,500
Grand Manan and the mainland, New Brunswick, service between-----	95,000
Halifax, Canso, Guysborough, and Isle Madame, Nova Scotia-----	30,000
Ile-aux-Coudres and Les Eboulements, Quebec, service between-----	15,000
Ile-aux-Grues and Montmagny, Quebec, summer service between-----	3,300
Ile-aux-Grues and Montmagny, Quebec, winter service between-----	1,700
Mulgrave and Canso, Nova Scotia, service between-----	54,900
Mulgrave, Queensport, and Isle Madame, Nova Scotia, service between-----	32,500
Murray Bay and north shore of St. Lawrence River, Quebec, winter service between-----	50,000
Owen Sound and ports on Manitoulin Island and Georgian Bay, Ontario, service between-----	100,000
Pelee Island and the mainland, Ontario, service between-----	42,500
Pictou, Mulgrave and Cheticamp, Nova Scotia, service between-----	17,000
Pictou, Nova Scotia, Charlottetown, Prince Edward Island, and the Magdalen Islands, service between-----	174,000
Prescott, Ontario, and Ogdensburg, N.Y., service between-----	15,000
Prince Edward Island and Newfoundland, service between-----	104,000
Prince Edward Island and Nova Scotia, service between-----	567,000
Quebec, Natashquan, and Harrington, Quebec, service between-----	607,000
Quebec or Montreal, Gaspé and Magdalen Islands, Quebec, service between-----	189,000
Rimouski, Matane, and points on the north shore of the St. Lawrence River, Quebec, service between-----	125,500
Rivière du Loup and St. Simon and/or Tadoussac, Quebec, service between-----	21,000
St. John, New Brunswick, Tiverton, Freeport, Westport, and Yarmouth, Nova Scotia, service between-----	33,000
Sorel and Ile St. Ignace, Quebec, service between-----	43,000
Sydney and Bay St. Lawrence, Nova Scotia, service between-----	45,000
Newfoundland coastal steamship services-----	2,800,000
Total-----	5,563,500

Item 3—Page 41

Furnish information as to what ships in the reserve fleets are suitable and in comparative readiness for use in the several domestic offshore trades if a Government charter program is deemed appropriate.

With respect to the Alaska, Guam, and Hawaiian trades, the following suitable ships are available from the west coast reserve fleets:

C-3-----	1
C1-M-AV1 (many fitted for Alaskan trade)-----	23
VC2-S-AP2 (Victory)-----	68
VC8-S-AP3 (Victory)-----	14

In addition to these ships it is estimated that one C-2 ship will be traded in under the trade-in and build program and become available on the west coast during the next 12 months.

With respect to the Puerto Rican trade, the following ships are available from the Atlantic and gulf coast fleets:

C-2	1
VC2-S-AP2	68
VC2-S-AP3	31
C1A	6
C1B	26

In addition to the above it is estimated that two C-2 ships will become available from the trade-in and build program on the Atlantic coast during the next 12 months.

Item 4—Page 44

Advise whether certificates of convenience and necessity would be limited to ships or whether they would also be applicable to barge operations.

We understand the test as to the applicability of certificates of necessity requirements under the Interstate Commerce Act is whether the carrier operates as a common carrier by water. If so, a certificate is required. If the operation is that of a contract carrier, a permit is required, except in a very limited area.

Consequently, it appears that certificates of necessity could be issued to barges, as well as ships, when operating as common carriers.

Item 5—Pages 46-47 (see pp. 30-32)

Furnish any available information as to the relation between ocean transportation costs and consumer costs in the offshore domestic areas.

As was indicated at the hearing, the Federal Maritime Board has undertaken no cost study, as such, of the relation between ocean transportation costs and other costs which are involved in establishing the ultimate consumer costs.

The subcommittee chairman apparently concurred in our recommendation that before any conclusion is reached as to the advisability of adopting any of the enumerated alternative methods of lowering freight rates, an effort should be made to settle definitely the relationship of the ocean carrier charges to other cost factors. We believe that only by an analysis of the result of a thorough study of the cost factors contributing to the ultimate consumer costs can it be determined whether the ocean transportation charge is such a significant factor in the ultimate consumer cost that a reduction of ocean freight rates would accomplish the desired result. As we envisage it, the suggested cost analysis would be made with respect to commodities exported from the mainland to Alaska, Hawaii, Guam, and Puerto Rico, and commodities imported therefrom which have a significant effect on the economy of these domestic, noncontiguous areas. The study would cover all factors that affect the ultimate costs of each selected commodity, including, but not limited to, price of items at mainland sources, packaging and crating, inland transportation and handling at each end, ocean transportation, insurance, loading and unloading aboard ship, losses, inland distribution, and wholesale and retail prices. Inasmuch as such a study is beyond the area of our responsibility and capability at present, we suggest that the subcommittee consider employment of one of the many independent research and management consultant firms who can furnish an objective report of the type desired. In order that the subcommittee have some idea of the expense it would incur in obtaining such a report, we have obtained from one firm an estimate of \$57,000, under a cost-plus-a-fixed-fee type of contract and a 6-month period for completion.

Item 6—Pages 48-59, 65

In the hearing before the Subcommittee on Merchant Marine and Fisheries, Committee on Commerce, on March 6, 1961, relative to the domestic offshore shipping problems, Hon. Ernest Gruening, U.S. Senator from the State of Alaska, asserted that the effects upon Alaska of the operations of the carriers and the administration of shipping affairs by the present Federal Maritime Board and its predecessors have not given indications that consideration of the public interest is of concern to either. In addition, Senator Gruening stated that neither the Federal Maritime Board, the Maritime Administration, nor their predecessors had ever offered any suggestions to solve the plight of domestic water transportation—particularly in the Alaska trade.

The Federal Maritime Board and the Maritime Administration feel that they and their predecessors have shown continuing concern for the public interest of the noncontiguous States and territories and that their concern in this respect, as well as their concern for the economic well-being of the carriers, is indicated by their annual reports to Congress since World War II. In fact, the volume of material included in the annual reports during those years relative to the domestic offshore trades makes it impractical to repeat for insertion in the record. However, an examination of such reports makes it apparent that the Board and Administration, and their predecessors have been acutely aware of the problems in the offshore domestic trade, particularly Alaska. Within our statutory authority, various efforts have been made to implement the requirements of services to such areas. Among other things, carrier service to the Alaska area has been aided for years by providing Government-owned vessels under bareboat charters. Favorable bareboat charter rates and off-hire arrangements have enabled the furnishing of services to Alaska which would not otherwise have been provided by commercial enterprises. Bareboat charters to all domestic operators provided for a base charter rate of 8½ percent of the statutory sales price, with additional charter hire of 6½ percent, if earned. Charters for foreign operations provided a single rate of 15 percent. Following World War II, the first choice for purchase of Government-owned vessels made available under the Merchant Ship Sales Act of 1946 was given to domestic operators in recognition of the fact that their ships were the first ones available for defense purposes and in recognition of the urgent need for reestablishing domestic waterborne services.

Senator Gruening also asserted, "That the unduly high cost of living [in Alaska] is a direct result of the high costs of waterborne transportation is unquestioned."

On the basis of the limited information developed in the hearings and our information as reported to your subcommittee for inclusion in the hearing record, there is considerable doubt as to that conclusion. This uncertainty is the prime reason for our recommendation to your subcommittee that a comprehensive survey be made to settle definitively the relationship of the various cost factors which go into the ultimate consumer costs.

As to Senator Gruening's allegation of a lack of concern for the "public interest," it is the view of the Board and the Administrator that the "public interest" of the offshore domestic areas is best served by adequate and continued waterborne transportation. Consequently, the Board has exerted its efforts to prevent unwarranted returns to carriers through increased rates but with the knowledge that refusal of increases which are shown to be necessary in order to provide a minimum fair return to the carriers on their investments would be contrary to the carriers' constitutional rights and would lead them to reduce substantially or completely terminate their services to such areas.

Item 7—Page 67

Has the Department of Defense ever made a determination as to how many ships are required in the domestic offshore trade?

The planning groups of all services submit their ocean lift requirements to JCS in terms of measurement tons. These data are collated by the joint staff and summarized in terms of overall military requirements. Ocean lift requirements are not refined to the point of specifically stating ship requirements for a particular service or operation.

Item 8—Page 69

Has the Board ever made a general investigation of domestic offshore shipping, both with respect to increasing rates and a projection of the burden it would impose on the economy generally?

The Board has not made a general investigation of this nature. However, a study was conducted by the Maritime Administration in April 1959, entitled "United States South Atlantic-Puerto Rican Shipping Services" which indicates the consideration given to the economy of that area. Copies of this report were sent to the House Merchant Marine and Fisheries Committee, House of Representatives, in April 1959. (The study referred to is contained in the committee file for reference.)

Item 9—Page 71

Furnish a comparison of the rates between mainland—domestic offshore areas and mainland—foreign ports of comparable distances.

Freight rates are stated in different fashions, some as cents per cubic foot or 100 pounds, others as dollars per ton of 2,240 or 2,000 pounds or of 40 cubic feet, etc. In order to present the desired comparison in a readily understandable manner, the attached table (item 9A) has been prepared to show the charges for moving defined lots of cargo from named ports to particular destinations. For example, the first column is the charge for moving a typical automobile (Ford, Chevrolet, Plymouth) measuring 540 cubic feet and weighing 3,600 pounds.

Column 2 portrays the rates for one roll of newsprint 3 feet in diameter and 5 feet long, weighing 1,500 pounds.

Column 3 is for 2,240 pounds of flour (wheat) in bags.

Column 4: 1,000 board feet of lumber weighing 3,200 pounds.

Column 5: Steel sheets, 2,000 pounds.

Column 6: Canned vegetables, 2,000 pounds measuring 50 cubic feet.

Column 7: Cotton piece goods, 2,000 pounds measuring 80 cubic feet.

Rates are quoted for hundreds of items in almost every tariff and no effort has been made to compare all of them. These seven items were selected at random and are considered a fair comparison.

Item 9-A

Nautical miles		1 automobile	1 roll newsprint	2,240 pounds of flour	Lumber	Steel sheets	Canned vegetables	Cotton piece goods
6,703	New York to Hawaii.....	\$391	\$27.21	\$38.00	\$63.86	\$29.96	\$38.89	\$82.22
6,786	New York to Capetown.....	371	18.08	32.00	37.50	19.20	61.56	113.50
5,871	New York to Buenos Aires.....	446	21.43	25.00	104.17	16.07	75.00	132.00
2,091	San Francisco to Hawaii.....	243	19.11	27.53	50.00	25.76	32.20	51.52
2,098	New York to Azores.....	419	25.45	25.50	53.57	25.00	40.18	117.00
2,047	New York to Costa Rica.....	246	23.63	20.16	45.72	25.00	40.00	90.40
2,588	San Francisco to El Salvador.....	405	17.41	25.76	55.00	25.00	57.00	160.00
4,536	San Francisco to Yokohama.....	618	29.25	25.48	48.75	20.22	83.44	111.00
1,232	Seattle to Alaska (Seward).....	298	28.05	35.84	45.72	41.58	35.86	40.80
1,372	New York to Haiti.....	351	22.50	21.28	35.00	21.50	50.00	86.00
1,474	New York to Jamaica.....	297	23.25	19.49	40.00	24.00	33.75	86.00
1,489	New York to Dominican Republic.....	281	28.50	24.19	42.50	21.80	44.50	69.60
1,399	New York to Puerto Rico (San Juan).....	205	11.70	19.04	32.77	18.60	25.00	43.20

¹ Palletized or in vans.

NOTE.—Freight calculated from tariffs on file with the Board and in effect Feb. 28, 1961.

Item 10—Page 72

Furnish a contrast between the subsidized operators and the nonsubsidized operators as to reserve funds and the tax treatment thereof.

Nonsubsidized American-flag carriers in the domestic offshore trade, as well as other nonsubsidized U.S.-flag operators engaged in the foreign or domestic commerce of the United States or in the fisheries, may establish pursuant to section 511 of the Merchant Marine Act, 1936, as amended, a construction reserve fund into which may be deposited the proceeds from the sale of vessels and indemnities from the loss of vessels. Section 511 allows the postponement of the tax on gains arising from such sale or loss (where the owner so elects) by providing for nonrecognition of the tax but requiring a corresponding reduction in the basis of a new vessel acquired with such proceeds, thus reducing depreciation deductions on the latter vessel, thereby increasing taxable income over the economic life of the new vessel. Such tax deferment is available only if the gains are expended for the acquisition of a new vessel within a period of 2 years or extensions granted up to an additional 3 years. Provision is also made for the deposit of earnings in the construction reserve fund but no tax deferment is available with respect to such deposited earnings.

A subsidized operator is required, pursuant to section 607 of the act, to create and maintain (1) a capital reserve fund, and (2) a special reserve fund.

The subsidized operator is required to deposit into the capital reserve fund—

(a) Annually an amount equal to the annual depreciation, if earned, on its subsidized ships; otherwise when earnings permit;

(b) The proceeds of insurance and indemnities received on account of total loss of any subsidized vessel;

(c) The proceeds from the sale or other disposition of a subsidized vessel;

(d) Such percentage of the annual net profits from subsidized operations as the Maritime Administration shall determine is necessary for the purchase, replacement, or reconstruction of vessels, if the cumulative net profits are over 10 percent per annum of capital necessarily employed;

(e) Interest on securities and cash balances in the capital reserve fund and the interest on securities in the special reserve fund;

(f) Such voluntary deposits as may be approved by Maritime; and

(g) Such transfers from the special reserve fund as may be approved by Maritime.

Into the special reserve fund, the subsidized operator is required to deposit—

(a) Annually the entire amount of profits (without regard to capital gains and losses) earned in the subsidized operations in excess of 10 percent per annum of CNE;

(b) Interest on the fund's cash balances; and

(c) Voluntary deposits as approved by Maritime.

Section 607(h) of the act provides that "earnings of any contractor receiving an operating-differential subsidy under authority of this act, which are deposited in the contractor's reserve funds * * * shall be exempt from all Federal taxes." The Treasury Department and the subsidized operators have entered into closing agreements concerning the meaning of the above as applied to deposits of earnings (including capital gain).

The closing agreements provide that the deposited earnings and capital gains shall be tax deferred, i.e., such earnings and gains are not recognized as taxable income but the depreciation basis of any vessel acquired with such deposits shall be reduced by the amount of such deposits used in the acquisition of said vessel. The closing agreements further provide that the difference between depreciation computed on this reduced basis and the depreciation required to be deposited in the capital reserve fund by section 607(h) of the act, which is computed on the basis of the full cost of the vessel to the operator, shall be treated as tax deferred funds.

In the event amounts are withdrawn from the capital or special reserve funds and paid into the contractor's general funds or distributed as dividends or bonuses, the earnings are taxable as if earned during the year of such withdrawal.

Item 11—Pages 73, 74

Furnish information as to changes in trade pattern of offshore domestic areas as between the U.S. mainland and foreign sources.

Foreign and noncontiguous inbound trade at Alaska, Hawaii, and Puerto Rico in dry-cargo ships, calendar years 1955 and 1959

[In thousands of long tons]

	1955	1959		1955	1959
Imports from foreign sources: ¹			Receipts from U.S. mainland: ²		
Alaska.....	2.1	16.3	Alaska.....	353.6	281.3
Hawaii.....	98.9	123.2	Hawaii.....	1,408.7	1,572.6
Puerto Rico.....	216.0	520.8	Puerto Rico.....	1,394.0	1,307.7

¹ Source: Bureau of Census (all dry-cargo ships).

² Source: Corps of Engineers (self-propelled dry-cargo ships 1,000 gross tons and over).

Item 12—Page 76

Did Mr. Morse, former Chairman, Federal Maritime Board, indicate about a year ago that he had changed his opinion so that he then thought certification of carriers in the domestic offshore trades and some changes in the form of economic regulation might be desirable?

A review of testimony by the former Chairman before congressional committees for 1959 and 1960 fails to confirm that he expressed such an opinion and we are unaware of any other indication by Mr. Morse to this effect.

Item 13—Page 76

Furnish specific data in the form of a tabular presentation of the tonnage and number of dry-cargo common-carrier vessels involved in the noncontiguous services as compared to the domestic operations.

The following tabulation is of ships of 1,000 gross tons and over which were operating as common carriers in the coastwise, intercoastal, and noncontiguous trades on December 31, 1960. A limited number of ships, engaging in domestic trade incidental to their principal foreign trade services, have been excluded. If further information concerning these exclusions and the companies involved is desired it can be provided.

[Tonnage in thousands]

	Number of ships	Gross tons	Deadweight tons
Total, all trades.....	86	691	923
Coastwise trade.....	37	283	394
Atlantic and Gulf.....	10	77	86
Pacific.....			
Intercoastal trade.....	27	206	308
Noncontiguous trade.....	49	408	529
Alaska.....	7	40	61
Hawaii.....	24	226	292
Puerto Rico.....	18	142	176

Vessels normally included in domestic trade but excluded from above because of being inactivated or chartered out for foreign service on Dec. 31, 1960

	Inactive			Chartered for foreign service		
	Number of ships	Gross	Deadweight tons	Number of ships	Gross	Deadweight tons
Atlantic-Gulf.....	1	8	11			
Intercoastal.....	4	29	44	4	30	47
Noncontiguous:						
Alaska.....	3	18	27	1	8	11
Hawaii.....	1	8	12			
Puerto Rico.....	2	14	22	11	75	109
Total.....	11	77	116	16	113	167

Item 14—Pages 70, 77, 78

What is the Federal Maritime Board permitting as a fair return to the carriers involved in the domestic offshore trades?

Supply Federal Maritime Board's order, report, and brief in docket No. 807, Atlantic & Gulf-Puerto Rico, General Increase in Rates and Charges, together with the decision of the U.S. Court of Appeals for the District of Columbia, No. 15846, decided February 23, 1961, which vacated the Board's order and remanded the case for reconsideration and clarification of the rate base question.

In docket No. 807, the Board stated that the maximum permissible rate of return in the Puerto Rico trade is 7½ per centum of a rate base consisting of the value of owned property devoted to the trade¹ plus working capital. The Board's decision in docket No. 807 is attached hereto, together with the decision of the U.S. Court of Appeals for the District of Columbia, remanding the case to the Board for reconsideration of specific issues.²

¹ In computing the rate base, vessels are valued at market value and other assets devoted to the trade are valued at net book value.

² The issues as stated by the Court are:

"* * * the case [is] remanded for the Board to consider and clarify the rate base question. The Board should also pass upon the Commonwealth's argument that it is not fair to ratepayers to let an accumulated depreciation reserve be depleted and depreciation charges thereby increased."

Attached are the requested order, report, brief and court decision. This matter is currently under consideration as to the appropriate further action by the Board.

Item 14—Order and report

ORDER

At a Session of the Federal Maritime Board, held at its office in Washington, D.C., on the 28th day of April A.D. 1960

No. 807

ATLANTIC & GULF-PUERTO RICO GENERAL INCREASE IN RATES AND CHARGES

This proceeding having been instituted by the Board on its own motion, and having been duly heard and submitted by the parties, and full investigation of the matters and things involved having been had, and the Board, on the date hereof, having made and entered of record a report stating its conclusions and decision thereon, which report is hereby referred to and made a part hereof, and having found that the proposed rates and charges herein under investigation are just and reasonable:

It is ordered, That this proceeding be, and it is hereby, discontinued.

By the Board.

JAMES L. PIMPER, *Secretary.*

FEDERAL MARITIME BOARD

No. 807

ATLANTIC & GULF-PUERTO RICO GENERAL INCREASE IN RATES AND CHARGES

Rates between North Atlantic and gulf ports of the United States and Puerto Rico, as increased 15 percent or 6 cents per cubic foot or 12 cents per 100 pounds, whichever produces the greater increase in revenue, and as further increased 12 percent, found just and reasonable

Odell Kominers, Mark P. Schiefer, and Sterling F. Stoudemire, Jr., for respondents.

Eduardo Garcia, Walton Hamilton, William D. Rogers, Abe Fortas, Seymour Berdon, and William L. McGovern for Commonwealth of Puerto Rico, intervener.

John Regan for Administrator of General Services, intervener.

Mitchell J. Cooper, Frank M. Cushman, Vernon C. Stoneman, and John B. Street for Asociacion de Industriales de Puerto Rico (Manufacturers Association of Puerto Rico) and Commonwealth Manufacturers Association, interveners.

John B. Street, Frank M. Cushman, and Vernon C. Stoneman for Paula Shoe Co., intervener.

John B. Street and Vernon C. Stoneman for Caribe Shoe Corp., intervener.

Mitchell J. Cooper and Frank M. Cushman for Coastal Footwear Corp., intervener.

L. Merrill Simpson for Bata Shoe Co., Inc., intervener.

William M. Requa for Association of Sugar Producers of Puerto Rico, intervener.

J. W. Harnach for Cooperative Grange League Federation, Inc., intervener.

Harold L. Copp for Atlantic Industries, Inc., intervener.

T. A. Smith for Louisiana State Rice Milling Co., Inc., intervener.

Wm. M. Reid for the Rice Millers' Association, intervener.

Alan F. Wohlstetter for Trailer Marine Transportation, Inc., intervener.

Alfred K. Kestehbaum for Cigar Manufacturers Association of America, Inc., intervener.

Robert E. Mitchell and Edward Aptaker as public counsel.

REPORT OF THE BOARD

(Clarence G. Morse, Chairman; and Thos. E. Stakem, Vice Chairman)

Submitted December 3, 1959. Decided April 28, 1960.

On December 4, 1956, the U.S. Atlantic & Gulf-Puerto Rico Conference (the Conference), then comprised of Bull Insular Line, Inc., Lykes Bros. Steamship Co., Inc., Waterman Steamship Corp., and Alcoa Steamship Co., Inc. (Bull, Lykes, Waterman, and Alcoa), filed with the Board Tariffs FMB F-No. 14, Homeward Freight Tariff No. 7, and FMB F-No. 13, Outward Freight Tariff No. 7, naming increases in commodity rates over the applicable rates then in effect, to become effective January 5, 1957, between U.S. Atlantic and Gulf of Mexico ports and ports in Puerto Rico.

On December 20, 1956, J. W. de Bruycker, agent for the conference, filed special permission application to modify on short notice the increases in rates to reflect an adjustment not in excess of 15 percent or 6 cents per cubic foot or 12 cents per 100 pounds, whichever produces the greater increase in revenue, over the applicable rates then in effect. This increase will be referred to as the 15-percent increase.

On January 4, 1957, pursuant to section 18 of the Shipping Act, 1916, as amended, 46 U.S.C. 817 (the 1916 act), and the Intercoastal Shipping Act, 1933, as amended, U.S.C. 843 et seq. (the 1933 act), we ordered an investigation into the reasonableness and lawfulness of the rates, charges, regulations, and practices stated in the tariff schedules filed December 4, 1956, and ordered the operation of these schedules suspended until midnight January 8, 1957, unless otherwise ordered.

On January 8, 1957, we amended our order of January 4, 1957, and granted the special permission to publish the rate increases, as modified, to be effective not earlier than January 9, 1957, on 1 day's notice. We also ordered an investigation of the 15-percent increase, and directed (a) that the carriers shall keep an account of all freight moneys received by reason of said rate increases for the period commencing January 9, 1957, and terminating May 5, 1957; and (b) that the carriers, upon final determination by the Board, shall pay to shippers, out of their general funds, the sums if any to which the respective persons who pay the freight may be entitled. The 15-percent increase became effective on January 10, 1957.

The orders of January 4 and January 8, 1957, made the conference, Agent de Bruycker, Bull, Lykes, Waterman, and Alcoa respondents in this proceeding. Notice of investigation and hearing appeared in the Federal Register of January 17, 1957, 22 F.R. 355, and hearing was held in New York, N.Y., April 16 through May 3, 1957. After hearing on the 15-percent increase, but before briefs of the parties were due, the respondents published on July 18, 1957, a 12-percent additional general rate increase (the 12-percent increase), to become effective September 14, 1957. On August 14, 1957, Pan-Atlantic Steamship Corp. (Pan-Atlantic), an affiliate of Waterman, filed revisions to its Homeward Tariff No. 1, FMB, F-No. 1, to become effective September 18, 1957, naming local commodity rates from Puerto Rico to U.S. Atlantic ports based on the same pattern as the conference rates.

By supplemental order of September 5, 1957, we (a) expanded the proceeding to include an investigation into the lawfulness of the rates as further increased by 12 percent; (b) suspended the operation of the Conference and Pan-Atlantic schedules naming the 12 percent increase until January 14, 1958; (c) made Pan-Atlantic a respondent; and (d) ordered a further hearing in the proceeding. Notice of the expanded investigation and further hearing appeared in the Federal Register of September 12, 1957, 22 F.R. 7291, and further hearing was held at New York October 21 through 28, 1957, and concluded in Washington, D.C., November 1, 1957. The 12 percent increase became effective on January 15, 1958.

During the course of the hearings the examiner denied requests by the interveners that the respondents be required to produce or make available underlying books, records, and accounts for the purpose of cross-examination in order to test the accuracy of certain of respondents' exhibits in the form of financial

and statistical summaries based upon allocations and computations derived from underlying documents. In an initial decision served February 3, 1958, the examiner considered those exhibits as reliable, probative, and substantial, based on the sworn testimony of the witnesses through whom they were introduced as to their correctness and accuracy.

After oral argument upon exceptions to the initial decision of the examiner, in an order entered June 13, 1958, we overruled the examiner as to these issues, and stated:

"We do not agree with the examiner that the summary evidence presented by respondents, without reasonable access to supporting and underlying books, records, and accounts by which the accuracy and sufficiency of the evidence may be tested, is 'reliable, probative, and substantial evidence' as required by section 7(c) of the Administrative Procedure Act. The record is insufficient for the Board to make proper findings as to the lawfulness of the rates under section 18 of the 1916 act and under the 1933 act.

* * * * *

"We conclude that this proceeding should be remanded to the examiner for further hearing, and, in order that the full record herein shall contain probative and substantial evidence sufficient for the Board to make valid determinations as to the lawfulness of the rates under investigation, respondents should produce at such further hearings, or make available to interveners and public counsel, such original and underlying books, records, accounts, and worksheets, including corporate profit and loss statements and balance sheets, as are required to determine the probative value of the evidence, the accuracy of computations and allocations between regulated and nonregulated activities, and the scope and accuracy of intercorporate transactions. Further, there should be full disclosure of data with respect to any sales or transfers of corporate assets which would be relevant and material in determining accurately the fair value of properties and assets devoted to this Puerto Rican service."¹

The proceeding was remanded to the examiner for the purpose of receiving further evidence.

Further hearings were held before an examiner during the period October 6-28, 1958. Intervenors who appeared during the course of the proceeding in opposition to the rate increases, or as their interests may appear, were the Commonwealth of Puerto Rico (the Commonwealth), the Administrator of General Services, Asociacion de Industriales de Puerto Rico (Manufacturers Association of Puerto Rico), Commonwealth Manufacturers Association, Paula Shoe Co., Caribe Shoe Corp., Coastal Footwear Corp., Bata Shoe Co., Inc., Association of Sugar Producers of Puerto Rico, Cooperative Grange League Federation, Inc., Atlanta Industries, Inc., Louisiana State Rice Milling Co., Inc., the Rice Millers' Association, Trailer Marine Transportation, Inc., and Cigar Manufacturing Association of America, Inc.

In his initial decision the examiner found and concluded that the 15 percent and 12 percent increases under investigation were just and reasonable and that the proceeding should be discontinued.

Exceptions to the initial decision and replies thereto were filed, and oral argument was heard. Exceptions and proposed findings not discussed in this report nor reflected in our findings have been considered and found not justified by the facts or not related to material issues in this proceeding.

The carrier respondents

1. Alcoa: Alcoa offers weekly service from the North Atlantic ports of New York and Baltimore, Md., and weekly service from the gulf ports of Mobile, Ala., and New Orleans, La., to ports in Puerto Rico. Each of the sailings serves all ports in Puerto Rico. The vessels in the North Atlantic service, after discharge at Puerto Rico ports, proceed into other trades, generally contract services. In the gulf service, the vessels return from Puerto Rico to the gulf ports in the northbound trade, a service inaugurated in March 1958.

2. During 1956, 1957, and the first 6 months of 1958, average vessel utilization on a cubic basis by Alcoa in the Puerto Rican service ranged from 39.5 percent in the second quarter of 1956 to 84.3 percent in the fourth quarter of 1957 in the North Atlantic service, and from 44.4 percent in the second quarter of 1956 to 66.6 percent in the second quarter of 1957 in the gulf service. Alcoa's average southbound voyage in 1957 from the North Atlantic consumed 14.5 days, and from the gulf 12.7 days.

¹ U.S. Atlantic and Gulf/Puerto Rico Rate Increase, 5 FMB 426, 429, and 430-1.

3. Bull: Bull provides three sailings per week from North Atlantic ports to Puerto Rico. One sailing proceeds from Baltimore and Philadelphia, Pa., to Puerto Rico and return. Another sailing proceeds from New York to Puerto Rico and return (the Thursday sailing), and the third from New York to Puerto Rico, thence to the Dominican Republic and return (the Friday sailing). Basically the services are provided with six C-2 type vessels, operated on a strict 2-week turnaround. In addition, Liberty-type vessels are also employed to lift stators, generators, ammunition, and other specialized cargo destined to Puerto Rico which cannot be handled on the regular C-2 vessels. Liberty ships were also utilized in some instances to carry full cargoes of bagged raw sugar under the tariff, but this movement declined rapidly in 1957 due to conversion of the raw sugar movement to bulk movement under contract, and has since come to a virtual halt. Caribbean Dispatch, Inc., an affiliate of Bull, is a major contract carrier of bulk sugar.

4. In a transaction closed December 18, 1956, characterized in the brief for the Conference as "an irrefragably [sic] arm's-length transaction between completely unrelated interests," Olympia Corp., Inc., in Delaware, acquired substantially all of the stock of A. H. Bull Steamship Co., a New Jersey corporation (A. H. Bull, New Jersey). Prior to the transaction, the purchaser and the sellers had no stockholders, directors, or other interests in common, or any similar relationship. Olympia had been organized by its parent, American Coal Shipping, Inc. (ACS), which paid \$100,000 for all of Olympia's outstanding stock, as the instrument designed to facilitate the consummation of the transaction. ACS and its own stockholders also loaned to Olympia about \$5 million, at interest of 5 percent. Between December 18, 1956, and January 21, 1957, Olympia's name was changed to A. H. Bull Steamship Co. (A. H. Bull, Delaware). The transaction contemplated purchase by Olympia of all of the outstanding stock of A. H. Bull, New Jersey, for a total consideration of \$40 million (which was not finally accomplished until February 28, 1957), the liquidation of A. H. Bull, New Jersey, and the transfer of all of its assets to A. H. Bull, Delaware.

5. On December 18, 1956, A. H. Bull, New Jersey, had over \$18 million in cash, obtained from surplus, liquidation of quick assets representing in part depreciation funds, release of vessel replacement funds, and receipt of repayments of advances and dividends from subsidiary companies, among others. On the closing date of the stock purchase, this \$18 million was declared by A. H. Bull, New Jersey, as a dividend, paid principally to Olympia, and the remainder of the purchase price of \$40 million was met from the proceeds of the loans from ACS and its stockholders of \$5 million mentioned above, and bank loans of some \$17 million at interest rates ranging from 4 $\frac{1}{4}$ to 5 percent, guaranteed by ACS.

6. The net purchase price paid by Olympia for A. H. Bull, New Jersey, was therefore about \$22 million. The book net worth of A. H. Bull, New Jersey, at the time of closing was about \$12,330,000. Incident to the purchase, the physical assets of A. H. Bull, New Jersey, and its subsidiaries had been independently appraised. About January 21, 1957, in partial but almost complete liquidation of A. H. Bull, New Jersey, its assets were transferred to the books of A. H. Bull, Delaware, and in the process the vessel book values were raised from \$5,160,421.85 to \$12,892,610.21, effective as of the closing date, the latter figure representing about 70 percent of the appraised values of the vessels. The ascribed values of certain other assets were changed also for consolidated statement purposes, but on the corporate books only the vessel values were changed. Thus on the books of A. H. Bull, Delaware, the vessel book values are carried presently at amounts, less accrued depreciation since the closing date, representing a pro rata share of the total purchase price paid by A. H. Bull, Delaware, for the assets of A. H. Bull, New Jersey.

7. Corporate entities affiliated with respondent Bull, so far as is here pertinent, include A. H. Bull, Delaware, of which respondent Bull is a subsidiary; A. H. Bull & Co., which provides continental U.S. overhead services for Bull and others in the corporate family in return for management and operating commissions composed principally of a percentage of revenues and a per diem husbanding charge; several separate corporations which own and operate pier facilities in Puerto Rico; Caribbean Dispatch, Inc., mentioned above; and Dafton Realty Co., owner of office facilities in New York utilized by Bull.

8. For 65 days between August 19 and October 22, 1957, Bull's operations were immobilized by a strike arising out of a jurisdictional dispute between seafaring unions. The strike was not unrelated to the fact that ACS, the new owner of the

Bull properties, was in part owned by the United Mine Workers. Other strikes which have affected the operations of Bull at various ports, for varying reasons, and for periods of time ranging from 2 to 44 days, totaled 33 days in 1951, 1952, and 1956; 12 days in 1953; 101 days in 1954; 78 days in 1955; 14 days in February 1957; and 20 days in the first 6 months of 1958.

9. Lykes: Lykes operates its weekly service between the gulf ports of Lake Charles, La., and Houston and Galveston, Tex., and occasionally other western gulf ports, and Puerto Rico, as a part of its subsidized service on trade route 19 (line A service) between gulf ports of the United States and Cuba, Haiti, the Dominican Republic, Venezuela, Colombia, and Panama. No voyages are operated to or from Puerto Rico exclusively. The number of vessel days operated by Lykes in the Puerto Rican portion of its line A service is less than that in the service to and from foreign ports. During 1956, 1957, and the first 6 months of 1958, average vessel utilization on a cubic basis achieved by Lykes in its combination Puerto Rican service ranged from 66.6 percent in the fourth quarter of 1957 to 90.9 percent in the first quarter of 1957.

10. Waterman: At the outset of this proceeding Waterman operated a weekly service between New Orleans and Mobile and Puerto Rico, utilizing two vessels on a 14-day turnaround, with additional vessels for relief purposes and when extra cargo demanded. Beginning in October 1957 Waterman also inaugurated weekly sailings, utilizing two vessels on a 14-day turnaround in regular breakbulk service, between New York, Baltimore, and Puerto Rico. Waterman intended to provide a permanent North Atlantic-Puerto Rico service, at first with regular breakbulk vessels, and later converting to trailership service. Waterman is a subsidiary of McLean Industries, Inc.

11. Effective February 4, 1958, Waterman withdrew from the conference, and simultaneously ceased all operations in the Puerto Rican trades, which were taken over without break in service by Waterman Steamship Corp. of Puerto Rico (Waterman P.R.). The latter is a wholly owned subsidiary of Waterman, is not a respondent, and is not a member of the conference, although its rates are in all respects the same as those of the conference. When filing its initial tariffs with the Board, and in subsequent pleadings herein, Waterman P.R. has agreed to be bound by the results of this proceeding so far as its rates are concerned. Statistical and financial data reflecting the combined Waterman and Waterman P.R. operations are of record, although no recent data were presented forecasting operating results for the entire year 1958 as was the case with the other conference respondents.

12. On February 28, 1958, Waterman P.R. inaugurated its North Atlantic-Puerto Rico trailership service, with the sailing of the *Bienville*. This vessel, upon arrival in Puerto Rico, was prevented from discharging its cargo because of labor difficulties. After some delay the *Bienville* proceeded to New Orleans, where her cargo was discharged and that which had not spoiled was transferred to a ship regularly employed in the Waterman P.R. gulf-Puerto Rico breakbulk service. The *Bienville* voyage consumed in all 34 days. After this experience, Waterman P.R. discontinued its North Atlantic-Puerto Rico service, which has not since been resumed either on a breakbulk or trailership basis.

13. Pan-Atlantic: Pan-Atlantic is an affiliate of Waterman, and as such was required to maintain the same rates as the conference by the terms of the conference agreement to which Waterman was a party. Between April 1957 and early 1958 Pan-Atlantic provided a northbound service from Puerto Rico to Miami and Jacksonville, Fla., in conjunction with its intercoastal and west coast-Puerto Rico services, which was suspended at the end of this period and has not been resumed. The tariff under which such service was operated was canceled effective August 22, 1958. So far as the record discloses, this service was minimal, since the cargo carried averaged only 51 tons per voyage, with gross revenue per voyage of \$1,506. These data are so insignificant as to warrant their exclusion from consideration herein, although the rates under investigation will remain subject to the findings.

14. Pan-Atlantic instituted a trailership service between New York and Puerto Rico on July 30, 1958, which is presently being operated. On October 27, 1958, we denied a petition by the conference requesting that this investigation be broadened by naming Waterman P.R. as a respondent, and bringing in issue the current tariffs of Pan-Atlantic and Waterman P.R.

The Puerto Rican economy and the trade

15. Puerto Rico is a small island, 100 miles long and 25 miles wide, separated from the nearest point in the United States by over 1,000 miles of open water. The economy of the island has never been self-sustaining, and it has few natural

resources. It is one of the most densely populated areas of the world. Puerto Rico's external trade is almost entirely with the United States. About 40 percent of all goods produced, and about 54 percent of all goods consumed, by the people of Puerto Rico are destined to, or originate in, the United States. Average income per capita in Puerto Rico in 1954 was \$446, as compared with \$1,770 in the United States. The percentage of the labor force of Puerto Rico unemployed or only partially employed has consistently exceeded that in the United States. These data indicate that increases in the cost of shipping such as are here involved affect the economy of Puerto Rico and the living standards of its populace more sharply than would similar increases elsewhere in the Nation.

16. The conference rates in the Puerto Rican trade are determined by three-fourths majority vote of the members. Therefore no one carrier can dominate the making of rates. Waterman P.R., presently operating in the gulf-Puerto Rico trade, is not a member of the conference, and its rates can be made by individual action, subject only to the competitive impact of the rates maintained by the conference. As is indicated by the revenue statistics shown in table I below, Bull is the dominant carrier in the trade, receiving approximately 50 percent revenues even in the year 1957 when Bull's operation were immobilized for more than 65 days.

TABLE I.—*Gross transportation revenues of the respondents*

Carrier	1956	1957	1st half 1958
Bull.....	\$24,993,850	\$21,646,383	\$11,682,207
Waterman.....	6,534,389	9,416,267	4,651,468
Alcoa.....	6,244,864	9,175,949	4,215,049
Lykes.....	3,843,368	3,774,843	1,940,279
Total.....	41,616,471	44,013,342	22,489,003

17. The most recent traffic and revenue projections of the respondents, where given, were based on an extension of their most recent experience, that for the first half of 1958, subject to the adjustments for known or contracted cost increases. Although there is testimony of record to the effect that a gradual increase may be expected in the movement of general cargo between Puerto Rico and the mainland, the statistics of record disclose a decline in tonnage carried of cargo subject to the tariffs here involved. This decline is attributed in large part to the conversion of the raw sugar movement from bagged movement under the tariffs to bulk movement under contract, and to the construction of a fertilizer plant in Puerto Rico, which virtually eliminated the movement of prepared fertilizer and substituted therefor the movement of fertilizer raw materials in tramp vessels. Table II below shows the tonnage data submitted for the years 1955-57 and the first half of 1958, and the projections for the full year 1958 where given. Weight tons are computed on the basis of the weight of the cargo carried, and freight payable tons on the basis on which the freight charges were paid, either weight or measurement. The data for the full year 1957 in tables I and II reflect the impact of the long strike in that year against Bull, and the consequent diversion of substantial amounts of traffic normally carried by it to Alcoa and other carriers. They show the dominant position of Bull in the trade.

TABLE II.—*Tonnage carried in freight payable tons, except where indicated*

Carrier	1955	1956	1957	1st half		1958 projected
				1957	1958	
Bull.....	1,876,964	1,828,275	1,151,993	710,877	558,880	1,117,760
Alcoa.....	429,470	312,701	418,509	186,422	169,363	340,000
Waterman.....	239,535	238,895	298,831	148,526	132,202	-----
Lykes.....	-----	-----	203,438	-----	107,822	215,644
Do.....	¹ 245,334	¹ 262,389	¹ 186,220	¹ 102,522	¹ 102,918	¹ 205,836

¹ Weight tons.

18. Taking into consideration the factors mentioned in paragraph 17 above, and the entry into the trade of Pan-Atlantic with its new and attractive trailer-ship service, which will no doubt succeed in diverting some traffic from the services maintained by the other respondents, it is found that the projections of the respondents as to the year 1958 are reasonable.

Specific commodity rates

19. In the first initial decision issued herein, the examiner found as follows:

"60. The shipper interveners, generally, are those who ship commodities under so-called promotional rates. These rates have been maintained by the carriers, prior to the proposed increases, at comparatively low levels designed to promote the movement of the commodities so rated. The promotional rates apply primarily to northbound traffic, and most of them have been used since 1946 in cooperation with and at the request of the newly developing industries in Puerto Rico. This traffic, in gross tons, in 1955, amounted to approximately 20,000 tons northbound and 1,000 tons southbound. In 1956 it amounted to approximately 25,000 tons northbound and 2,000 tons southbound. The revenue from this traffic in relation to total revenue was perhaps less than one-half of 1 percent.

"61. Selected commodities from those transported at promotional rates, stated by the carriers to be typical, were northbound: Shoes, paperboard, chinaware, coffee, cigars, rugs, artificial flowers, boxes, knocked down, scrap metal, scrap tobacco and confectionary; and southbound: Tin cans, iron and steel articles, glass jars, bottles, not otherwise specified, paper and paper products, and tiles. Two shippers, understood to be representative of shippers of such commodities, testified at the first hearing. One was a shipper of candy and the other of shoes, both shipping from Puerto Rico to the U.S. mainland. Their main objections were that the first rate increases on the commodities were greater than 15 percent. This is so because of the 6 cents per cubic foot or 12 cents per 100 pounds aspect of the first increase.

"62. The shippers gave important consideration to the relatively low shipping rates for their products, it is stated, in their decisions to establish business in Puerto Rico, since transportation charges are vital factors in their business prospects. The record shows that the 15 percent rate increase raised footwear costs 1.13 percent of the value of the product, and candy 1.78 percent. These increases, it is stated, seriously limit the possibilities of expanding mainland business, and discourage people from establishing business in Puerto Rico.

"63. The records show that the promotional rates are too low, and appear to be noncompensatory, even with the 15 percent increase, and there is some question as to whether the further 12 percent increase renders said promotional rates compensatory."

20. No exceptions were taken to the findings quoted above. They are borne out by the record, and no additional evidence was presented at the second further hearing relating to these issues. We adopt the findings set forth above.

Cost increases

21. The cumulative rate increases under investigation herein aggregate about 29 percent. The last prior general rate increase in the Puerto Rican trade was made effective November 12, 1951. Since that date, the expenses of the respondents have increased substantially. For example, Bull shows that stevedoring wages in the United States have increased 46 percent and in Puerto Rico about 63 percent, fuel oil costs have increased 23 percent, vessel operating costs as a whole 54 percent, crew wages 62 percent, vessel repair costs 50 percent, and insurance 52 percent. Comparable cost increases are shown for the other three carriers in the trade.

22. There is evidence that the carriers, through increased efficiency of operations, have endeavored to minimize the impact of the stated cost increases. Stevedoring expenses account for a substantial proportion of total operating expenses. Bull shows that from 1951 to the end of 1957 loading costs in New York increased from \$4.06 to \$4.69 per ton, and discharge costs at the same port from \$4.80 to \$5.74 per ton, increases of 15.5 percent and 19.6 percent respectively, far lower than the wage increases shown. This favorable result is attributed to increased efficiency in loading and discharge operations, the leasing of modern improved terminal facilities, and in some degree to the use of containers and vans. Loading and discharge at San Juan, P.R., however, reflected more closely the wage increases, attributed to the lesser efficiency of port arrangements and labor. Loading costs at that port in the same period increased from \$2.02 to \$3.07 per ton, and discharge costs from \$2.79 to \$4.71 per ton, increases of 52 percent and 68.8 percent respectively.

23. Waterman shows, in addition to the cost increases stated above, that effective in October 1958 longshore wage increases at Puerto Rican ports will after that date increase stevedoring expenses by about 92 cents per ton, and that known prospective wage increases will by the end of 1958 increase crew wage costs by \$160,000 annually over the wage levels for 1957.

Allocation methods

24. Of the principal respondents, Waterman is the only carrier which operates an exclusive Puerto Rican service. The remaining respondents, as shown in paragraphs 1-9, *supra*, operate their services to and from Puerto Rico either wholly or partially on a joint basis with other services. This has necessitated allocation of the joint service expenses of the respondents, and of the assets devoted to these services, so as to ascertain as nearly as possible the proper apportionment of expenses and assets between the regulated and nonregulated trades in order to determine the adequacy of revenue in the regulated trade. For this purpose, the respondents have made their allocations principally on ton-mile prorate formulae.

25. Where possible, such as in the case of port and cargo handling expenses incurred in Puerto Rico, the expenses were directly assigned. Most other expenses, including vessel operating expenses, cargo and port expenses in the United States, vessel depreciation, and overhead, were subject to allocation. The need for allocation does not alter the basic factors contributing to vessel operating expenses, the tonnage and the distance carried. In applying the ton-mile prorate, the respondents used the straight-line distances between ports of loading and discharge, since a vessel sailing toward Puerto Rico is also sailing toward the foreign ports of call. Vessel operating expenses and certain other expenses were then allocated to the Puerto Rican service in the proportion that Puerto Rican ton-miles bore to total ton-miles operated in the joint services.

26. Where the ton-mile prorate involved too heavy a burden, as where the allocation was between the Puerto Rican trade and the entire company operation, a revenue prorate was used for convenience, using as factors the proportion that Puerto Rican revenue bore to total revenue. In the case of loading costs, distance is not a relevant factor, and allocations were generally made on the basis of the number of tons handled. In the case of Bull's substantially equidistant Puerto Rican and Dominican destinations, its use of a ton-mile prorate in the allocation of loading and stevedoring costs in the United States resulted in an approximately equal allocation of loading expense per ton.

27. Strike expenses incurred by Bull in 1957 were allocated by it on the basis of a revenue prorate, because the development of a ton-mile formula would have made necessary a port-to-port analysis of tonnage and distances for a minimum of 155 sailings, a burdensome task. Since the Dominican revenue is substantially higher per ton than Puerto Rican revenue for approximately the same distance, as shown below, this actually allocated a higher proportion of strike expenses to the Dominican traffic, and a lower proportion to Puerto Rican traffic, than would have resulted from the use of a ton-mile prorate.

28. Vessel assets were assigned to the Puerto Rican services of the respondents on the proportion of the vessel operating days in those services, allocated where necessary on the basis of a ton-mile prorate. Assets in Puerto Rico were directly assigned to the Puerto Rican service, and terminal property in the United States was generally allocated on a revenue prorate.

29. At the request of other parties, the respondents in most instances also computed their expenses on the basis of revenue prorate formulae. The interveners contend that for the purposes of this proceeding revenue prorate allocations should be used. For example, the Commonwealth argues that segregation of the joint voyage results on the Friday sailings of Bull gave inordinately excessive profits to the Dominican portion and exceptionally large losses to the Puerto Rican portion in 1957, as to which on a ton-mile prorate Bull shows a combined net revenue on the joint sailings, after depreciation and overhead but before taxes, of \$46,345, with allocation of a loss of \$244,973 to the Puerto Rican portion and a profit of \$291,318 to the Dominican portion.

30. In 1957 total tonnage carried by Bull on the joint voyages was 311,699 tons, of which 36,784 tons were Dominican cargo. In the same year total joint voyage freight revenue was \$5,367,625, of which Dominican revenue was \$924,140. The Commonwealth characterizes as anomalous the results of the ton-mile prorate which attributes to the Dominican trade net revenue equal to 30 percent of each dollar of revenue. Bull's revenue per ton in the Dominican trade in 1957

was 36 percent higher than in the Puerto Rican trade (\$27.04 versus \$19.94), and costs of discharge in the same year in the Dominican Republic were only 22.5 percent of like costs in Puerto Rico (\$1.06 versus \$4.71). These data indicate that the profit results derived through use of ton-mile prorata formulae reflect with a reasonable degree of accuracy the inherent differences as between the Dominican and Puerto Rican trades. The Commonwealth also argues that the use of the ton-mile prorata results in somewhat higher unit costs on the joint service voyages than on the Thursday sailings of Bull which serve only Puerto Rico. These results are fully explained by the facts that there were more sailings in 1957 in the joint service with about the same amount of total tonnage, and consequently lower tonnage per voyage and higher costs per ton, and also that the joint voyages were subject to overtime costs because of late sailings not incurred on the Thursday sailings.

31. The Manufacturers Association of Puerto Rico contends that allocation of expenses for the Friday joint service sailings of Bull should be made on a so-called known-cost-per-ton method. By this method, allowable expenses on the joint service voyages would be confined to the unit costs incurred on the Thursday sailings which serve Puerto Rico exclusively, which costs can be computed without the necessity for allocations. Such a method bears no relation to the realities of the situation, and is clearly erroneous.

32. The Commonwealth alternatively suggests that in lieu of allocation in the case of Bull's Friday sailings, the total profit results on the joint voyages should be included, on the grounds that the Dominican operation is a byproduct of the Puerto Rican trade which could not stand on its own feet; that only 13 percent of the cargo on the joint voyages is Dominican; that Dominican Cargo is less than one-half of 1 percent of the total Bull Puerto Rico tonnage; and that the carrier itself recognizes the incidental nature of the Dominican operations by failing to allocate out of its asset statements any portion of vessel and other property values attributable to the Dominican operation. The issue here is not the profit accruing to Bull as a result of its joint service operations, but the justness and reasonableness of the rates under investigation, which in the nature of the case must be decided on the basis of the adequacy of the revenues derived therefrom. There is no suggestion that allocation is not necessary in the case of the other respondents which operate joint services, and no good reason appears why Bull should be accorded special treatment in this respect. The authorities cited clearly support agency action in general rate proceedings in adopting appropriate means of effectuating a separation of the regulated and nonregulated portions of an integrated enterprise. See *Cities Service Gas Co. v. Federal Power Com'n*, 155 F. 2d 694, 704-5 (1946), *cert. den.* 329 U.S. 773; and *Colorado Interstate Gas Co. v. Federal Power Commission*, 324 U.S. 581, 586-92 (1945). The facts of record clearly indicate that dissimilar rates and cost factors as between the Puerto Rican and Dominican operations make allocation necessary in order to avoid distortion of the operating results in the Puerto Rican trade and the use of the resulting data in assessing the lawfulness of the rates under the jurisdiction of the Board.

33. In the light of the findings in paragraphs 23-31, *supra*, we agree with the examiner that the use of the ton-mile prorata formulas, where utilized, and the other allocation methods adopted by the respondents, are reasonable and proper for the purposes of this proceeding.

Depreciation and Bull's vessel book values

34. In general, the vessel book values maintained by the respondents represent the cost of acquisition, plus additions and betterments, depreciated on the basis of a 20-year vessel life down to a residual scrap value amounting to 2.5 percent of acquisition cost. In the discussion immediately to follow, vessel acquisition costs and book values are stated as approximations, since precision is not necessary for disposition of the issues here raised, and since precise data, after allocations, are shown, *infra*.

35. Alcoa's C-1 vessels, utilized in its gulf service, were acquired in 1941 and 1942 at costs ranging from \$1 million to \$1,250,000, and by December 31, 1956, had been depreciated down to net book values ranging from \$223,000 to \$322,000. Its C-2 vessels used in the North Atlantic service were acquired in 1946 and 1947 for \$1,200,000 to \$1,333,000 and by the same date had been depreciated down to \$535,000 to \$635,000.

36. Waterman's C-2 vessels used in its gulf service were acquired in 1947 and 1948 for \$984,000 to \$1,100,000, and by December 31, 1956, had been depreciated down to about \$500,000. Lykes' C-1 vessels were acquired between

1943 and 1949, for \$943,000 to \$1 million, and by the same date had been depreciated down to slightly less than 50 percent of original cost.

37. In the case of Bull, most of the C-2 vessels had been acquired in 1947 at costs of \$948,000 to \$1,006,000 by A. H. Bull New Jersey, and by December 18, 1956, had been depreciated down to about \$750,000. Two of the C-2 vessels were entered in 1954 by A. H. Bull New Jersey in exchange for fully depreciated Liberty vessels and modest amounts of cash, and entered on the books at about \$208,000 and \$248,000. These two C-2's by December 18, 1956, had been depreciated down to about \$173,000 and \$203,000. Annual depreciation charges in 1957, if taken by A. H. Bull Delaware on the basis of the vessel book values maintained in the books of A. H. Bull New Jersey, on the portion of the fleet allocated to the Puerto Rican trade, would have amounted to \$396,887.

38. As of December 18, 1956, as a result of the transaction detailed in paragraphs 4-6 above, the C-2 vessels utilized by Bull in its Puerto Rican services were entered on the books of A. H. Bull Delaware at acquisition costs of about \$853,000 to \$979,000, representing as there stated about 70 percent of their then appraised values. As a result, depreciation charges claimed herein by Bull in 1957, and actually taken on the books of A. H. Bull Delaware, amounted to \$929,514, or \$532,627 more than would have been claimed by A. H. Bull New Jersey in the event the transaction had not taken place. Similarly, the increased depreciation taken in the first 6 months of 1958 amounted to \$364,540, as against \$194,456 had the transaction not occurred.

39. Domestic market value for C-2 vessels, exclusive of extras, in April 1957 is shown in the record as \$1,350,000, which by October 1958 had declined to \$875,000. The earlier value reflects the high market values which were the result of the Suez Canal crisis which created a sudden shortage in available vessels. The later value reflects the decline in vessel market values resulting from the depression in the shipping industry which occurred between the dates given. For C-1 vessels, exclusive of extras, the domestic market value in April 1957 was \$1,100,000, which declined by October 1958 to \$575,000.

40. The Commonwealth contends that, with respect to depreciation generally, the vessels of the respondents have already been depreciated below realistic economical residual values as reflected by the market values shown, that residual values based on nominal scrap value are unrealistic and do not represent an accurate measure of the actual residual value of the vessels which can be presumed to have a service life of more than 20 years and will at the expiration of that time either be sold or traded in at prices much higher than scrap value, that the residual service value of the vessels is at least equal to their book values at the end of 1955, and that as a consequence depreciation charges taken by the respondents should be disallowed in their entirety as an item of expense in determining the results of the operations by the respondents in the Puerto Rican trade.

41. The depreciation practices of the respondents, and the estimated residual value, are recognized for tax purposes, and are in conformity with the Board's General Order 24 (46 C.F.R. sec. 284.2(f)). Contrary to the contention of the Commonwealth, this record affords no basis for conjecture as to the possible residual value of the vessels utilized in the Puerto Rican trade, other than the traditional and long-accepted residual value used by the respondents. To adopt the suggestion of the Commonwealth would substitute speculation for certainty, since depreciation charges allowed would fluctuate with varying judgments as to possible future residual values which may be affected by unforeseen circumstances. We reject the contention of the Commonwealth.

42. Public counsel and the interveners also contend that for the purposes of this proceeding the depreciation charges claimed by Bull on the basis of vessel acquisition costs entered on the books of A. H. Bull Delaware must be disallowed, depreciation allowed only on the book values maintained prior to the ACS transaction by A. H. Bull New Jersey, and vessel book values determined on the basis of projections of the books of A. H. Bull New Jersey. The arguments are based in the main on the rule propounded by the Supreme Court, particularly with regard to utility companies such as power and light and telephone companies, that the proper guide to book value of a utility's property is the cost as of the time when the property to be valued was first acquired by a public utility or dedicated to the public use. See *A.T. & T. Co. v. United States*, 299 U.S. 232, 239 (1936), and cases there cited. *A.T. & T. Co. v. United States*, *supra*, upon analysis, is also authority at pages 240-244 for the statement that acquisition cost of the last owner in a bona fide arm's-length transaction may

properly be entered on the books of the acquiring utility, and is the proper depreciation base.

43. There is no suggestion here that the ACS purchase was anything other than an arm's-length transaction between unrelated interests, that there was any attempt at collusion so as to arbitrarily inflate the values of the Bull properties, or that the purchase was an improvident one. In fact, based upon vessel market values shown in the record, the Bull assets were acquired at bargain prices, and the vessel acquisition costs entered upon the books of A. H. Bull Delaware represent the true acquisition costs incurred by that corporation. The Board has no jurisdiction over financial transactions involving carriers such as these subject to the statutes, and the decision here must be based on the facts as they exist.

44. It is found that the depreciation charges claimed as expenses by the respondents, including those claimed by Bull on the basis of vessel acquisition costs incurred by A. H. Bull Delaware, are reasonable and proper for the purposes of this proceeding, and that the vessel book values maintained by A. H. Bull Delaware reflect the true acquisition costs of the vessels utilized by Bull in its Puerto Rican services.

Valuation and rate bases

45. General: The conference advocates rate bases calculated as of June 30, 1958, notwithstanding that the first increase here involved became effective in January 1957. Waterman individually contends for rate bases compiled as of December 31, 1957. Public counsel and the Manufacturers Association of Puerto Rico contend that rate bases should be constructed as of December 31, 1957, applicable to the 1957 rate increase, and as of June 30, 1958, applicable to the 1958 rate increase. The Commonwealth assigns values based on a composite analysis of the totality of the exhibits submitted. In *General Increase in Hawaiian Rates*, 5 F.M.B. 347, 354-5, we stated that carriers are entitled to a fair return on the reasonable value of the property at the time that it is being used for the public, and that in ascertaining the "reasonable value" of the carrier's property devoted to public services, we are not bound by any artificial rules or formula, citing *San Diego Land Company v. National City*, 174 U.S. 739 (1899), and *the Minnesota Rate Cases*, 230 U.S. 352 (1913).

46. This proceeding involves two separate rate increases, the second superimposed upon the first. The record, includes data concerning the actual operations of the respondents for almost a full year under the first of these increases, and for almost 6 months under the combined increases. In the usual rate increase case, determination of the lawfulness of the increases proposed is necessarily predicated upon projections of revenues and expenses expected in the future, and the property values for the purpose of calculating the expected rate of return are most readily determinable as of the time the rate increases are proposed. Here, however, particularly with regard to the 15-percent increase, the results of operations under the increased rates can be ascertained with some degree of certainty. The most precise method of resolving the issues presented by this proceeding would be to determine average values of the property of the respondents employed during 1957, applying operating results for the year 1957 to the resulting figures to determine rates of return actually earned during that year, and then to ascertain values as of December 31, 1957, applying projected operating results for the year 1958, based upon actual operations during the first 6 months of that year, to the ascertained values as of December 31, 1957, the approximate date when the 12 percent increase became effective, so as to compute expected rates of return for the year 1958. Such extreme precision, however, is not required, and it is doubtful that the different values arrived at would be substantially at variance with each other. For the purposes of this proceeding, therefore, property values will be determined as of December 31, 1957, and the resulting rate bases applied to the actual operating results so far as they can be determined on the record for the year 1957, and the projected results for the year 1958. While this may have a tendency to lessen somewhat the values applicable to the year 1957 because of depreciation, it is deemed that the results will not be unreasonable.

47. In table III below are set forth the rate bases claimed by the conference, and in table IV the rate bases claimed individually by Waterman.

TABLE III.—Rate bases claimed by the conference

Bull:	
Vessels.....	¹ \$12,048,584
Working capital.....	2,000,000
Brooklyn terminal (nonowned).....	5,000,000
Philadelphia terminal (nonowned).....	3,064,916
Baltimore terminal (nonowned).....	6,000,000
Puerto Rico terminals.....	4,062,194
Other property.....	747,387
Claims pending.....	22,584
Total.....	<u>32,945,665</u>
Alcoa:	
Vessels.....	5,183,638
Working capital.....	1,233,955
New York terminal (nonowned).....	2,015,400
Baltimore terminal (nonowned).....	1,117,000
Mobile terminal (nonowned).....	1,901,800
New Orleans terminal (nonowned).....	825,700
Puerto Rico terminal (nonowned).....	1,500,000
Terminal equipment (nonowned).....	356,600
Structures.....	98,371
Equipment.....	231,957
Spare parts.....	67,734
Total.....	<u>14,532,155</u>
Lykes:	
Vessels.....	3,784,230
Working capital.....	445,212
Terminal property.....	3,589
Other property.....	92,801
Statutory reserve funds.....	2,022,488
Total.....	<u>6,348,320</u>
Waterman:	
Vessels.....	4,170,856
Working capital.....	1,208,091
Mobile terminal (nonowned).....	1,000,000
New Orleans terminal (nonowned).....	750,000
Puerto Rico terminal.....	1,242,716
Furniture, fixtures and other equipment.....	167,604
Office building, mobile.....	289,491
Puerto Rico stevedore equipment.....	23,863
Puerto Rico wharf equipment.....	1,239
Total.....	<u>8,853,860</u>
Grand total.....	<u>62,680,000</u>

¹ This figure does not include any value assigned for Liberty ships, and, because of an error in calculation in the conference brief, should be \$12,288,581 on the basis claimed by the conference.

TABLE IV.—Rate bases claimed by Waterman

Method 1:

Vessels, average of reproduction cost depreciate and net book value.....	¹ \$4,666,171
Other property.....	3,474,913
Working capital.....	1,892,107
Total.....	<u>10,033,191</u>

Method 2:

Vessels, market value.....	3,070,500
Other property.....	3,474,913
Working capital.....	1,892,107
Total.....	<u>8,437,520</u>

¹ This figure, although labeled average of reproduction cost depreciated and net book value, embraces as an element the depreciated value of replacement vessels rather than reproduction cost depreciated of the vessels employed.

48. The items listed in table III designated as "other property;" "structures;" "equipment;" "spare parts;" "terminal property;" "furniture, fixtures, and other equipment;" "office building;" and "stevedore equipment"; and "wharf equipment" represent allocations of owned property carried into the claimed rate bases at net book value, and there is generally no dispute concerning the propriety of including such asset values. There is little justification for the inclusion of the item called claims pending in the rate base claimed for Bull, and it will not be further considered.

49. Lykes alone among the respondents does not claim as a part of its rate base the values of any nonowned terminals, on the ground that its vessels utilize a number of different public terminals, and the ratio of its use of any particular terminals would be minimal and difficult to determine. Accordingly, it claims as expense items in its profit and loss statements the full rentals paid for terminal use. Lykes includes in its claimed rate base statutory reserve funds amounting to \$2,022,488, made up of capital reserve funds of \$1,734,919 representing accumulated depreciation on the portion of its vessels allocated to the Puerto Rican services, and special reserve funds amounting to \$287,569. Both of these reserve funds are required to be maintained by Lykes in connection with its subsidized foreign operations under section 607 of the Merchant Marine Act, 1936, as amended, 46 U.S.C. 1177. We are not impressed with the argument advanced that these statutory reserve funds should be considered as property devoted to the Puerto Rican service, and no further consideration will be given to this item.

50. Vessels: In table III, the vessels allocated to the Puerto Rican trade by the respondents are valued by weighting original and reproduction costs, depreciated, using as factors 70 percent of reproduction cost depreciated and 30 percent of acquisition costs, depreciated. These percentages were rejected by us in our decision in *General Increases in Alaskan Rates and Charges*, 5 F.M.B. 486, 498 (1958). The respondents argue that Bull has in the distant past built its own ships and operated in the Puerto Rican trade with newly constructed tonnage, and has developed plans for replacement vessels, although there are no present indications that new ship construction will be embarked upon in the near future; that Alcoa has likewise had naval architects prepare designs for replacement vessels; and that Lykes is contractually committed to a ship replacement program in connection with its subsidized operations. For these reasons, the conference contends that the circumstances presented in this proceeding differ from those in the *Alaska* case and justify the use of the 70 percent/30 percent weighting. The examiner used an average of original costs and reproduction costs, citing prior decisions, see *Rates of Inter-Island Steam Navigation Co., Ltd.*, 2 U.S.M.C. 253 (1940); *Alaskan Rates*, 2 U.S.M.C. 558 (1941), and 2 U.S.M.C. 639 (1942); *General Increase in Hawaiian Rates, supra*; and *General Increases in Alaskan Rates and Charges, supra*.

51. Table V below shows, after allocation, the original and reproduction costs, depreciated as of December 31, 1957, the averages therefore, and the market values of the vessels employed by the respondents. The market values are averages of the domestic market values stated in paragraph 39 above, taken so as to eliminate extremes of value occasioned by the special circumstances detailed. As in the case of table III, the vessel values in the case of Bull do not include assigned values for Liberty-type vessels which the record indicates will occupy a diminishing role in its operations.

TABLE V.—Vessel values

	Original cost depreciated	Reproduction cost depreciated	Average	Domestic market values
Bull.....	\$4,875,995	\$16,890,740	\$10,883,318	\$7,620,900
Alcoa.....	1,421,166	7,487,081	4,454,124	3,913,972
Lykes.....	993,200	5,409,969	3,201,585	2,359,806
Waterman.....	1,152,132	6,535,356	3,843,744	3,167,275
Total.....	8,442,493	36,323,146	22,382,771	17,061,953

52. We disagree with both the conference and the examiner as to the fair and reasonable value of respondent's vessels. What the respondent carriers are entitled to is "a fair return on the reasonable value of the property at the time it is being used for the public," *San Diego Land Company v. National City, supra*. We find that value of the vessels on the domestic market at or about the time the rate increase is requested with adjustments to eliminate short-term peaks in vessel values, is the proper method for determining the reasonable value of the property being used for the public. We do not feel that we should assume for ratemaking purposes that a carrier has reproduced its vessels. When the carrier has reproduced a vessel and placed it in service he is entitled to a fair return on its value. Until then, the shipping public should not be forced to pay rates based even in part on the conjectural value of some phantom vessel which may never serve it. To the extent the conclusions set forth in prior cases disagree with those expressed herein they are overruled.

53. We find the fair and reasonable values of the vessels of the respondents devoted to the Puerto Rican service to be those set forth in table V under the heading "Domestic Market Values."

54. Working capital: The examiner found that a fair and reasonable allowance for working capital as an element of the rate bases would be approximately one-twelfth of the annual operating expenses experienced in 1957 of the respective carriers, exclusive of depreciation, or \$1,800,000 for Bull, \$860,000 for Alcoa, \$360,000 for Lykes, and \$615,000 for Waterman.

55. The conference excepts to this finding, contending that the carriers are entitled to (1) a buffer fund equivalent to one-twelfth of annual operating expenses, exclusive of depreciation, plus (2) an amount sufficient to cover the lag in revenue collections behind the related disbursements citing *Alaskan Rates*, 2 U.S.M.C. 558, 566 and 2 U.S.M.C. 639, 645. Under this method they say Bull is entitled both to the buffer of one-twelfth of operating expenses or \$1,800,000 and the collection lag of \$1 million and that the other respondents are entitled to a similar working capital determination.

56. The interveners and public counsel also except to the examiner's finding, contending that working capital should be computed on the basis of the requirements laid down in General Order 31, 46 C.F.R. sec. 286.3(a)(1).²

57. In *General Increases in Hawaiian Rates, supra*, we used General Order 71 as the method for the computation of working capital as an element of the rate base. In *General Increases in Alaskan Rates and Charges, supra*, we disallowed claimed working capital computed by the formula detailed in the *Alaskan Rates* cases, *supra* and allowed working capital calculated in accordance with General Order 71 (superseded by General Order 31). In that case we characterized that general order as basically consisting of the average voyage expenses for each vessel in the carrier's fleet.

58. The examiner concluded that use of the formula was not appropriate in this proceeding, pointing out that under limitation 3, the inclusion by Bull in its current liabilities of annual installments due of its debt, and annual interest payments would leave it with a negative balance for working capital. We find nothing in this record to warrant a reversal of our holding in *General Increases in Hawaiian Rates, supra* and *General Increases in Alaskan Rates and Charges, supra*. We will, however, clarify those two decisions in one respect. In determining a fair and reasonable allowance for working capital as an element of the rate bases in proceedings such as these, we will limit the amount to that determined under limitation 4 of General Order 31 and give no consideration to limitation 3 of that order.

² Limitations 3 and 4 of that order which relate to the computation of working capital are set forth in appendix A.

59. We find that the fair and reasonable allowance for working capital would be the amount computed under limitation 4 of General Order 31, or \$1,087,000 for Bull, \$264,100 for Alcoa, \$222,100 for Lykes, and \$285,800 for Waterman.

60. Property used but not owned: As is indicated in table III, Bull, Alcoa, and Waterman claim as elements of their rate bases substantial amounts representing the value of terminals and terminal equipment used by them in their Puerto Rican services which are owned by others. In conjunction with these claims, Bull has adjusted its operating expenses to substitute owners' expenses detailed on the record in the case of the Brooklyn and Philadelphia terminals for terminal rentals, and has credited its revenues with the profits derived from the operation of the Puerto Rican terminals by its subsidiaries; Alcoa has adjusted its operating expenses to eliminate rental costs for terminals; and Waterman has adjusted its operating expenses to eliminate profits from the operation of its Puerto Rican terminal owned by Waterman P. R. However, Waterman claims as operating expenses the rentals paid for terminals at Mobile and New Orleans, and the record affords no basis for determining the amount of such rental payments. The Baltimore terminals used by Bull and Alcoa are leased to them free by the owners as an inducement to increase the amount of traffic moving over the piers, and Bull's rental payments for its Philadelphia pier are substantially less than owners' costs.

61. The examiner found that in the case of Bull and Alcoa the inclusion in their allowable rate bases of the value of property used but not owned with the concurrent elimination from operating expenses of rentals paid for such property and the substitution of owners' expenses therefor, is reasonable and proper. In the case of Waterman, however, he found that since it was impossible to determine on the record its rental payments for the use of its Mobile and New Orleans terminals or the expenses of the owners thereof, that the value of such property should not be included in its rate base. In arriving at the value of property used but not owned he found the proper valuation to be the net book value where ascertainable, or if not, he found a value on the basis of other evidence of record. The examiner concluded that prior decisions of the Board had allowed for rate base purposes the value of property used, although not owned by the carriers, which he states is in accord with the accepted theory of valuation.

62. In our most recent ruling on this point in *General Increases in Alaskan Rates and Charges, supra*, we included the value of a chartered vessel in the carrier's rate base but excluded certain nonowned shoreside property since it was difficult if not impossible to determine its proper value. We think we were in error in including the value of the nonowned assets in the carrier's rate base. We are not impressed with the arguments of the conference that such assets should be included in the rate base of some of the carrier respondents in this proceeding. We note that Lykes did not claim as part of its rate base such nonowned property, and it appears that Bull did not include piers owned by the Commonwealth of Puerto Rico. Further, in the case of Waterman, the examiner refused to include the value of such property in its base. Again in the case of Alcoa, in arriving at a value to be included in that company's rate base the examiner because of insufficient data reduced the amounts claimed by the same percentage he had reduced Bull's claimed values. These same problems led us to conclude in *General Increases in Alaskan Rates and Charges, supra*, that certain nonowned property was not properly includible in the carrier's rate base.

As indicated above, such assets were claimed by some of the carriers and not by others, were excluded by the examiner in the case of Waterman, and Bull apparently did not claim all of such property. Thus we are asked to arrive at rate bases of various carriers containing different elements depending in some cases on the claims of the carriers and in others on the evidence submitted by it as to the value of the property. This we will not do. Proceedings such as this are difficult enough without adding to the problems. The respondents in this case present no binding precedent that requires us to include such property in a carrier's rate base. We do not feel that either logic or law necessitates their inclusion. The carriers are not devoting their capital to the shipping public insofar as such property is concerned. It is proper of course to include in allowable expenses the rental paid and other expenses of the carriers which arise by reason of the use of such facilities, but to include the value of nonowned property in the rate bases in our opinion would grant the carriers a windfall at the expense of the shipping public.

63. Bull's Puerto Rican terminal: The examiner included in the rate base of Bull \$2,144,572, the net book value as of December 31, 1957, of certain Puerto Rican terminals owned by Bull and devoted to the trade. Public counsel excepts to this inclusion and the Commonwealth contends that the amount should be reduced by some \$475,000 representing the total acquisition cost of certain property adjoining one of the terminals on which is located a building which occupies about one-twelfth of the area and which is leased for purposes not related to the Puerto Rican trade. The remainder of the property is admittedly used for terminal services and the building rentals are credited to the Puerto Rican services of Bull. We agree with the examiner that \$2,144,572 should be included in the rate base of Bull as representing the value of Bull's Puerto Rican owned terminals. This property is owned by Bull and devoted to the trade, rentals from the building will be credited to Bull's Puerto Rican service, as well as any profit realized from the operation of the terminal. Under such circumstances there is no justification for excluding the terminals in whole or in part from Bull's rate base.

64. Recapitulation: Table VI below sets forth the total values of the property of the respondents devoted to their Puerto Rican services, as found for the purposes of this proceeding, reflecting the findings specifically made above concerning the valuation of vessels, working capital, and terminals and terminal equipment as of December 31, 1957, and reflecting also the net book values of all other property as of December 31, 1957, as found in the record. In the case of Lykes, net book values for such other property were not submitted as of December 31, 1957, and the values included are the averages of net book values shown in the record as of June 30, 1957, and as of June 30, 1958.

TABLE VI.—Values

Bull	\$11,491,987
Alcoa	4,570,966
Lykes	2,680,115
Waterman	5,350,285

REVENUES AND EXPENSES

65. General: As stated in paragraph 46 above, in the present posture of this proceeding it is possible to determine with reasonable accuracy the actual operating results experienced by the respondents during 1957 in the performance of their Puerto Rican services, and thus to make findings concerning the lawfulness of the 15 percent increase. Reasonable projections for the future may be made based upon revenue and expense data submitted by the respondents covering the first 6 months of operations in 1958 under the combined 15-percent and 12-percent increases, by which the lawfulness of the combined increases may be gaged. Numerous issues are raised by the parties concerning the revenues to be assigned to the Puerto Rican trade, and the expenses allowable. Certain of these, relating to allocation methods employed by the respondents, depreciation claimed by them, and the adjustment of expenses to eliminate rental costs for nonowned terminals or to substitute owners' costs therefor, have been treated separately above, and need not be restated here. In restating the assignable revenues and allowable expenses, the findings there made will govern. Generally, disposition of the issues raised concerning 1957 expenses and revenues will suffice, and later data restated accordingly.

66. Interveners and public counsel contend that the revenues of the respondents for 1957 should be restated so as to give effect to a full year's operations under the 15-percent increase, which became effective on January 10 of that year. It is also contended that the expenses of Bull for that year should be adjusted so as to eliminate the expenses incurred during the strike mentioned in paragraph 8 above, of which \$643,037 of general operating expenses and \$146,483 of depreciation are allocable to the Puerto Rican services, on the ground that this strike was unique in character, and occurred for reasons not related to the Puerto Rican trade. As to the strike expenses, the examiner concluded that the effect on the revenue position of Bull was no different except in degree from that of any other strike for which no claim was made. We disagree with the examiner. This strike was unrelated to the ordinary labor-management controversies, and the general operating expenses incurred during the strike should be excluded from Bull's expenses for 1957, but no sound reason

is shown for the elimination of depreciation expenses incurred during that period. With respect to the restatement of revenues to cover a full year of the 15-percent increase, we agree with the examiner that the operating results for 1957 do not enter into projections for the future, and restatement thereof so as to reflect a full year's operation would serve no useful purpose.

67. 1957 revenues and expenses: Bull shows operating revenues for 1957 of \$21,646,383, which are adjusted to include amounts of \$117,954 covering interest revenue from a mortgage on the Brooklyn terminal held by Bull, \$86,018 covering net profit of the Puerto Rico terminal companies, and \$68,187 covering top wharfage collected in Philadelphia. Public counsel and the interveners contend that the revenues should be further adjusted so as to include \$38,335 of the net profits of Caribbean Dispatch, Inc., earned in carrying bagged raw sugar under contract terms which would normally have been transported by Bull at tariff rates, and \$60,069 of profits earned by Bull in conducting independent stevedoring operations at Puerto Rico for other carriers during the strike period. Of these adjustments, the examiner found that only the inclusion of the interest revenue is improper, that it is included only for the reason that the value of the Brooklyn terminal is claimed in Bull's rate base and that it is no more a part of the earnings derived from the Puerto Rican service than the revenue from any other unrelated investment. We agree with the examiner, as to the interest revenue, but are of the opinion that elimination of the strike expense for 1957, as found above, requires also that the bagged raw sugar and stevedoring profits should be excluded from the assigned revenues.

68. Bull shows total allocated operating expenses of \$22,644,027. Adjustments upward include \$95,872 covering costs incurred as a result of actions brought in Puerto Rican courts for overtime wages by stevedore foremen, and \$69,273 covering the excess of actual Puerto Rican overhead expenses over budget provisions therefor. Adjustments downward include a credit of \$145,299 for stevedore overhead charged into the stevedoring account; \$72,319 to substitute owners' expenses for terminal rentals; \$3,813 to cover a correction in the allocation of 1957 strike expenses; and a stipulated correction of \$35,232 in management and operating commissions. The Manufacturers Association of Puerto Rico contends that the adjustment of expenses to cover the foremen's overtime suits is improper on the ground that the expense is attributable to a violation of law by Bull. The suits arose from a difference of opinion as to Bull's liability for overtime payments, and the costs incurred by Bull are operating costs properly includible.

69. The Manufacturers Association of Puerto Rico also contends that Bull's 1957 expenses should be adjusted downward by \$6,398 to reflect an allocation of inactive vessel expense and depreciation of other equipment to the Dominican traffic not made by the respondents, and this adjustment is considered proper. We agree with the examiner that operating expenses should be reduced by \$139,404 to cover the excess of commissions paid to A. H. Bull & Co. over and above the costs of the latter as allocated on a revenue prorate.

70. Alcoa shows gross operating revenues in 1957 of \$9,175,949. Operating expenses after allocation were \$10,615,037, adjusted downward by \$423,120 to exclude pier rentals.

71. Lykes shows gross operating revenues in 1957 of \$3,774,843. Operating expenses after allocation were \$4,540,813.

72. Waterman shows gross operating revenues in 1957 of \$9,416,267, covering both its gulf and North Atlantic operations. Expenses were \$8,771,685. Intervenors contend that the expenses should be adjusted to eliminate charter hire of \$32,400 on a vessel included in the rate base, and to eliminate \$13,770 interest on a vessel mortgage. Since the vessel is not included in the rate base the charter hire paid is a proper expense. Interest payments are not operating expenses as such, but are rather costs of capital employed which should be borne out of profits earned, and an adjustment is proper. It is also contended that Waterman's revenues and expenses for 1957 should be restated so as to eliminate the results of its North Atlantic service, which was conducted in that year at a loss, for the reason that such service was only temporarily operated. As stated above, operating results for 1957 do not enter into projections for the future, and the service was instituted by Waterman with the full intention of making it permanent. To eliminate the results of this service would distort the actual revenue position of Waterman in defiance of the facts of record.

73. Giving effect to the findings above, including elimination of strike expenses and adjustments relating thereto, and the adjustment in Bull's revenues as found in paragraph 67 above, and the inclusion of rental expenses and deletion of owners' expenses for nonowned property disallowed in the rate base, table VII below shows the operating results of the respondents in 1957, as adjusted:

TABLE VII.—1957 operating results

	Revenues	Expenses	Net profit or (loss)
Bull.....	\$21,800,488	\$21,835,989	(\$35,501)
Alcoa.....	9,175,949	10,615,037	(1,439,088)
Lykes.....	3,774,843	4,540,813	(765,970)
Waterman.....	9,416,267	8,757,915	658,352

74. 1958 revenues and expenses: As stated in paragraph 17 above, the revenue projections of the respondents, where given, were based on an extension of their most recent experience, that for the first half of 1958, subjected to adjustments for known or contracted cost increases. Revenues for 1958 were calculated as twice those for the first 6 months, adjusted to give effect for the full year to the 12 percent increase which became effective January 15. Expenses for the first 6 months were adjusted upward by about 1 percent. Waterman did not submit future projections, basing its position on the fact that it ceased operations in the trade and its successor in the operation is not a respondent herein. Waterman contends, therefore, that no consideration may be given to the future operations of Waterman, P. R., in the trade in determining the lawfulness of the rates here under investigation. Waterman, P. R., is, however, an existing operator in the Gulf-Puerto Rico trade, its rates are identical with those under investigation, and it has agreed to be bound by the findings herein. Accordingly, for the purposes of this report, projected 1958 results for the combined Waterman and Waterman, P. R., operation from the gulf ports to Puerto Rico are calculated below on the same basis as used by the other respondents. Revenues for the first 6 months are doubled, and adjusted upward by \$54,000 as suggested by public counsel to reflect a full year's operation under the 12 percent increase. Expenses for the first 6 months, as adjusted, are doubled and adjusted upward by 1 percent to reflect the cost increases expected by the other respondents. This will fail to give effect to the cost increases shown by Waterman individually as stated in paragraph 23 above, but it is expected that similar cost increases will also affect the other respondents, and they are disregarded here in order to treat all the carriers similarly.

75. In computing operating expenses for the first 6 months of 1958, Bull included vessel repair expenses on a reserve basis in its voyage accounts. For the period these reserves totaled \$197,428. Actual repair expenses during the period were \$57,951 less than this amount, and public counsel and the interveners contend that the excess should be credited to Bull's expenses and only actual repair costs allowed. Bull's actual repair expenses were \$413,311 in 1957, and \$562,795 in 1956, and it does not appear that the reserves are excessive. For the purpose of projecting expenses over the full year 1958, the reserves for repair expenses will be allowed.

76. The combined Waterman and Waterman, P. R., expenses reported for the first 6 months of 1958 in their Gulf-Puerto Rico service include costs of \$8,617 attributable to transfer of the Bienville cargo at New Orleans into a vessel regularly providing breakbulk service to Puerto Rico. Waterman contends that this amount should not be disallowed. It is an expense of a nonrecurring nature and for the purpose of projecting future operating results, the contention has merit, and the adjustment requested will be made.

77. Giving effect to the findings relating to 1957 revenues and expenses, and those made specifically with regard to 1958, table VIII shows the revenues and expenses of the respondents for the first 6 months of 1958, and the projected operating results for the full year 1958.

TABLE VIII.—1958 operating results

	First half 1958		1958 projected		
	Revenues	Expenses	Revenues	Expenses	Net profit or (loss)
Bull.....	\$11,706,918	\$11,384,232	\$23,650,643	\$23,070,350	\$580,293
Alcoa.....	4,215,049	4,990,803	8,484,000	10,027,000	(1,543,000)
Lykes.....	1,940,279	2,150,083	3,919,737	4,318,234	(398,497)
Waterman and Waterman P.R.....	4,121,323	3,417,080	8,296,646	6,902,501	1,394,145

DISCUSSION AND CONCLUSION

In our order remanding this proceeding for further hearing we directed that the record developed should be sufficient for consideration of the issues either through analysis of all carriers, or through consideration of Bull as the rate-making carrier. The examiner treated the respondents as a whole. We disagree. In *General Increases in Hawaiian Rates, supra*, and again in *General Increases in Alaskan Rates and Charges, supra*, we followed our prior decisions and adhered to the principle that the dominant carrier in a noncontiguous domestic trade will be taken as the ratemaking line. We find nothing in this record which warrants a different conclusion here. Bull is by far the dominant carrier in the trade and its gross revenues during the first half of 1958 exceeded those of the other three carriers. They were approximately 2½ times those of the next largest carrier. Consideration of the issues in this proceeding will be made on the basis of Bull as the ratemaking carrier.

On the basis of the findings set forth herein Bull in 1957 suffered a loss of some \$35,500 and the 15-percent increase has been shown to be fully justified. On the basis of the 1958 projection which we have found to be reasonable, Bull on a rate base of \$11.5 millions during 1958 would earn 5 percent before income taxes.

The Commonwealth contends that Bull's allowable return should be 5 percent. The conference argues that a rate of 10 percent after taxes is reasonable. Public counsel says 7.5 percent after tax is the proper rate of return in this proceeding.

Our predecessors fixed 7 percent after taxes in *Rates of Inter-Island Steam Navigation Co., Ltd.*, 2 U.S.M.C. 253, 262 (1940), and 7.5 percent in *Alaskan Rates*, 2 U.S.M.C. 558, 573. Recently in *General Increases in Alaskan Rates and Charges, supra*, at pages 500 and 501, we allowed rates of return of 5.22 and 8.90 percent upon two alternative methods of rate base valuation considered by us. We find that a rate of return of not in excess of 7.5 percent after income taxes of the rate bases determined as set forth in our findings is fair and reasonable.

In view of our finding as to a fair and reasonable rate of return and the finding as to Bull's earnings under the combined 15-percent and 12-percent increases we find it unnecessary to give further consideration on the contentions of the Commonwealth with respect to the treatment of income taxes.

The conference excepts to the examiner's failure to include in the rate base a separate amount for going concern value. As we said in *General Increases in Alaskan Rates and Charges, supra*, at page 500, "Neither the Board nor any of its predecessors has ever included a separate 'going concern value' in a rate base of any of the respondent carriers."

We see no reason to depart from the fair-return-on-fair-value standard which the Board and its predecessors have used and reject the contention of the conference that the operating ratios experienced by the respondents should be considered by us as a method of determining the reasonableness of the rates under investigation in this proceeding.

ULTIMATE FINDINGS

We find and conclude that the 15- and 12-percent increases here under investigation are just and reasonable.

An order discontinuing this proceeding will be entered.

By the Board.

JAMES L. PIMPER, *Secretary.*

APPENDIX A

General Order No. 31, provides in pertinent part as follows (46 C.F.R. sec. 286.3(a)(1) in part):

LIMITATION (3)—ADJUSTED WORKING CAPITAL

The excess, if any, of the balance of "adjusted working capital" of the operator and its wholly owned subsidiary companies as of the balance sheet date, after interim adjustments thereof, as provided in paragraph (d) of this section, and allocated to subsidized operations as provided in paragraph (e) of this section, over "limitation of adjusted working capital" in subsidized operations, as defined in limitation (4), shall be deemed to be "capital held in reserve" in the business and shall not be taken into account in determining "capital employed."

For the purpose of applying this limitation, "adjusted working capital" shall include only the following accounts defined in part 282 of this chapter:

Accounts:

100-199 (369): Current assets (less reserves and provision for accrued deposits in statutory reserve funds other than voluntary deposits, which shall not be accrued for deposit).

200: Unterminated voyage expense.

375-389: Deferred charges (to operations) and prepaid expenses.

Less accounts:

400-534: Current liabilities (excluding mortgage notes—vessels, and other liabilities payable from statutory reserve funds).

495: Advance ticket sales and deposits.

500: Unterminated voyage revenue.

The provision for accrued deposits into the statutory reserve funds referred to in accounts 100-199 hereinabove shall include, but is not limited to, the following:

(i) Accrued depreciation on vessels required to be deposited into the capital reserve fund;

(ii) Proceeds from sale or loss of vessels and other amounts which, upon collection, are required to be deposited into the capital reserve fund;

(iii) All accrued mandatory deposits into the special reserve fund.

LIMITATION (4)—LIMITATION OF ADJUSTED WORKING CAPITAL

Adjusted working capital as determined under limitation (3) shall be allowed as "capital employed" to the extent of the total average voyage expenses employed in subsidized operations determined as follows:

Average voyage expenses shall be determined on the basis of the actual expenses of operating and maintaining the subsidized vessels (excluding layup expenses) for a period represented by the average length of time of all round voyages (excluding layup periods) calculated separately for each subsidized service (line). For the purposes of this limitation, the term "line" shall be deemed to mean those described in part I of the operating-differential subsidy agreement, or in instances where the routes or services described therein are not designated as "lines," then the trade routes referred to in part I of the subsidy agreement shall for such purposes be deemed to be "lines": *Provided*, That in any event passenger services shall be deemed to be "lines" separate and distinct from freight services: *And provided further*, That in instances where unsubsidized vessels are operated in subsidized services and are subject to the reserve and recapture provisions of the agreement, they shall not be considered as a separate category but shall be included with the subsidized vessels for the line involved.

This determination shall be made in the following manner:

First: By dividing the sum of such expenses for the accounting period involved applicable to the subsidized vessels in each such service (line) by the aggregate number of days (excluding layup days) consumed in all voyages of such vessels in each such service (line) terminating during such period;

Second: By multiplying the quotient thus obtained by the number of days (excluding layup days) in the average voyage in each such service (line); and

Third: By multiplying the resulting product by the quotient of the total number of days (excluding layup days) consumed in voyages of subsidized vessels

in each such service (line) terminating during the accounting period divided by the number of calendar days within the accounting period.

The expense of operating and maintaining the subsidized vessels shall include overhead (accounts 900-955 less accounts 670 and 895) allocated to subsidized operations under § 286.4 and total operating expense—terminated voyages (accounts 701-799 in pt. 282 of this chapter). For the purpose of this limitation (4), if in any instance, the average subsidized voyage in any subsidized service (line), as determined above, is of less than 90 days' duration, the expense of hull and machinery insurance (account 755) and P. and I. insurance (account 757) shall be determined to be that for a period of 90 days: *Provided*, That such allowance for insurance expense shall not, in the aggregate, exceed the total actual insurance expense for the accounting period. Expenses used for this purpose shall be those included in the annual accounting for each calendar year, filed under part 292 of this chapter, and shall not be adjusted thereafter.

BRIEF OF RESPONDENT FEDERAL MARITIME BOARD
AND STATEMENT OF RESPONDENT UNITED STATES
OF AMERICA

IN THE
United States Court of Appeals
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 15,846

COMMONWEALTH OF PUERTO RICO, PETITIONER

v.

UNITED STATES OF AMERICA AND FEDERAL MARITIME BOARD,
RESPONDENTS

No. 15,847

UNITED STATES ATLANTIC & GULF-PUERTO RICO CONFERENCE,
ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA AND FEDERAL MARITIME BOARD,
RESPONDENTS

**On Petitions for Review of an Order of the Federal
Maritime Board**

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Washington 25, D. C.
November 7, 1960

STATEMENT OF QUESTIONS PRESENTED

The questions presented by the Commonwealth of Puerto Rico¹ are:

1. Whether the Board erred in ascribing to the carriers' vessels a valuation for rate base purposes equal to their market value.
2. Whether the Board allowed an excessive rate of return to the carriers.
3. Whether the Board allowed the carriers to charge an excessive annual vessel depreciation expense.

The questions presented by the United States Atlantic and Gulf/Puerto Rico Conference, et al., are as follows:

1. Whether the Conference has standing to seek review of the Board's order.
2. Whether the Board erred in considering the Bull Steamship Company to be the "ratemaking carrier" in the trade.
3. Whether the Board erred in excluding from the carrier's rate base terminal properties which are used, but not owned, by the carriers.
4. Whether the Board understated the carriers' rate base by allowing an unreasonably low working capital.
5. Whether the Board erred in ascribing to the carriers' owned terminal facilities a valuation for rate base purposes equal to their net book value.
6. Whether the Board erred in rejecting an operating ratio approach, rather than the fair-return-on-rate-base approach, in determining whether the carriers' rates are just and reasonable.

¹ The Commonwealth's petition for review raises additional questions, which are abandoned in the Commonwealth's brief. Accordingly, respondents' statement of the questions presented by the Commonwealth is limited to only those questions which the Commonwealth is now pressing.

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v.

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RESPONDENTS

No. 15,847

UNITED STATES ATLANTIC & GULF-PUERTO RICO CONFERENCE,
BULL-INSULAR LINE, INC., ALCOA STEAMSHIP COMPANY,
INC., LYKES BROS. STEAMSHIP CO., INC., and RICHARD
KINSELLA, PETITIONERS

v.

UNITED STATES OF AMERICA AND FEDERAL MARITIME BOARD,
RESPONDENTS

**BRIEF OF RESPONDENT FEDERAL MARITIME BOARD
AND STATEMENT OF RESPONDENT UNITED STATES
OF AMERICA**

JURISDICTIONAL STATEMENT

The jurisdiction of this Court is based on the Judicial Review Act of December 29, 1950 (64 Stat. 1129, as amended, 5 U.S.C., Section 1031, *et seq.*).

(1)

STATEMENT OF THE CASE

A. Statutory Background

The proceeding arises out of petitions by the Commonwealth of Puerto Rico (Commonwealth) and by the United States Atlantic & Gulf-Puerto Conference, et al. (Conference),¹ for review of an order of the Federal Maritime Board entered after an investigation held by the Board pursuant to Section 18 of the Shipping Act, 1916 (39 Stat. 735, as amended, 46 U.S.C. Section 817), and Section 3 of the Intercoastal Shipping Act, 1933 (47 Stat. 1426, as amended, 46 U.S.C. Section 845), wherein the Board found certain rate increases of the Conference to be just and reasonable. The increases applied to rates governing the common carriage of ocean-borne cargo between United States Atlantic and Gulf ports and ports in Puerto Rico.

On December 4, 1956, the Conference filed with the Board tariffs increasing the existing rates by 15 percent. Exercising the powers vested in it by the 1916 and 1933 Acts, the Board entered an order, January 4, 1957, instituting an investigation into the lawfulness and reasonableness of these increases. The Commonwealth moved for leave, and was permitted, to intervene in the proceeding.

Hearings were held before a hearing examiner of the Board in April, 1957. However, prior to issuance of an initial decision by the Examiner, the Conference, on August 14, 1957, filed a further general rate increase of 12 percent to become effective on September 14, 1957. The Board suspended the 12 percent rate increase for four months, as authorized by Section 3, Intercoastal Shipping Act, 1933 (46 U.S.C. § 845), thus postponing the effective date of the increase to January 15, 1958. The Board's investigation was expanded to cover this second increase, and further hearings were held in October, 1957. An initial decision was issued by the hearing examiner, and ex-

¹ Joined with the Conference as petitioners are its individual steamship line members and its secretary.

ceptions thereto were filed with the Board. One of the principal issues raised in the exceptions was whether the examiner had erred in not requiring the carriers to produce books and records to substantiate certain financial statements which they had offered in evidence. On June 13, 1958, the Board remanded the proceedings to the examiner for further hearings, with a direction to the carriers to produce substantiating records for all financial exhibits submitted at the previous hearing. Following such further hearings, in which the carriers produced and/or made their underlying records available to all parties for inspection and copying, the examiner issued an initial decision on September 10, 1959 (J.A. 54). In the initial decision, the examiner found both the 15 and the 12 percent rate increases to be just and reasonable.

Exceptions were filed to the initial decision, and oral argument was heard by the Board. Thereafter, the Board issued the Report and Order of April 28, 1960, which are the subject of these review proceedings.

B. The Board's Findings

In its Report and Order of April 28, 1960 (J.A. 12), the Board announced its findings and conclusions, with reasons therefor, holding the rate increases to be just and reasonable (J.A. 53).

In arriving at its conclusions, the Board followed the traditional "fair return on rate base" approach, calculating the carrier's rate base by placing a valuation on the property devoted to the trade by the carriers (the rate base), and allowing the carriers a fair and reasonable return thereon.

The Board treated the Bull Steamship Company, one of the Conference members, as the "ratemaking line" (J.A. 49). This approach was based principally on the facts that Bull was by far the largest carrier in the trade, and that in its capital investment, revenues, and expenses, Bull was fairly representative of all the lines in the trade (J.A. 49).

The Board's findings and conclusions, and its reasoning in support thereof, may be summarized as follows:

1. *Valuation and Rate Base*

In determining the rate base, the Board followed the principle that the carriers are entitled to a fair return on the reasonable value of the property at the time it is being used for the public (J.A. 34). In valuing the carriers' vessels, the Board rejected such approaches as original book cost depreciated (suggested by the Commonwealth) and reproduction values (urged by the carriers), and instead, used as a basis the domestic market values of the vessels for the period under consideration. These market values were averaged out so as to eliminate fairly wide fluctuations occasioned early in the period by the Suez crisis and later in the period by a depression in the shipping industry (J.A. 37-38).

In determining the value of terminals, the Board distinguished between those owned by the carriers and those used-but-not-owned by the carriers. For the used-but-not-owned terminals, the Board did not include their value in the rate base for the reason that the carriers are not devoting their own capital to the public service. However, the Board did allow the carriers to charge against revenues, as operating expense, the rental and other expenses incurred by the carriers by reason of their use of such facilities (J.A. 42). For the carrier-owned terminals, the Board, like the examiner, allowed the carriers to include the *net book* value of those properties in the rate base (J.A. 42), but it rejected the carriers' contention that such terminals should be valued at what a willing seller and willing buyer would settle on as a fair price for the property (J.A. 131).

The Board found that a fair and reasonable allowance for working capital as an element of the rate base would be an amount equal to the total of vessel operating expenses for one round voyage for each vessel in the carrier's fleet. This formula is the same as that set up in its General Order 31, Limitation 4, by which "capital neces-

sarily employed" is calculated for carriers operating under subsidy contract in the foreign trades (46 C.F.R. 286.3(a)) (J.A. 40).

2. *Expenses*

The only expense item in dispute in this proceeding is depreciation expense. As to this expense item, the Board found that in December, 1956, American Coal Shipping, Inc., through a subsidiary (Olympia Corporation) purchased substantially all of the stock of A. H. Bull Steamship Co. of New Jersey. In January, 1956, in substantially complete liquidation of A. H. Bull, New Jersey, its assets were transferred to the books of Olympia Corporation, since renamed A. H. Bull Company of Delaware, and the vessels were entered on the latter's books at an acquisition cost of \$12.9 millions, the latter figure representing about 70 percent of the appraised value of the vessels (J.A. 19). The same vessels had, at the time of the transfer, a book value of \$5.2 million on the books of the predecessor corporation. The purchase of Bull by Olympia was found on undisputed evidence to be an arms-length transaction between unrelated interests. The Board concluded that in the light of the bona fides of the transaction and the reasonableness of the purchase price, as compared with the substantially higher market values for vessels, the acquisition cost of the vessels as entered on Bull of Delaware's books constituted a proper depreciation base (J.A. 33).

The carriers depreciate their vessels, on the basis of a 20-year service life, from acquisition cost down to a residual scrap value amounting to 2.5 percent of acquisition cost (J.A. 30). In the case of Bull's vessels, the residual value was thus set at about \$55,000 per vessel. The Board found that such depreciation practice is recognized for tax purposes, and is in conformity with the Board's regulations; and it approved this method of depreciating the vessel assets. The Board rejected the Commonwealth's contention that residual value must be based on predicted market values at the end of the vessel's service life, on the ground that such a method would substitute speculation for certainty (J.A. 31-32).

3. *Dominant Carrier Theory*

After thoroughly examining all the evidence relating to traffic and operations of the four carriers in the trade, the Board determined that Bull is by far the dominant carrier in the trade.² It makes three sailings weekly, as compared with only weekly services by each of the other three carriers (J.A. 17 & 20). Unlike any of the other three carriers, Bull is not engaged in substantial vessel operations in other trades (J.A. 17 & 20). And with the ships used in the Puerto Rico trade, Bull calls at no foreign ports on two of its three weekly sailings, while on the third, it calls only at one foreign port and handles a proportionately small volume of foreign traffic (J.A. 17). Two of the other three carriers carry substantial volumes of foreign cargo, and call at a number of foreign ports, with the same ships which serve Puerto Rico (J.A. 20). Consequently, the Board followed the theory, also followed in its prior decisions, that the dominant carrier in a noncontiguous domestic trade may, on facts such as these, be taken as the ratemaking line. The issues in the proceeding were determined, therefore, by treating Bull as the ratemaking carrier (J.A. 49).

4. *Rate of Return*

The Board carefully projected an estimate of operating results for the year 1958, based on actual operating results of record for the first half of 1958. 1958 was the first year in which the carriers operated under the increased rates. The Board found that Bull, with a rate base of \$11.5 millions, would earn before taxes a net profit of \$580,293 for 1958 with the increased rates in effect.

² The gross revenues for the first half 1958 were as follows:

Bull	\$11,706,918
Alcoa	4,215,049
Lykes	1,940,279
Waterman and Waterman P.R.....	4,121,323
	(J.A. 48)

Such earnings are equivalent to a return of 5.0 percent, before taxes, on the rate base. The Board found that a rate of return of not in excess of 7.5 percent after income taxes would be fair and reasonable (J.A. 49). Inasmuch as the combined 15 percent and 12 percent increases thus resulted in a return of not more than 5.0 percent before income taxes to Bull, the ratemaking carrier, the Board reached the ultimate conclusion that the increased rates were just and reasonable (J.A. 50).

5. Operating Ratio as Measure of Reasonableness

The Board, finding that the rate increases under investigation were just and reasonable under the fair-return-on-fair value standard adopted by the Board and its predecessors in similar investigations, found no reason to depart from that standard. Consequently, the Board rejected the contention of the Conference that the operating ratio theory, rather than the rate base theory, be used as a method of determining the reasonableness of rates (J.A. 50).

C. The Instant Petitions

The instant petitions, filed separately by the Commonwealth and by the Conference although consolidated for argument, seek review of the order of the Federal Maritime Board finding the increased freight rates in the United States Atlantic and Gulf Coast to Puerto Rico to be just and reasonable. On the one hand, the Commonwealth challenges (a) the vessel valuations, (b) the rate of return, and (c) the depreciation expense allowed by the Board as unreasonably oppressive on the shippers, and as excessively liberal to the carriers. On the other hand, the Conference challenges as unreasonably oppressive on the carriers and excessively liberal to the ratepayers (a) the Board's valuation of terminals, (b) its exclusion from the carriers' rate base of certain terminals which are used, but not owned, by the carriers, and (c) the amount of working capital allowed by the Board. The Conference, in addition, attacks the Board's (d) use of the "ratemaking line" ap-

proach, and (e) the Board's refusal to use the operating-ratio formula rather than the fair-return-on-rate-base formula in determining a just and reasonable rate level.

SUMMARY OF ARGUMENT

There are three basic considerations which closely affect any exercise by the Board of its power to prescribe just and reasonable rates under the Intercoastal Shipping Act, 1933.

The first of these considerations is the fact that the Board cannot control entry into the regulated field, for there is no statutory requirement of a license or certificate of public convenience and necessity as a prerequisite to operation in the domestic off-shore trades.

Secondly, there is no limitation upon abandonment of service. Any carrier in the domestic off-shore trade is entirely free to decrease the number or scope of its sailings or to abandon service altogether.

Thirdly, the capital equipment employed in the regulated off-shore trades is mobile and immediately useable in unregulated business. The vessels employed in the regulated trade can be shifted readily into the foreign trades where the level of rates is unregulated.

These three factors distinguish the regulated off-shore domestic trades from all other businesses in which rates are regulated. Such other businesses where there are limitations on inauguration and abandonment of service, and where capital equipment is not adaptable to unregulated use, give rise to regulatory principles which are not always applicable to the regulatory problems confronting the Board with respect to rates in the domestic off-shore trade.

A. Summary of Argument in Response to Brief of Commonwealth of Puerto Rico

I. The Board was correct in valuing vessels at current market value for rate base purposes. If the Board were to limit vessel valuation to net book cost depreciated, as urged by the Commonwealth, carriers would feel a strong inducement in inflationary times such as these to take their

ships out of the regulated trade and place them into foreign trades.

The basic reason for using net book value in determining a rate base lies in the great difficulty encountered in determining an exchange value for the capital equipment used by most types of utilities. This consideration does not apply in the case of ships, for ships are commonly bought and sold in the market, and they have a readily ascertainable exchange value.

Another reason for adhering to net book value for rate base purposes is the fact that the capitalization of net earnings furnishes an unrealistic yardstick. This is because future net earnings depend on the rates allowed by the regulatory body. In the case of ships, however, current market value is in fact a capitalization of earnings realizable in the unregulated trades. In other words, vessels have a value independent of what the Board allows for rate base purposes, since they are immediately available for use in unregulated trades.

In view of these considerations, the use of market value by the Board was reasonable and proper. It resulted in a valuation very substantially lower than that argued for by the carriers who sought to introduce reproduction cost as a relevant factor. The Board's use of market value has the merit of insuring that carriers will not abandon the domestic service for more profitable ventures elsewhere.

II. The Board did not err in finding a $7\frac{1}{2}\%$ rate of return to be reasonable. Contrary to the Commonwealth's contention, Bull should not have been restricted to earnings which would merely permit it to pay the interest on its debt capital and to realize a reasonable return on its equity capital. Since the company is to an overwhelming extent debt-financed, the approach urged by the Commonwealth would result in an unreasonably small return on the investment risked in the trade. Whether the capital is borrowed or owned, its value remains the same and the public benefits to the same degree.

In any case, the Board simply engaged in *obiter dictum*

in establishing a $7\frac{1}{2}\%$ rate of return as the maximum allowable rate. In fact, as the Board expressly found, Bull, the ratemaking carrier, earned a return of only 5.0% on its rate base during the first year of operation under the increased rates. With allowance for income taxes, this rate of return is reduced to roughly 2.5%. This can scarcely be condemned as an excessive rate of return.

The rate of return allowed by the Board compares reasonably with the returns allowed in comparable trades serving Alaska and Hawaii. It is lower than the 10% rate of return allowed to subsidized carriers in foreign commerce before recapture of subsidy. It is not out of line even with returns earned by other regulated utilities which have the benefit of a franchise or other protected monopoly. The rate of return allowed by the Board is very substantially below the rate of return contended for by the carriers.

III. The Board did not allow excessive depreciation charges. In this connection, the Commonwealth argues that the Board erred in allowing Bull to use as a vessel acquisition cost a cost higher than the original cost to a predecessor company. It further argues that the residual values for ships have been fixed too low, with the consequence that annual depreciation expense is too high.

With respect to the acquisition cost allowed for Bull's vessels, the Board found on undisputed evidence that the present owners of the Bull Steamship Company purchased that company from its predecessors in a *bona fide*, arms-length transaction. The purchase price was prudent and, as ratably apportioned to the vessels, resulted in an acquisition cost for the vessels considerably below their then market value. It is settled that where a utility purchases capital equipment at a cost higher than the seller's book cost, the excess may properly be amortized over the life of the property if such excess is a "true increment of value." In the instant case, the higher acquisition cost reflected a true increment of value since ships had in fact appreciated in value. Since the acquisition cost of the ships was the result of a *bona fide*, arms-length purchase,

and was manifestly within the range of prudent investment, the Board was correct in allowing Bull to claim depreciation on the basis of such cost.

With respect to residual value, the Board allowed the carriers to charge annual depreciation against a residual value equal to estimated scrap value. The Commonwealth argues that the residual value is unrealistically low, and that at the end of their service lives, the ships are likely to be worth much more. The Commonwealth's argument is based entirely on conjecture. It is impossible to know whether after the approximately seven remaining years of their service life, the ships will be worth more or less than the residual value ascribed to them on the carriers' books.

If it should turn out that the ships have a value in excess of the book residual value, the carriers are required under the tax laws to apply such excess against the tax base of any replacement vessel in the purchase of which the proceeds of the prior vessel are used. Thus, even if there is an excess, such excess does not represent a wind-fall to the carrier, but instead, reduces the depreciation expense borne by ratepayers during the life of the replacement vessel.

B. Summary of Argument in Response to Brief of United States Atlantic & Gulf-Puerto Rico Conference

I. The Conference's petition should be dismissed for want of jurisdiction. The Board's decision finds the Conference's rate increases to be just and reasonable. It consequently does not adversely affect the Conference, nor does it have any present impact upon the Conference. All that the Conference can complain about is the possible application of statements in the Board's report in a way that may adversely affect petitioners in some future rate case if future contingencies should so eventuate. This position is wholly conjectural and fails to present at this time any case or controversy for decision. Moreover, the Conference can not at one and the same time both support the Board's decision and attack it.

II. The Board did not err in considering Bull as the "ratemaking carrier." The "ratemaking carrier" approach followed in the instant case is consistent with Board precedent. It correctly recognizes that Bull is by far the largest carrier in the trade, and that its service is almost entirely free of any foreign admixture. Unlike the other carriers in the trade, Bull's service presents no serious problems of cost or asset allocation.

In arguing against the "ratemaking carrier" approach, the Conference wishes to introduce Alcoa and Lykes into the ratemaking picture in a way that accords them equal weight with Bull and Waterman. Since Alcoa, and to a lesser extent, Lykes, operate in an atypical fashion, their introduction into the ratemaking picture would materially distort the results.

The use of Bull as the "ratemaking carrier" brings about an end result closely similar to that which would be reached if a composite of Bull, Waterman, and Lykes were used. Since Alcoa, by reason of its highly peculiar operations is not entitled in any event to consideration in the ratemaking process, the Board's use of the "ratemaking carrier" approach did not adversely affect the Conference.

III. The Board did not err in excluding from the carriers' rate base certain terminal properties used but not owned by the carriers. The exclusion of such non-owned property is consistent with Board precedent. A contrary approach would permit the carriers to earn a return on property which they have never risked or put into the public service.

This is especially true in the instant case. The terminal used by Bull at Philadelphia is rented to Bull by the Municipal Port Authority at a favorable rental as a promotional device to increase traffic through the Port of Philadelphia. The terminal used by Bull at Baltimore is owned by an I.C.C.-regulated railroad, which permits Bull to use it free of charge. Thus, both the Philadelphia and Baltimore terminals have already been dedicated to and paid for by the public, and it would be an injustice to

require the public to pay again for such property. Such payment would give Bull an unearned windfall. With respect to the terminal used by Bull at New York, the Board was satisfied that the rental payment was prudent, and the inclusion of such payment as an operating expense made it unnecessary to include the asset value as an element of Bull's rate base. The Board thus treated all used-but-not-owned terminals consistently.

IV. The Board did not err in allowing the carriers an insufficient working capital. As computed by the Board, the working capital allowed the carriers was equivalent to the expense of one complete round voyage for each of the ships in the service. This sum is ample to meet all working capital needs of the carriers. Under the terms of the carriers' tariff, freight in the Puerto Rico trade is prepaid and consequently the carriers, unless they depart from their own tariff, have in hand the voyage's revenues before the voyage begins. The Conference has failed to show that it needs any allowance greater than that fixed by the Board.

V. The Board did not err in ascribing to carrier-owned terminals a rate base valuation of net book value. The carriers contend that since the Board allowed market value for ships, it should have done the same for carrier-owned terminals. The record, however, contained no evidence of market value for terminals. All that was available was an appraised value resulting from the consideration of a number of factors, including original cost, reproduction cost, present and future revenues, etc. There would have been no consistency if the Board used this appraised value for terminals and true market value for ships.

Moreover, the use of any "market value" for terminals introduces great uncertainty, since there is no active exchange of terminal properties. The Board was correct in using net book value for carrier-owned terminals.

VI. The Board did not err in rejecting the operating ratio approach. It has never followed such approach in any precedent case, although it has often been urged to

do so. The nature of the steamship industry is such as to make the fair-return-on-fair-value approach reliable. Since it is the method traditionally used, the Board would need some important reason for departing from it. The record discloses no such reason. Moreover, the Conference cannot claim that it is prejudiced by the Board's refusal to use the operating ratio approach, since the Board found the rate increases to be just and reasonable on the basis of the approach which it did follow.

ARGUMENT

In empowering the Board to prescribe "just and reasonable" rates, the Intercoastal Shipping Act, 1933 (46 U.S.C. Sections 843-848), employs terminology which resembles that employed in other rate-regulatory statutes. But this resemblance should not be permitted to obscure some very important differences between the statutory scheme entrusted to the Board's jurisdiction and those entrusted to other rate-regulating agencies. These differences are so basic that they cast grave doubt upon arguments premised upon analogies between the Board and such other agencies as the I.C.C., C.A.B., F.P.C., and state public utility commissions.

The first of these differences lies in the fact that, unlike other rate-regulating bodies, the Board has no power to control entry into the regulated field of business.³ It cannot grant or withhold a certificate of public convenience and necessity. Such a certificate or some other type of license is a prerequisite to engaging in all other rate-regulated businesses.

Because there is no licensing restriction in the domestic

³ Since enactment in 1940 of Part III of the Interstate Commerce Act, which applies to common carriers by water in commerce between points in one state and points in another state, the Intercoastal Shipping Act applies only to trade between points in the 48 contiguous states, on the one hand, and points in the outlying states and territories, on the other. The most important areas of application of the Intercoastal Shipping Act are the domestic trades to and from Alaska, Hawaii, Puerto Rico, Guam, and the Virgin Islands.

off-shore trades, carriers in those trades do not enjoy a protected monopoly. It is true that such carriers may, as they do in the trade under consideration, join together into conferences for the purpose of fixing rates in concert, as authorized by Section 15 of the Shipping Act, 1916 (46 U.S.C. Section 814). Such conferences, however, are purely voluntary, and regardless of their existence, new carriers are free to enter into the regulated service without any restriction whatsoever. Thus, while carriers in the domestic off-shore trades are subjected to rate regulation, they do not have the countervailing benefit of being protected against excessive competition.

A second difference between the regulatory scheme involved here and those applicable in other public utility fields is the absence of any governmental control over abandonment of service. Any carrier in the domestic off-shore trade, although regulated as to its rate level, is unregulated as to whether and to what degree it will continue to operate in the regulated trade. Any such carrier can at will add to or subtract from its number of sailings or ports served; or it may abandon its service altogether if it wishes to.

A third difference between this regulated trade and most others lies in the mobility and adaptability of the capital equipment. The vessels used in domestic off-shore trade are equally capable of use in unregulated business. In this respect, the carriers' capital equipment is different from pipeline, communications, and power equipment, since these are immobile and unadaptable for use in any unregulated business. Railroad equipment can similarly be used only in regulated business. Even aircraft, although they are mobile, cannot be transferred readily into unregulated services, for there are only a limited number of unregulated activities in which aircraft can be used. The only other regulated business in which the capital equipment is, like ships, readily adaptable to unregulated activity is trucking. But motor carriers are given some protection against excessive competition by the regulatory requirement that new carriers must first obtain a certificate of

public convenience and necessity. It is significant of the adaptability of trucks to unregulated use that the I.C.C. fixes truck rates on an operating ratio basis, rather than on a fair-return-on-rate-base formula. Under the operating ratio approach, carriers are allowed to earn a net profit which is measured in terms of the relationship between operating revenues and operating expenses, and not in terms of the relationship between net profit and capital investment.

The foregoing differences closely affect the Board's rate-making powers. These differences have long been recognized by the Board. In *Alaskan Rates*, 2 U.S.M.C. 558, 572 (1941), the Board's predecessor called attention to the fact that:

"... question arises whether such risks warrant a higher rate of return than would be allowed a land utility. Such utilities operate under public franchise or other protection and are, in effect, monopolies within the areas they serve. Railroads also are afforded protection against undue competition through the issuance of certificates of public convenience and necessity. There is no such protection in the Alaskan trade."

These considerations are such as to give a present relevance to the words of Justice Jackson:

"We are confronted with regulation of a unique type of enterprise which I think requires considered rejection of much conventional utility doctrine and adoption of concepts of 'just and reasonable' rates and practices and of the 'public interest' that will take account of the peculiarities of the business.

* * * * *

"To regulate such an enterprise by indiscriminately transplanting any body of rate doctrine conceived and adapted to the ordinary utility business can serve the 'public interest' as the Natural Gas Act requires,

if at all, only by accident." Dissenting opinion of Justice Jackson, *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 646, 649-650 (1944).

A. *Argument in Response to Brief of Commonwealth of Puerto Rico.*

The Commonwealth attacks three aspects of the Board's order: The valuation of ships at market value; the rate of return allowed by the Board; and the amount of vessel depreciation expense recognized by the Board. The Board is said by the Commonwealth to have been too liberal with the carriers with respect to each of these elements of the Board's order. In so contending, the Commonwealth is in error.

I. **The Board Did Not Err in Valuing Vessels at Market Value.**

The Board rejected the carriers' contention that the vessels should be valued at a weighted average of original and reproduction costs depreciated, weighting the former at 30 percent and the latter at 70 percent.⁴ On this theory, Bull's vessels would have been assigned a value of \$12,048,584 (Conference's Brief on Further Hearing, p. 46, App. A).

Instead, the Board held that reproduction cost should not be a factor in vessel valuation, because "the shipping public should not be forced to pay rates based even in part on the conjectural value of some phantom vessel which may never serve it" (J.A. 38) (Bd. Rep., p. 25). Accordingly, the Board refused to "assume for rate-making purposes that a carrier has reproduced its vessels" (Ibid.). Instead, the Board found that the carriers are entitled to "a fair return on the reasonable value of the property at the time it is being used for the public" (Ibid.). On this theory, the Board fixed Bull's vessel values at \$7,620,900, i.e., the "value of the vessels on the domestic market at or about the time the rate increase is requested, with ad-

⁴The Examiner recommended that Bull's vessels be valued at \$10,883,318, the straight arithmetical average of original and reproduction costs depreciated (J.A. 84-87). (In. Dec., pp. 25, 29).

justments to eliminate short-term peaks in vessel values" (Ibid.).

The Commonwealth contends that the Board should have permitted Bull only to earn a return on the depreciated vessel book cost of \$4,875,995. The Commonwealth's "basic objection is one of fundamental principle" (Comm. Br., p. 14), i.e., that the Board erred in using market value at all, rather than original book cost depreciated. Accordingly, we do not herein reargue the accuracy of the market value as determined by the Board. That value was testified to by a competent, wholly disinterested expert witness from the Maritime Administration's Office of Ship Construction, whose responsibility it is to maintain current information on the market values of vessels of all types. We discuss here only the principle of using market value as the proper formula for valuing vessels in the regulated domestic off-shore trades.

In rejecting the extremes suggested by the Conference and the Commonwealth, and adopting market value, the Board correctly settled on a valuation that was fair and reasonable. Under the controlling case law—of which *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591 (1944), is the basic expression—the ratemaking agency is "not bound to the use of any such formula or combination of formulae in determining rates." 320 U.S. at p. 602. ". . . the result reached, not the method employed, . . . is controlling" (Ibid.). "If the total effect of the rate order cannot be said to be unjust or unreasonable, judicial inquiry under the Act is at an end" (Ibid.).

As pointed out in the introductory passages of this argument, the vessels employed by Bull in this trade are useable in the unregulated foreign trades, and available for such use without limitation.

For this reason, market value is the proper measure of valuation of ships⁵ for ratemaking. So low a value as

⁵ Fixed properties, such as terminals, used by carriers in their regulated operations call for a different method of valuation. In recognition of this fact, the Board valued the terminal properties

book cost depreciated—at a time when ships have, in general, greatly appreciated in value during the years since their acquisition—would be unrealistic. It would tend to discourage, rather than foster, regular and dependable service in the regulated domestic trades. In periods when rates are firm in foreign commerce—i.e., when vessel market values are high—carriers in the regulated domestic off-shore trades will be strongly induced to do what they are always able to do—to put their vessels into more profitable foreign service.

In contending that ships should be held to their net book value and no more, the Commonwealth places great reliance on the “classic dissent” of Justice Brandeis in *Missouri ex rel. Southwestern Bell Tel. Co. v. P.S.C.*, 262 U.S. 276, 289 (1923). One of the principal bases for Justice Brandeis’ disagreement with certain valuation theories theretofore followed was the fact that “It is impossible to find an exchange value for a utility, since utilities, unlike merchandise or land, are not commonly bought and sold in the market.” 262 U.S. at p. 292. This is pertinent and correct in reference to all other utilities; but is not pertinent and correct in reference to common carriers by water. Ships *are* commonly bought and sold in the market, and their exchange value is at least as easily ascertainable as that of land.

A further basis for the Brandeis rationale lies in the fact that “the present value of a utility [cannot] be determined by capitalizing its net earnings, since the earnings are determined, in large measure, by the rate which the company will be permitted to charge; and thus, the vicious circle would be encountered” 262 U.S. at pp. 292-3. The same idea underlies the majority decision in *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 601 (1944), where the Court reasons: “The heart of the matter is that rates cannot be made to depend upon ‘fair

owned by the carriers at their net book cost, depreciated. The Conference, in its petition, assails this method of valuation of terminals as unfairly low (see *infra*, p. 54).

value' when the value of the going enterprise depends on earnings under whatever rates may be anticipated."

These observations have cogency in relation to "captive" utilities, in which capital is committed more or less irrevocably to the regulated business. The capital equipment of such utilities can be used only in regulated enterprises, and can earn only what the regulatory authority will allow. This is not so in the case of off-shore domestic carriers. The carriers in the Puerto Rico trade, with only small operating adjustments, could withdraw their equipment and engage in foreign commerce. Bull already calls to a minor extent at the Dominican Republic with the ships used in the Puerto Rico trade; if rates in the Puerto Rico trade failed to reflect fairly the earning capability of these ships, Bull would be under considerable inducement to reduce or abandon its Puerto Rican service and increase its service at foreign ports in the Caribbean or other areas. So also Lykes, which devotes about 30 percent of its vessel days to domestic calls as against 70 percent to foreign calls in the Caribbean. And Waterman, with services embracing broad trading areas in the trans-Atlantic and trans-Pacific trades, could readily put its two Puerto Rico vessels into these trades where it is well-established, if its management felt that the returns earned by these ships do not fairly reflect their earning capacity. No legal limitation exists to prevent or even hinder such a change in operations.

Thus, unlike most other utilities, where value depends on what earnings the regulatory authority will allow, ocean shipping equipment has a value independent of what the regulatory authority will allow. Vessel values are established, in fact, on precisely the basis that Justice Brandeis correctly observed to be impossible in the case of other utilities: their present values can be, and are, determined by capitalizing earnings, and thus are precisely what their market value is, after all. Vessel market values are a direct reflection of the earning capacities of vessels.

When ocean rates are firm, ship market values are high, and when the contrary is true, vessel values drop.

As the Supreme Court held in the *Hope Natural Gas* case, the ratemaking function "involves the making of pragmatic adjustments" 320 U.S. at p. 602. It is a necessary pragmatic adjustment for the Board to recognize the fact that ships have a particular earning capacity, represented by their market value, and that this earning capacity, if it cannot be realized in the regulated trade, can readily be realized in unregulated trades.

Nor can it be argued that, by operating in a regulated trade, the carriers have elected to surrender temporarily high earning capabilities in return for long range regulatory protection against competition. Unlike other rate-regulated fields, the domestic off-shore trades are open to the entry of any carrier without limitation. The carriers before this Court hold no certificate or license; and no would-be competitor needs any certificate or license to enter the trade in competition with them.

The principle followed by the Board was proper. The Commonwealth concedes, as it must, that "the Board might employ an alternative to prudent investment" (Comm. Br., p. 15). As the Supreme Court said in the *Hope* case:

"* * * it is the result reached not the method employed which is controlling. * * * If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end. * * * and he who would upset the rate order under the Act carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences." 320 U.S. at page 602, 64 S. Ct. at page 287.

The "total effect" of the Board's determination is not unjust or unreasonable. The use of market value for vessel valuation has the merit of tending to insure that the carriers will not abandon the domestic service for greener pastures elsewhere, and thus helps to preserve

regular and dependable service in the domestic trades.⁶ Moreover, the Commonwealth has not carried the "heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences." The rates between Puerto Rico and the mainland have not been shown to be unduly high in relation to rates between the mainland and other off-shore states or territories, or in relation to rates for any other kind of comparable service.

II. The Board Did Not Err in Finding a 7½% Rate of Return To Be Reasonable.

On the theory advanced by the Commonwealth, Bull should be confined to no "greater return than is required to service the debt and pay the cost of equity capital." (Comm. Br., p. 19.) Anything more, asserts the Commonwealth, would "create a windfall to the owners." (Ibid.)

In the case of Bull, a company purchased in early 1957 for \$22 million, only \$100,000 of the purchase price was equity capital. The entire balance was debt capital, borrowed at rates ranging from 4½ to 5 percent. The Commonwealth seems to be arguing that as to the debt capital, Bull should be permitted only to recoup the cost of that capital, i.e., the interest expense, and as to the equity capital, Bull should be permitted only to recoup from the ratepayers a fair return—let us say for the sake of argument, 7½ percent—as reflecting the cost of that capital. On the theory apparently advanced by the Commonwealth,

⁶ The Board has had occasion in the past to concern itself with this question. In *General Increase in Hawaiian Rates*, 5 F.M.B., 347, 356, it said.

"If the book value of Matson's property is used as a rate base, the proposed tariffs may well be said to yield an unreasonably high return. Matson's vessels were purchased at a time when their cost was considerably lower than they are at the present time. If the fleet were liquidated it would have twice the amount of its book value, available for other investment. Therefore, book value, as the measure of the fair value of the property devoted to these trades is entirely unrealistic."

the owners of Bull, on what is in fact a \$22 million investment, should be allowed to earn no profit on the borrowed money, and an annual profit of $7\frac{1}{2}$ percent on the \$100,000 equity, or only \$7,500. Such a return represents an annual profit of about four one-hundredths of one percent on an investment of \$22 million. This is a sure way to inhibit investment.

Whether the money is borrowed or owned, the value of the capital devoted to the public service remains the same. It is the carrier's rate base on which a rate of return should be calculated. It cannot affect the ratepayer if the carrier uses borrowed, rather than owned capital. To the ratepayer, the ships and other facilities which are placed at his service remain the same, and the service afforded him remains as valuable, whether the carrier has used owned or borrowed capital. The carrier, when it borrows capital, assumes the liability to repay it. It does not receive any unconscionable windfall by reason of using borrowed money rather than owned money. The capital comprising the rate base is risked equally, whether it is borrowed or owned.

The question before the Board was "what return should a carrier be permitted as a fair compensation for putting a rate base, of whatever value, into the Puerto Rico trade?" This question the Board answered, by finding that a return not in excess of $7\frac{1}{2}$ percent would be a fair compensation for employing such rate base in the trade. The Board was, in effect, setting an upper limit beyond which it would not find a rate of return to be reasonable.

In making this finding, the Board went somewhat further than was necessary, by way of *obiter dictum*. The Board found that Bull, the ratemaking carrier, was in fact earning under the increased rates a return, before taxes, of 5.0 percent on its rate base (J.A. 49). With allowance for income taxes, this rate of return is reduced to roughly 2.5 percent. It cannot seriously be argued that this is an excessive rate of return.

The *Hope* case tells us that it is enough if the "total effect of the rate order cannot be said to be unjust and

unreasonable." 320 U.S. at p. 602. The total effect of the Board's decision is to let stand a rate structure which returns to the ratemaking carrier the modest return of 2.5 percent on its rate base, after taxes. It is therefore, we submit, a just and reasonable rate order.

Even the 7½ percent return which the Board fixed as a maximum by way of *dictum* "cannot be said to be unjust or unreasonable," in the language of the *Hope* case. "It is not theory but the impact of the rate order which counts." *Hope*, 320 U.S. at p. 602. Here the 7½ percent maximum rate of return, which the Board said it would have found reasonable, is the same as that allowed in comparable trades serving Alaska and Hawaii. It is lower than the 10 percent return on "capital necessarily employed" which is allowed to subsidized carriers in the foreign trades before recapture of profits (see Section 607(c), Merchant Marine Act, 1936, 46 U.S.C. Section 1177(c)). It is not out of line with returns realized at the present time even by public utilities which enjoy a protected monopoly by reason of holding a certificate or some other form of franchise.

It is also far below the rate of return contended for by the carriers. The carriers argued that "in the sharply competitive Puerto Rican trade 10% is a rock-bottom minimum." (Conference's Brief on Further Hearing, p. 50). The carriers argued also that Bull's rate base should be valued at \$32,945,665. (J.A. 35) (Bd. Rep., p. 22). Thus, the Conference was asking for a permissible return for Bull after taxes of \$3,294,566 annually. The Board, however, found Bull's rate base to be \$11,491,987 (J.A. 43) (Bd. Rep., p. 30), and thus, under its *dictum*, would have allowed an annual return for Bull, after taxes, of up to 7½ percent of this amount, or \$861,898. On the rate base contended for by Bull, this return would represent a rate of return of less than 3 percent. The Board allowed, in effect, a return less than one-third of that contended for by the carriers.

There is, in summary, no merit to the Commonwealth's claim. If the return were limited, as the Commonwealth

contends, to "proven capital costs," the carriers would be held to an insufficient return.

III. The Board Did Not Allow Excessive Depreciation Charges.

The Commonwealth argues that the depreciation expense allowed Bull is excessive for two reasons: (a) it is based on an asset cost which is higher than the original cost to the original owners of the assets; and (b) it is based on an unrealistically low residual value, with the result that the amount of asset value to be annually depreciated—i.e., the difference between values when the asset is acquired and when it is disposed of—is greater than if a higher residual valuation were used. Neither contention has merit. The Board, as will be shown, allowed Bull an acquisition cost that properly reflected the cost of acquisition in a bona fide, arm's length transaction, and it allowed as a residual valuation a reasonable amount, based on expected scrap value.

(a) The acquisition cost allowed by the Board was not unreasonably high.

In October 1956, the owners of the Bull Steamship Corporation of New Jersey agreed to sell their stock in that company to a group of purchasers for the price of \$40 million. This was a bona fide, arm's length transaction. There was no relationship whatsoever between the two agreeing parties other than the relationship of buyer and seller (J.A. 120-121).

One of the elements in the purchase price was the large cash reserve of the company, amounting to \$18 million. The purchasers, in short, knew that the purchase represented an outlay of \$22 million for the assets of the company other than cash. The purchasers set up a Delaware corporation named "The Olympia Corporation," and it bought the stock of Bull, New Jersey. After the purchase, the name of the Olympia Corporation was changed to A. H. Bull Company of Delaware.

The \$22 million purchase price was then distributed among the various assets for the ultimate purpose of es-

tablishing an acquisition cost for each asset on the books of Bull Delaware. The method of distribution was a reasonable one. An independent appraisal of market value was made for each asset. So determined, the total appraised market value for all the assets of the company came to approximately \$31.5 million. Thus, the purchase price of \$22 million was equal to 70 percent of the appraisal value. The \$22 million purchase price was then distributed among the component assets by assigning to each 70 percent of its appraisal value. By this method, the six Bull-C-2 vessels were assigned an acquisition cost of \$878,000 each for four of the vessels and \$980,000 each for the other two vessels which had valuable improvements. The actual market value of the four ships in 1957 was \$1,200,000 each, and for the two improved ships was \$1,300,000, as established in the undisputed testimony of the valuation expert from the staff of the Federal Maritime Board (J.A. 194-196, 225). Thus, the acquisition cost assigned to the vessels was roughly 25 percent below their market value.

The assets of Bull, New Jersey, were then transferred to Bull, Delaware, and entered on the books of the latter corporation at the acquisition costs calculated as described above.

The Commonwealth, recognizing that the initial purchase by Bull, Delaware, of Bull, New Jersey's stock was indisputably an arm's length transaction, attacks the transfer of the ships from the New Jersey to the Delaware corporation as a transfer between related interests. It is true that these companies were related, the Delaware corporation having become the parent of Bull, New Jersey, at the time of the book transfer of the ships.

What the Commonwealth overlooks, however, is the fact that the entire purchase, although involving several steps, was intended to be a single transaction. It is settled that ". . . where the essential nature of a transaction is the acquisition of property, it will be viewed as a whole and closely related steps will not be separated. . . ." *Georgia Properties Co. v. Henselee*, 138 F. Supp. 587 (M.D. Tenn.

1955). Thus, in effect, such a transaction is nothing more than the acquisition of the assets of Bull, New Jersey, by the new owners. A subsequent book transfer of these assets, as a step in the process of acquisition, does not have a separate legal effect independent of the entire purchase. *Kanawha Gas and Utilities Co. v. Commissioner of Int. Rev.*, 214 F. 2d 685 (C.A. 5, 1954); *Kimbell-Diamond Milling Co. v. Commissioner*, 187 F. 2d 718 (C.A. 5, 1951); cert. den. 342 U.S. 827 (1951).

What we have, then, is an arm's length purchase of ships at a price which cannot be called anything but prudent, in view of the substantially higher prevailing market prices. Should such a price be discounted by the regulatory authority, and disallowed to the extent that it exceeds the depreciated book cost of these assets to the original owner of the ships? The Board correctly concluded that it should not.

Even where fixed utility equipment was involved, the Supreme Court has held that a prudent, bona fide purchase, made at arm's length, will support the entry of assets on the purchaser's books at the purchase price. In *American Tel. & Tel. Co. v. United States*, 299 U.S. 232 (1936), the Court held that where acquisition costs for valid reasons exceed the seller's book costs, the excess will be considered a "true increment of value" and "provision will be made for amortization of such amounts through operating expenses." (299 U.S. at pages 240, 243.) Of course, they will not be permitted to be amortized if they appear "to be a fictitious or paper increment." (299 U.S. at p. 240.) In the instant case, the higher cost to the new owners does in fact represent a "true increment of value," for the market values of the ships was materially higher than the new owner's cost, which, to the extent it exceeded the old owner's cost, was truly representative of increased value of the asset.

If the rule of the *American Tel. and Tel.* case is properly applicable to such fixed utility assets as communications equipment, it is *a fortiori* applicable to the vessels used in domestic off-shore trade. Such trades are not fran-

chised; and carriers engaging in it are not only open to the competition of new carriers, they are also subject to no restrictions as to abandonment of service. Thus, in contrast to communications equipment, which has a value and is useful only as it is used in a regulated utility, ships have an independent value as assets readily useable in unregulated business. If an investor in the domestic offshore service were limited to an acquisition cost, for depreciation purposes, equal to the original cost of the ships to the original owner, it is safe to say that there would be very little capital available for investment in these trades.

In short, the owners of Bull, Delaware, invested in the ships of that company a sum truly and accurately reflected in the acquisition costs entered on the books of that company. Since the acquisition costs were the result of a bona fide, arm's length transaction, and since such costs were manifestly within the range of prudent investment, they are properly subject to amortization out of operating expense. The Board correctly allowed Bull to claim depreciation expense calculated on the basis of such cost.

(b) Bull's vessel depreciation expense was not improperly based on an unrealistically low residual value of the ships.

The Board, as it has uniformly done in all prior rate cases, allowed the carriers to charge annual depreciation against a residual value equal to estimated scrap value. This was to be depreciated over a 20-year period, the estimated service life of the vessels. This method of depreciation is in accord with the Board's—and the Interstate Commerce Commission's⁷—uniform system of accounts, and it accords with the conventional, long-standing prac-

⁷ The Board and the Interstate Commerce Commission have collaborated in setting up a Uniform System of Accounts to be used by water carriers. Many of the water carriers under the jurisdiction of one agency are also under the jurisdiction of the other, and the Uniform System of Accounts was set up so that a single report could be made and filed by carriers with the two agencies.

tice of vessel owners. It also has been sanctioned by the tax authorities (J.A. 152).

The Commonwealth, however, disputes the use of scrap value as residual value. It points to the fact that vessel values have over the postwar years declined more slowly than anticipated, so that ships bought immediately after the war, such as the ships under consideration, are now, with about two-thirds of their normal service life expired, still worth more than one-third of their original post-war purchase price. The Commonwealth conjectures that when the ships are retired, they will bring not merely the residual scrap value to which the book values of the ships are being depreciated, but instead will be sold or traded in for new ships at a price considerably in excess of the scrap value.

It is possibly true that, if the Board had prescribed a higher value than scrap value, and a correspondingly lower annual depreciation expense, such prescription would be legally valid, if the residual value fixed by the Board could be supported as a reasonable prediction of future value. There is no constitutional or statutory requirement that the operator of a public service shall receive in the end more than he has put into it at the beginning. *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 606-7 (1944). But on the other hand, there is no prohibition against his receiving more if, as here, asset values have in effect appreciated during their useful life.

The nub of the question is, what should be done with the incremental value of assets which are worth at the end of their service life more than the residual value ascribed to them on the carriers' books? Under the Board's view, the carrier will receive this value. Under the Commonwealth's view, the owner is not entitled to this benefit. Only the ratepayers may receive it, in the form of lower annual depreciation expense during the life of the vessel.

What the Commonwealth is really saying is that the carriers should have predicted that vessel values would

not decline to scrap value. The Commonwealth goes on to say that, having failed to predict the still conjectural fact that their resale value at the end of their service lives will exceed the predicted scrap value, the carriers should compensate for their faulty prediction by no longer charging depreciation expense. It should be noted that the Commonwealth does *not* say that when it was set up on the carriers' books, the residual value was unreasonably or capriciously chosen.

While the Commonwealth has the benefit of a decade and a half of hindsight on its side, it still is by no means clear that it is correct in its contention. The ships now being used in the Puerto Rico trade have a few years of service life ahead of them. As of January 1957, the six Bull C-2 vessels principally used in the Puerto Rico common carrier service had, depending on the individual ship, anywhere from 74 to 93 months, or an average of 7 years, of depreciable life ahead of them. The carriers had—and still have—no way of knowing that at the end of those seven years (roughly, January 1964) the ships will be worth more, and if so, how much more, than the predicted scrap value of approximately \$55,000 per ship. There is no assurance that values will not decline more sharply in the next few years. The Commonwealth cannot show that the carriers' claimed residual values are necessarily too low. Whether they are or not is a fact that will not be known for a few more years.

The Commonwealth speculates, however, that it is a fair probability that at the end of their service lives the ships will be worth a good deal more than \$55,000 apiece. Conceding for the sake of argument that this is true, and conceding even that this might have been foreseen when the ships were first acquired immediately after World War II, we question whether it follows that carriers should for this reason be required to base their accounting practices during the life of the vessel on any such prediction. We further question whether depreciation schedules should be periodically revised to reflect changing conjectures about vessel values at the end of their service lives.

The effect of such a prediction is to increase greatly the carriers' capital risk. If residual values are put at a high figure representing the judgment that market values will in the future be high, the carrier is held to a limited depreciation expense that will not restore his investment if, in the end, the market value fails to maintain the predicted level. The Commonwealth's theory, in short, would force the carrier to rely on a highly speculative trade-in or resale value for the recoupment of his capital investment, rather than to rely on the far more certain method of recouping capital during the service life of the ships by an evenly spaced depreciation expense based on a conservative residual scrap value.

The choice, in essence, is between a large terminal recoupment at the end of twenty years, or a more gradual recoupment evenly spaced over the twenty years. The former choice puts on the carriers all risk of loss if the actual residual value turns out to be lower than predicted, and gives the ratepayers precisely the same kind of "wind-fall" which the Commonwealth would withhold from the carrier. The latter choice appears to be the more reasonable, for although it leaves open the possibility that the carrier will get the benefits of any capital gain that results from appreciations in ship values, it merely puts on the ratepayer the not unfair burden of paying out over the vessel's service life no more than its cost of acquisition by the carrier. In short, we do not believe that the ratepayer has ground for complaint if benefits resulting from asset appreciation accrue to the carrier rather than the ratepayer. The alternative, of requiring the carrier to predict appreciations in value and causing him to bear all risk of loss in the event of an erroneously high prediction, makes for too much uncertainty and, in a field where carriers are subject to rate regulation but are not franchised against competition, would tend to discourage investment in new equipment.

Nor can it be assumed that any incremental value would necessarily accrue to the carriers to the exclusion of the ratepayer. What is most likely—and what might be re-

quired by the Board if and when the question is presented—is that the incremental value would be applied to the acquisition cost of the replacement vessel and thus reduce its initial book value, resulting in correspondingly reduced depreciation expense on the replacement vessel.

Under section 1031(a) of the Internal Revenue Code, 26 U.S.C. section 1031(a), no gain or loss shall be recognized for tax purposes if property held for use in business is exchanged solely for property of a like kind to be used in business. This means that a carrier may avoid tax liability on the capital gain realized in the exchange of fully depreciated vessel where the trade-in allowance is in excess of the depreciated basis of that vessel. See I.T. 2615, XI-1 Cum. Bull. 112 (1932). Such capital gain is applied to the purchase price of the replacement vessel so as to reduce its tax basis and thus reduce the depreciation expense allowable for tax purposes against the new vessel.

It is entirely possible that when and if the carriers are able to sell their present vessels for a price materially in excess of the residual value, such "windfall" (as the Commonwealth calls it) would be required by the Board to be deducted from the book value of the replacement ships and thus *pro tanto* to reduce the depreciation expense to be borne by ratepayers during the life of the replacement vessel. Certainly, it would at that time be open to the Commonwealth to make its "windfall" argument, if the Board treated the matter differently. But to make this argument now is premature.

The theory advanced by the Commonwealth is, we believe, less meritorious than the theory followed by the carriers and sanctioned by the Board. The Commonwealth overlooks the fact that at the outset of the depreciation period, it is likely to be impossible to judge reliably what market values will prevail twenty years hence; and it moreover fails to consider the inhibition on investment that would result if the carrier were to be deprived in advance of any benefits that might result from asset appreciation. The depreciation practices under review are, we submit, reasonable, and "the total effect of the rate order cannot be said to

be unjust and unreasonable." *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944).

B. Argument In Response To Brief of United States Atlantic & Gulf-Puerto Rico Conference

Notwithstanding the fact that the Board's order permits the Conference's rate increases to stand, the Conference assails the Board's action as possibly restrictive on future rate actions of the Conference.

The Conference's petition should be dismissed for want of jurisdiction, because it does not present a case or controversy.

The Conference's petition is, moreover, without merit. On the basis of arguments which are unsupported by either the evidence or the applicable law, it seeks a gross enlargement of its rate base which the Conference would no doubt seize upon to justify large further rate increases. In addition, it seeks to overturn the Board's "ratemaking carrier" approach in favor of an approach which would in this trade materially distort the aggregate profit-and-loss position of the carriers, and it seeks to replace the Board's traditional fair-return-on-rate-base approach with a novel operating ratio approach. In all of these contentions, the Conference is in error.

I. The Conference's Petition Should Be Dismissed for Want of Jurisdiction.

The Board's decision finds the Conference rate increases to be just and reasonable, and permits the Conference rate structure to stand undisturbed. There is, therefore, no case or controversy for the Conference to bring before the Court. An earlier motion by respondents for dismissal of the Conference's petition was denied by the Court, without prejudice to its renewal at this time. The respondents accordingly renew the motion.

The Conference seeks to find standing to sue by arguing that the Board's order lays down principles which adversely affect the Conference. Even though the rate increases have not been interfered with, the Conference asserts

that these principles somehow have an immediate impact upon the Conference.

The unanimous decision of the Supreme Court, per Justice Brandeis, in *United States v. Los Angeles and S.L.R. Co.*, 273 U.S. 299, 309-310 (1927), is dispositive of the Conference's position:

"The so-called order here complained of is one which does not command the carrier to do, or refrain from doing anything; which does not grant or withhold any authority, privilege, or limits; which does not extend or abridge any power or facilities; which does not subject the carrier to any liability, civil or criminal; which does not change the carriers existing or future status or condition; which does not determine any right or obligation." *Supra*, 309-310.

The Conference cites the decision in *Rochester Tel. Corp. v. United States*, 307 U.S. 125 (1939), as modifying the principle of the *Los Angeles* case. In fact, the *Rochester* case confirms that the Conference has no standing.

In its *Rochester* decision, the Court quoted the above passage from the *Los Angeles* case, and went on to say:

"Plainly the denial of judicial review in these cases does not derive from a regard for the special functions of administrative agencies. Judicial abstention here is merely an application of the traditional criteria for bringing judicial action into play. Partly these have been written in Article 3 of the Constitution, U.S.C.A., by what is implied from the grant of 'judicial power' to determine 'Cases' and 'Controversies,' Art. 3, Sec. 2, U.S. Constitution. Partly they are an aspect of the procedural philosophy pertaining to the federal courts whereby, ever since the first Judiciary Act, Congress has been loathe to authorize review of interim steps in a proceeding." [Footnotes omitted.] 307 U.S. at p. 131.

This is simply a re-affirmation of the principle that where, as here, "the order sought to be reviewed does not of it-

self adversely affect complainant but only affects his rights adversely on the contingency of future administration action," then "resort to the courts . . . is either premature or wholly beyond their province." 307 U.S. at p. 130.

In a further attempt to establish its standing, petitioner cites *United States v. Storer Broadcasting Co.*, 351 U.S. 192 (1956), and *Frozen Foods Express v. United States*, 351 U.S. 40 (1956). In the former, the Federal Communications Commission issued a "rulemaking order" which had the effect of placing a limit on the number of broadcasting stations in which the applicant, directly or indirectly, could have an interest. In the latter, the Interstate Commerce Commission issued an order that specified certain commodities as not being "agricultural" within the meaning of an exception of 203(b) of the Interstate Commerce Act.

In the *Storer* case, the Court found that:

"The regulations here under consideration presently aggrieve the respondent. . . . The Rules now operate to control the business affairs of Storer. . . . Commission hearings are now affected by the Rules. Storer cannot cogently plan its present or future operations." 351 U.S. at pp. 199-200.

In the *Frozen Food Express* case, the Court found that:

"[The Commission's determination] has an immediate and practical impact on carriers. . . . The 'order' of the Commission warns every carrier, who does not have authority from the Commission to transport these commodities that it does so at the risk of incurring criminal penalties. . . . [they] run civil and criminal risks. . . . [A carrier] may lose its rights to operate at all, if it does not respect the Commission's 'order'." 351 U.S. at p. 44.

It is clear that in these cases the orders under review established standards which immediately altered or affected the manner in which the regulated businesses were to be

conducted; and in the second of these cases, there was the additional fact that failure to comply with the standard could result in criminal and civil penalties. In contrast, the instant Report and Order of the Federal Maritime Board neither alters nor affects the Conference's business practices, and threatens no penalties. The carriers may conduct their business as they have been doing, with the rates which they have themselves established, entirely unaffected by the order.

All that the Conference is saying is that it is apprehensive that the Board has laid down "principles by which future regulation of the trade will be governed," with the result that the Board may have restricted the Conference's freedom in the future to make rates. The Conference is merely speculating that "all the carriers may at any moment find their existing rates unlawful because of improvements in Bull's operating efficiency or other factors, outside of their control, improving the profitability of Bull's operations." The simple fact, demonstrated by the Conference's own argument, is that it is asking for an advisory ruling that some of the statements made in the Board's Report are erroneous, because in the event of some future contingency, these statements may conceivably be applied so as to result in a future determination adverse to the petitioners.

The wholly conjectural argument of the Conference in the instant case is on all fours with that of the petitioner in *Montana-Dakota Utilities Co. v. Federal Power Commission*, 169 F. 2d 392, 402 (1948) (cert. den. 335 U.S. 853). There the Commission set up a formula designed to return to petitioner a fair and reasonable compensation for its services. In its suit for review, petitioner posed two hypothetical situations in which, so it argued, it would not in fact receive reasonable compensation. The Court said:

"Until an actual test of the rate schedule is made showing that it results in some unfairness, the Court cannot annul a prescribed rule for applying the rate to deliveries simply because petitioner can conceive a situation which considered in isolation might not return the amount hoped for." *supra*, at 402.

Similar reasoning was followed in *Sun Oil Company v. Federal Power Commission*, 256 F. 2d 233 (1958). There, Sun's rate schedule filings were rejected and its certificates of public convenience and necessity were cancelled, but no injury to Sun was shown nor was there any threat of injury. The Court stated:

"There is no need to anticipate an injury not presently threatened and not shown to be something likely to arise in the future." 256 F. 2d at p. 239.

The Conference has been unable to show that there is any injury likely to arise in the future under the conditions which presently exist and which presumably will continue to exist. The Conference can at best only assume that Bull's operating efficiency will increase or that other factors—not further described—may occur to the detriment of the remaining carriers in the Conference. Such speculative conjecture does not warrant the Court's setting aside the Board's order.

The Conference cannot at one and the same time both support the ultimate conclusion of the Board and attack the methods employed to arrive at that conclusion. The following language from *Lindheimer v. Illinois Bell Telephone Co.*, 292 U.S. 151 (1934), is dispositive of the instant case:

"The company was successful in the District Court and has no right to appeal from that decree in its favor. The company is not entitled to prosecute such an appeal for the purpose of procuring a review of the Court below with respect to the value of the company's property or other findings of which it complains." *supra*, at 176.

Even if the Conference were to prevail in the instant controversy, the rates would still stand as approved by the Board. This being the case, there is no purpose to be served by judicial inquiry. In *Interstate Natural Gas Co.*

v. *Federal Power Commission*, 156 F. 2d 949, 951 (1946) (affd. 331 U.S. 682), the Court stated:

“[T]he rate order must be viewed in its entirety, and ‘it is not the theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable judicial inquiry under the Act is at an end.’ ” (citations omitted) *supra*, at 951.

Here, the Conference admits that the total effect of the rate order is just and reasonable, for it has established the rate itself, and it supports the rate order against the challenge of the Commonwealth. It cannot now ask for further judicial inquiry.

II. The Board Did Not Err in Considering Bull as the “Rate-making Carrier.”

In certain prior rate investigations,⁸ the Board and its predecessors have followed the “ratemaking carrier” approach in analyzing the justness and reasonableness of the rates under inquiry. In so doing, the Board has, in effect, said that where there is a single, greatly predominant carrier in a domestic off-shore trade, whose operations comprehensively serve that trade, that carrier may be treated as the “ratemaking” carrier, and rates for the trade will be reviewed by the Board in the light of the rate base and profit and loss positions of that carrier.

In those cases, as in the instant case, this is a reasonable approach under the particular circumstances which the Board found to be prevailing in the trade. Bull is by far the largest carrier in the trade. For the first half of 1958 it carried 57 percent of the total tonnage carried by all carriers in the trade.⁹ Bull has three sailings per week

⁸ E.g., *General Increase in Hawaiian Rates*, 5 F.M.B. 347 (1957); *General Increases in Alaskan Rates*, 5 F.M.B. 486 (1958).

⁹ 558,880 tons for Bull; 169,363 tons for Alcoa; 132,202 tons for Waterman; and 107,822 tons for Lykes (J.A. 23) (Bd. Rep. 7).

from North Atlantic ports to Puerto Rico,¹⁰ utilizing six C-2 type vessels on a strictly maintained 14-day turnaround (J.A. 17) (Bd. Rep. 5). Moreover, Bull devotes its operations almost exclusively to the domestic trade. Of its three weekly sailings, two call at no other ports than those in the U. S. North Atlantic and in Puerto Rico. The third sailing calls at the Dominican Republic, but the amount of foreign cargo picked up and discharged is very small in proportion to the domestic cargo and the geographical deviation involved is trifling (J.A. 17). The Bull service, therefore, presents no very complex problem of revenue and expense allocation as between regulated and unregulated activity.

In contrast with the service of Bull, Alcoa and Lykes are preponderantly concerned with trades other than the Puerto Rican trade.

Lykes operates vessels worldwide as a subsidized carrier. Its so-called "Line A" service (one of five major services linking U. S. Gulf ports with every continent except Australia) sails once weekly to a broad area throughout the Caribbean, calling at Cuba, Haiti, the Dominican Republic, Puerto Rico, Venezuela, Colombia, and Panama, in addition to U. S. Gulf ports. Lykes makes no voyages to or from Puerto Rico exclusively (J.A. 20) (Bd. Rep. 8). The U.S.-Puerto Rican cargoes handled by Line A are far exceeded by the foreign cargoes handled.

Alcoa's Puerto Rican service consists of a weekly southbound voyage from North Atlantic ports to Puerto Rico, averaging 14.5 days in transit to Puerto Rico, as contrasted with 6 days for Bull (J.A. 17). After discharge at Puerto Rico, these vessels then proceed into foreign trades. Alcoa also has a weekly service from Gulf ports to Puerto Rico, averaging 12.5 days in transit to Puerto Rico (J.A. 17). Prior to March 1958, Alcoa had no northbound service in either its North Atlantic or Gulf trades, but in that month

¹⁰ Puerto Rico is roughly equidistant from New Orleans and New York. As the ratemaking carrier, Bull's service from the North Atlantic is also fairly representative of services from the Gulf.

it began to haul cargo homebound to the Gulf (but not the North Atlantic) from Puerto Rico. The record herein was made too soon after the commencement of Alcoa's homebound service to the Gulf to permit any firm impression of it to be drawn (J.A. 17) (Bd. Rep. 5).¹¹

Waterman, like Lykes, operates vessels in a number of wide-ranging trades, serving the Atlantic, Gulf, and Pacific ports of the United States and ports in Asia and Europe. It furnishes a weekly shuttle service between New Orleans and Puerto Rico, operating 2 C-2 vessels on a 14-day turnaround, and it calls at no foreign ports with these ships.

In short, Lykes serves Puerto Rico as an incident to its subsidized Line A service; and Alcoa serves Puerto Rico southbound primarily to place ships in position so that it can honor its northbound contractual commitments. Only Bull and Waterman operate what may be called a "pure" Puerto Rican service, and in contrast to Bull, Waterman carries a small proportion of the total traffic.

On these facts, the Board obviously was correct in concluding that Bull is the "rate-making line" in the trade.

The Conference, however, argues that the "rate-making carrier" doctrine deprives other carriers of their right to a fair return, thereby "depriving [them] of their property in violation of the Fourteenth Amendment." It advocates, as the only Constitutional approach, the use of "the composite results of the group or a representative sample of its members." Use of the composite results of the group (or their average, which is the same thing), or of a representative sample, would still result in rates too low for Alcoa and Lykes to earn a profit. This stems from peculiarities of their operation, not the Board's method of evaluating the overall rates. There is no way to assure every carrier a profit, unless the rates be set at a level which permits even the most inefficient carriers to earn a profit. Obviously,

¹¹ Alcoa has contract commitments which preempt its vessels after they have called at Puerto Rico on the southbound voyage from New York (J.A. 194).

such a rate level would destroy all incentive for efficiency and would be exorbitant in its effect on shippers.

There is no logic to the Conference's argument that the Board violates the carriers' Constitutional rights by using the "rate-making carrier" approach, but not by using composite results as a representative sample. As seen, whichever approach is used, the least efficient carrier or carriers will operate at a loss. There is nothing about the composite group or representative sample approach which makes it any more Constitutional than the "rate-making carrier" approach. Whatever approach the Board took, it would have to discount heavily the weight to be given to Lykes and Alcoa, whose Puerto Rican service is merely incidental to other predominating foreign operations, and whose operations even under the increased rates adopted by the Conference itself resulted in very substantial losses for the year 1958.¹² Their inclusion would materially distort the much more reliable picture to be gained from the operations of Bull and Waterman, which operate substantially "pure" Puerto Rican services unencumbered by far-ranging and heavy foreign carryings. These carriers operated at projected profits for 1958 of \$580,293 for Bull and \$1,394,145 for Waterman.

Even if the Conference's suggestion were adopted, and the composite group or a representative sample were used, Alcoa would have to be completely eliminated from the ratemaking picture because of its curiously atypical operations, which consume twice as many days in transit (with twice as much vessel operating expense) as the other carriers. It is even doubtful whether Lykes, with its very diffuse service, should be included in the composite or representative sample. But even including Lykes, the net result of a composite of Bull, Waterman, and Lykes would be more unfavorable to the Conference's position than using Bull alone. On the aggregate rate base for these three

¹² As projected on the basis of actual operations for the first six months of 1958, Alcoa would have suffered a loss of \$1,543,000 for the full year 1958; and Lykes on the same basis would have suffered a loss of \$398,497 (J.A. 48) (Bd. Rept., p. 36).

carriers as determined by the Board (J.A. 43) (Bd. Rep., p. 30), the aggregate net profit of the three (J.A. 47) (Bd. Rep., p. 36) would have resulted in a net rate of return of 7.7 percent before taxes, rather than the 5.0 percent rate of return calculated by the Board for 1958 using Bull alone.

There is therefore no merit to the Conference's contention that the composite results should have been used. The purpose of this contention is to bring into the picture the distortion that would result from giving any ratemaking weight to Alcoa's circuitous and unreasonably expensive and inefficient operations.

The Board did not violate the carriers' Constitutional rights by using Bull as the "ratemaking carrier." Deciding as it did, the Board actually reached a more favorable result for the carriers than if it had used the approach now advocated by the Conference.

III. The Board Properly Excluded From Rate Base the Terminal Properties Used, But Not Owned, By the Carriers.

The Board, upon consideration of the record, of the parties' arguments, and of previous Board decisions,¹³ concluded that the value of certain terminal facilities used but not owned by the carriers should not be included in the rate base. These were the terminals used by Bull at Philadelphia, Baltimore, and New York. The basis for the Board's conclusion lies in the fact that, insofar as such property is concerned, the carriers are not devoting their capital to the shipping public (J.A. 42).

The Board has maintained this consistent position (with the one exception mentioned in footnote ¹³) since enactment of the Shipping Act, 1916. In the very first rate investi-

¹³ Except on one occasion, the Board has uniformly held that used-but-not-owned property should be excluded from rate bases. As to the one instance in which the Board departed from the rule (*General Increases in Alaska Rates and Charges*, 5 F.M.B. 486), the Board stated in its instant decision that "we were in error in including the value of non-owned assets in the carrier's rate base." (J.A. 41).

gation under the Act, *Alaskan Rate Investigation*, 1 U.S.S.B. 1 (1919),¹⁴ the predecessors of the present Board stated:

“The reasonableness of the rates depends largely upon whether they yield a fair return upon the value of the *carrier's property* devoted to the public service.” (emphasis added.) (1.U.S.S.B. at p. 4.)

In the decision under review, the Board found that to depart from this principle and “to include the value of this non-owned property in the rate bases in our opinion would grant the carriers a windfall at the expense of the shipping public.” (J.A. 42)

The Conference assails the Board decision in this respect. It would have the Board include in the rate base the value of all terminals used by Bull, regardless of whether Bull owned, leased or was allowed to use the property free of charge. The Conference bases its position on its assertion that “the public benefits from the use of the property, and must therefore pay rates allowing a return thereon. . . .”

To support this position, the Conference cites various agency and court decisions arising out of section 19a of the Interstate Commerce Act (49 U.S.C. section 19a). That section requires the Interstate Commerce Commission to make a detailed physical valuation, classification, and inventory of all of the property of rail carriers under its regulation. There is nothing comparable to this in the Shipping Act.

But even the cases arising under Section 19a of the Interstate Commerce Act, including those cited by the Conference, run counter to, rather than in support of the Conference position. The Conference admits that “Bull leases the Philadelphia and Baltimore terminals from the municipal Port Authorities at favorable rentals (*i.e.*, below owner's costs), as a promotional device on their part to

¹⁴Petitioners in their brief (see Conference Brief, page 27) make the unsupported assertion that the Board included an item of non-owned property in the rate base in the *Alaska Rate* case of 1919. There is nothing in the text of the opinion to justify such an assertion.

increase the traffic using their services." (Conference Brief, page 26.)¹⁵ In dealing with the same type of situation, the ICC in *New York Central Railroad Company, et al.*, 27 Val. Rep. 1, 57 (1929), stated:

"In our view these properties must be regarded as held for development in the general public interest and not that of corporations organized for profit."

The Supreme Court in *Manufacturers Ry. Co. v. United States*, 246 U.S. 457, 496 (1918) has followed the same principle:

"If the stipulated rental is less than the fair annual value of the property, it is to be presumed that the grant of the excess was to the public, not to the private interest of the Railway."

The short answer to the Conference's contention is that in dealing with the ratemaking questions arising out of the lease of terminal properties from municipal authorities, the ICC considers that insofar as such property is municipally owned it is part of the public domain, and that:

"where the carrier makes no capital outlay in its acquisition, nothing should be included in the valuation for public property of this kind, but that the *rentals should be charged to operating expenses.*" (Emphasis supplied.) *Baltimore, Chesapeake & Atlantic Railway Company*, 31 Val. Rep. 505, 512. (1930).

The same reasoning is applicable to the Baltimore terminal. It is already devoted to public use by the railroad which owns it and is being compensated for it in the rail rate structure. Bull has no right to gain a windfall by including

¹⁵ According to the evidence of the record, only the Philadelphia terminal is municipally owned (J.A. 114). The Baltimore terminal is actually owned by the Baltimore and Ohio Railroad in whose rate base it is already included (J.A. 196). The railroad permits Bull to use the terminal free of charge for the purpose of attracting additional railroad cargo over its line.

it in its rate base, and thus to cause the public to pay twice for the same asset.

Thus, so far as Bull's Philadelphia and Baltimore terminals are concerned, the Board dealt with them in the same manner as the ICC would have: the rental expense, if any, was required to be treated as operating expense and the value of these terminals was excluded from the rate base.

Bull's New York terminal is used by Bull under an arm's length, commercial lease. The Conference argues that the Board should include the value of this terminal in the rate base, although it concedes that the Board has the discretion to do what it did, that is to include the rental as an operating expense, and to exclude the terminal value from the rate base.¹⁶ In the ascertainment of value of property used for the convenience of the public, the Board is not controlled by an artificial formula, "but there must be a reasonable judgment, having its basis in a proper consideration of all relevant facts." *Minnesota Rate Cases*, 230 U.S. 352, 434 (1913).

The Board exercised a "reasonable judgment" in excluding the New York terminal from Bull's rate base. In so doing, the Board treated all of Bull's terminals consistently: it excluded all used-but-not-owned terminals from the rate base, but permitted Bull to include as operating expenses the rental for such terminals. By satisfying itself that the rentals were reasonable, the Board protected the rate-payers against any exorbitant expense that might result from an improvident lease. And the method followed by the Board had the advantage of uniformity and certainty. The Board summarized the conflicting positions of the carriers and the highly uncertain valuations claimed by them, and said:

"As indicated above, such [used-but-not-owned] assets were claimed by some of the carriers and not by others, were excluded by the examiner in the case of Water-

¹⁶ *Interstate Commerce Commission v. New York, N.H. & H.R. Co.*, 287 U.S. 178, 198 (1932), fn. 6.

man, and Bull apparently did not claim all of such property. Thus we are asked to arrive at rate bases of various carriers containing different elements depending in some cases on the claims of the carrier and in others on the evidence submitted by it as to the value of the [terminal] property. *This we will not do.* Proceedings such as this are difficult enough without adding to the problems." (Emphasis supplied.) (J.A. 42)

The Conference cannot show that the Board has acted arbitrarily in choosing to include terminal rentals as an operating expense rather than to include their values in the rate base. The Board's treatment of the problem is on all fours with that of the ICC in *New York, N.H. & H.R. Co.*, 30 Val. Rep. 1, 36, (1929), aff'd 287 U.S. 178 (1932). There, the Commission considered the valuation for ratemaking purposes of the Grand Central Terminal in New York which the railroad was permitted to use, jointly with other carriers, under a lease or contract arrangement. The situation was thus similar to the situation before the Board. The Commission said:

"The carrier does not own an interest that would cause it to suffer a loss by deflation or to profit by the the enchancement of value which might take from or add to the intrinsic worth of the property."

The Commission, although acknowledging that such a use of the terminal is a "commercially valuable contract," concluded that for rate-making purposes, no portion of the Terminal's asset value should be included in the carrier's rate base.

The Board, in short, did not err in excluding used-but-not-owned terminal property from Bull's rate base.

IV. The Board's Allowance for Working Capital Is Fair and Reasonable and Consistent With the Facts and Evidence.

The Board considered three alternative methods of computing working capital:

1. To use an amount equal to one twelfth of the year's operating expenses, which would be approximately \$1,800,000 for Bull, using actual operating expenses for 1957. This was the method suggested by the hearing examiner.

2. The use the figure arrived at by the hearing examiner plus an additional \$1,000,000 allowance said to be necessary to cover the time lag involved in collecting receivables. This method was urged by the Conference, and would call for a working capital of \$2,800,000.

3. To calculate the amount by applying the formula set out in the Board's General Order 31, Limitations 3 and 4, 46 C.F.R. sec. 286.3(2)(1). This formula establishes the procedure for calculating adjusted working capital as an element of "capital necessarily employed" by subsidized operators in the foreign trade.¹⁷ This method was advocated by Public Counsel and interveners. In essence, this method fixes working capital at an amount equal to the expense of one round voyage for each vessel employed in the service. Bull, which operates 6 C-2s in the Puerto Rico service was thus allowed a sum equal to six times the voyage expense of a typical C-2 round voyage in the regulated trade. As applied to Bull, the formula resulted in a working capital allowance of \$1,087,000.

The Board had found in two prior rate investigations that the General Order 31 formula allowed a fair and reasonable valuation of working capital for rate-base pur-

¹⁷ Under the subsidy program enacted in the Merchant Marine Act, 1936, a carrier operating under a subsidy contract may distribute or withdraw as profit a sum "not in excess of 10 per centum per annum on the contractor's capital necessarily employed in his business. . . ." 46 U.S.C. Section 1177(a). Profits exceeding 10 per cent of capital necessarily employed are subject to partial recapture by the Government. Among other components, capital necessarily employed includes a working capital allowance as spelled out in the Board's General Order 31.

poses. *General Increase in Hawaiian Rates*, 5 F.M.B. 347, 350 (1957), and *General Increases in Alaskan Rates and Charges*, 5 F.M.B. 486, 500 (1958). In the latter case, the Board reviewed method (2) above, which had earlier been followed in *Alaskan Rates*, 2 U.S.M.C. 639, 644-6 (1942), and rejected that method as unsound and excessive. It is this rejected method which the Conference would reinstitute.

The amount of working capital allowed by the Board is, as seen, equal to the expense of one complete round voyage for each of the ships in the service. This sum is clearly sufficient to meet all working capital needs of the carriers. While some, but not all,¹⁸ of the voyage expenses are laid out by the carrier in advance, it is normal practice for the carrier to receive its freight payment either upon receipt of the cargo, or upon delivery thereof. Thus, the termination of the round voyage normally marks the point when the revenues for such voyage are in the carrier's hands. In fact, the Conference tariff specifies that freight must be prepaid (J.A. 157-8). Thus, to the extent the carriers live up to their own tariff, their freight revenues are actually in hand when the cargo is placed aboard the vessel. There is consequently no very substantial lag between payment of expenses and receipt of revenues. To the extent that there is any such lag, the working capital allowed by the Board—equal to the round voyage expense for each ship in the service—is ample to take care of the carrier's interim needs.

Working capital is required to meet the need which "arises largely from the time lag between payment by the Company of its expenses and receipt by the Company of payment for service in respect of which the expenses were incurred." *Alabama-Tennessee Nat. Gas Co. v. Federal Power Commission*, 203 F. 2d 494 (1953), cited in *General Increases in Alaskan Rates and Charges*, 5 F.M.B. 486, 500 (1958). The allowance of any additional amount would

¹⁸ It was conceded by the carrier's witnesses that some of the voyage expenses were not paid out in advance in cash, but were rather accrued as accounts payable, and thus did not represent any actual cash requirement (J.A. 157).

unnecessarily inflate the rate base to the detriment of the shipping public.

In support of its demand for a larger working capital, the Conference asserts that there is an additional need for a "fund for uncontrollable contingencies." They suggest that this fund be set at approximately \$2,000,000, representing 30 days' operating expenses. The only example of such an "uncontrollable contingency" given by the Conference is a strike. The conference apparently has overlooked the fact that where a strike causes a discontinuance of vessel operations, there would be a corresponding decrease, if not a cessation, of vessel operating expenses during the strike. In the event of such a contingency, the working capital allowed by the Board would still appear to be adequate to cover all foreseeable financial needs during such a contingency.

The Conference also criticizes the Board's working capital calculation on the ground that it is based on a formula applicable to subsidized carriers in the foreign trade, but the Conference is unable to show why this is necessarily bad. The fact is that Limitation 4 of General Order 31 sets up a clear and precise formula by which working capital can be computed; and it is a formula, moreover, which is entirely fair and reasonable and readily adaptable to the needs of carriers in the regulated domestic trades. The Board's working capital allowance should be found to be lawful.

V. The Board Correctly Ascribed To Carrier-Owned Terminals a Rate Base Valuation of Net Book Value.

As to terminals owned by the carriers, the Board allowed net book value for the rate base valuation. In the case of Bull, the ratemaking line, it owns the terminals which it uses in Puerto Rico. These terminals had a net book value of \$2,144,572 as of December 31, 1957. The Conference sponsored a witness who testified that Bull's Puerto Rican terminals should be valued at \$4,062,194, this being the value at which the terminals were appraised by the independent appraisers hired by the purchasers of Bull (J.A. 203). In arriving at this appraisal, the following

factors were considered: present and future earnings, degree of obsolescence and adequacy or inadequacy, original cost, reproduction cost, previous appraisals, etc. (J.A. 130-1). The appraisers then concluded that a willing buyer would pay a willing seller the price of \$4,062,194 for the properties; but there was no actual sale or market transaction against which this opinion could be checked (J.A. 131).

The Conference argues that the Board should have applied to the terminals the appraisal value of \$4 million instead of the net book value of about \$2 million. The sole ground advanced by the Conference for this argument is that, having valued the ships at their market value, the Board should also have valued terminals at their market value.

The Conference's argument is based on an erroneous premise. The record contained no market value for terminals comparable to the market value for ships. Ship market values are easily and objectively determined, on the bases both of sales prices on ships actually sold and of bidding and asking prices which are constantly being exchanged through ship brokers. The activity of the ship market reported currently in trade publications makes it possible for anyone conversant with this market to arrive at a fairly precise and objective judgment of the current market value for a particular type of ship at any given time.

In contrast, a judgment of the "market value" of terminals is entirely subjective, for there is no such thing as a market or frequent exchange of terminals. This is borne out by the testimony of the Conference's own appraiser, who admitted that such subjective factors as reproduction cost and future earnings entered into appraisal.

In view of these facts, the Board's decision to use net book value for terminals, far from being inconsistent with its ship valuation, is entirely reasonable. In the first place, the record contained no evidence of a terminal "market value," for there is no such "market value," in the sense that that term is applied to ships. Thus, although the Conference charges the Board with inconsistency in using book value for terminals while using market value

for ships, the Conference is equally inconsistent in urging that the Board should use appraisal value for terminals and market value for ships. The appraisal value is no more equivalent to market value than is net book value.

The Board was correct for the further reason that the considerations which led the Board to reject net book value for ships are absent in the case of terminals. Unlike ships, terminals are not mobile or readily saleable, and there is not the danger, present in the case of ships, that a restriction to net book value for rate purposes will induce the owner to withdraw the terminals from the regulated trade. This is especially true in the case of Puerto Rican terminals, whose usefulness is practically confined to the regulated domestic trade with the United States mainland, Puerto Rico having only a limited volume of trade with foreign countries.

In sum, the Board was correct, and was not inconsistent, in rejecting the highly uncertain and subjective appraisal value for terminals and adopting net book value instead.

VI. The Board Correctly Refused to Follow the Operating Ratio Approach.

The Board in the present case adhered to its regular practice of using the fair-return-on-rate-base approach in judging rates in the domestic offshore trades. *Alaska Rate Investigation*, 1 U.S.S.B. 1, 4 (1919), *Rates of Inter-Island Steam Navigation Co., Ltd.*, 2 U.S.M.C. 253 (1940); *Alaska Rates*, 2 U.S.M.C. 558 (1941); *General Increase in Hawaiian Rates*, 5 F.M.B. 347, 354 (1957); *General Increases in Alaskan Rates*, 5 F.M.B. 486, 495 (1958). The Board and its predecessors have invariably followed this approach, and have rejected the contention, advanced in previous rate investigations, that the operating ratio approach should be adopted. In *General Increases in Alaskan Rates*, 5 F.M.B. at p. 495, the Board stated:

“We agree with the examiner that the operating ratio theory has never been followed by the Board or its predecessors and should have no controlling weight

in this proceeding. Operating ratio has been used in motor carrier rate cases by the Interstate Commerce Commission, where the ratio of operating revenues (and expenses) to investment in capital equipment is relatively large; i.e., four or five to one or better. In contrast, Alaska Steam's ratio of revenue (or expenses) to capital investment is only slightly in excess of two to one. We see no reason to depart from the fair-return-on-fair-value standard which the Board and its predecessors have used."

To justify the requested departure from precedent, the Conference relies heavily upon cases involving motor carriers. Such cases have only a doubtful relevance to the instant case. Motor carrier equipment depreciates very rapidly in contrast to the far slower depreciation characteristic of ships. Trucks have a service life of the order of 5 years; the service life of ships is four times as long. It is commonplace for regulated motor carriers to operate hundreds of pieces of rapidly-depreciating rolling stock, thus making the rate base approach cumbersome. In contrast, Bull, the largest carrier in the Puerto Rican trade, operates only six ships.

In the instant case, the ratio of annual operating expense to investment is approximately two to one. In motor carrier cases, this ratio is much larger. In *Middle West General Increases*, 48 M.C.C. 541, 552 (1948), the Interstate Commerce Commission found that this ratio was 3.78 to 1 for 98 Class I motor carriers. However, even dealing with motor carriers, the Commission has recognized that rate of return on investment is "useful in an appraisal of the financial condition and progress of the motor carrier industry." 48 M.C.C. at p. 553.

In arguing that the Board should abandon the fair-return-on-fair-value principle, the conference is asking the agency to discard over forty years of well-settled practice. Commenting on the adoption of a method other than the traditionally used rate-base method to determine the lawfulness of natural gas rates, this Court in *City of Detroit, Michigan*

v. *Federal Power Commission*, 97 App. D.C. 260, 230 F. 2d 810, 818-9 (1955), stated:

“[The rate-base method] has been repeatedly used by the Commission, and repeatedly approved by the Courts, as a means of arriving at lawful—‘just and reasonable’—rates under the Act. Unless it is continued to be used at least as a point of departure, the whole experience under the Act is discarded and no anchor, as it were, is available by which to hold the terms ‘just and reasonable’ to some recognizable meaning.”

Similar considerations apply in the instant case.

Moreover, since the Board found the rates to be just and reasonable on the theory which it did follow, the Conference can scarcely claim that it is prejudiced because the Board did not go through the process of also using the operating ratio to reach the same conclusion. As the hearing examiner stated:

“Since in any event the use of the operating-ratio theory would have no effect on the ultimate conclusions here arrived at by the use of standards heretofore approved by the Board, no further consideration need be given to the contentions relating thereto.” (J.A. 104).

All that the Conference really seeks is for the Board to do a superfluous act. This request is without merit.

CONCLUSION

Although assailed from either extreme, the Board was correct in its decision that the rate increases under investigation are just and reasonable. For its part, the Commonwealth contends, without merit, that the carriers should be held to limitations on vessel valuation, rate of return, and depreciation expense which would unreasonably deprive the carriers of revenues to which they are entitled, and which would tend to discourage the investment of additional capital in the domestic off-shore trades, if not to

cause either the curtailment or abandonment of service. And for its part, the Conference, although it is in no way prejudiced or adversely affected by the Board's decision, seeks to impose on the Board such a change in its rate-making principles as would result in the end in a most exorbitant rate structure, intolerable and expensive to the taxpayers.

Both petitions are without merit. The Board's decision strikes the proper balance between the interests of the carriers and of the ratepayers. The decision should therefore be affirmed.

Respectfully submitted,

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ROBERT E. MITCHELL
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DONALD J. BRUNNER
Attorney
Attorneys for Respondent
Federal Maritime Board

Washington 25, D. C.

November 7, 1960

STATEMENT OF THE UNITED STATES

The United States does not believe that the issue of the appropriate rate base can be resolved on the basis of the present record. On this basic issue, the Board did not pass on the argument of the Commonwealth, but held simply:

“We find that the value of the vessels on the domestic market at or about the time the rate increase is requested with adjustments to eliminate short term peaks in vessel values, is the proper method for determining the reasonable value of the property being used for the public” (Par. 52).

This conclusion of the Board may come within the wide discretion the Board has in this area, in view of the peculiar limitations on its regulatory authority over the shipping industry. See *Federal Power Commission v. Hope Natural Gas Co.*, 320 U. S. 591. But it is impossible, on this bare assertion, to “know what [its] decision means . . .” (*Secretary of Agriculture v. The United States*, 347 U.S. 645, 654), and judicial review of it must await, the United States believes, a detailed explanation by the Board based upon the record in this case or other relevant considerations within the Board’s expertise. Cf., *Pacific Far East Lines v. Federal Maritime Board*, 107 U.S. App. D.C. 155, 275 F. 2d 184, 187; cert. den. 363 U.S. 827. The United States further believes that the Board, on such a remand, should pass on the Commonwealth’s argument that it is unfair to the ratepayers to permit the depletion of the old depreciation reserve built up over the years and removed to finance the purchase.

Respectfully submitted,

ROBERT A. BICKS,

Assistant Attorney General

RICHARD A. SOLOMON,

HENRY GELLER,

Attorneys, Department of Justice

Washington 25, D. C.

November 7, 1960

*Item 14—Decision*UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF
COLUMBIA CIRCUIT

No. 15846

THE COMMONWEALTH OF PUERTO RICO, PETITIONER, v. FEDERAL MARITIME BOARD
AND UNITED STATES OF AMERICA, RESPONDENTSUNITED STATES ATLANTIC & GULF-PUERTO RICO CONFERENCE, ET AL., WATERMAN
STEAMSHIP CORPORATION AND WATERMAN STEAMSHIP CORPORATION OF PUERTO
RICO, INTERVENORS

No. 15847

UNITED STATES ATLANTIC & GULF-PUERTO RICO CONFERENCE, ET AL., PETITIONERS,
v. FEDERAL MARITIME BOARD AND UNITED STATES OF AMERICA, RESPONDENTS

THE COMMONWEALTH OF PUERTO RICO, INTERVENOR

ON PETITIONS FOR REVIEW OF AN ORDER OF THE FEDERAL MARITIME BOARD

Decided February 23, 1961

Mr. William D. Rogers for petitioner in No. 15846. Mr. George Bunn also entered
an appearance for petitioner in No. 15846.Mr. Mark P. Schlefer, with whom Mr. T. S. L. Perlman was on the brief, for
petitioner in No. 15847.Mr. Edward Aptaker, Assistant General Counsel, Federal Maritime Board, with
whom Messrs. James L. Pimper, General Counsel, and Robert E. Mitchell, Assistant
General Counsel, were on the brief, for respondent Federal Maritime Board.Mr. Henry Geller, Attorney, Department of Justice, with whom Mr. Richard
A. Solomon, Attorney, Department of Justice, was on a statement filed in behalf
of respondent United States of America.Messrs. Warren Price, Jr., and Sterling F. Stoudenmire, Jr., were on the brief
for intervenors Waterman Steamship Corporation and Waterman Steamship
Corporation of Puerto Rico in No. 15846.Before EDGERTON, PRETTYMAN, and BASTIAN, *Circuit Judges*.PER CURIAM: We are asked to review a Federal Maritime Board ruling of
April 28, 1960, that certain large rate increases for carriage of cargo between
Puerto Rico and ports on the Atlantic and Gulf coasts of the United States are
just and reasonable.¹In a report which accompanied its order the Board said: "We find that value
of the vessels on the domestic market at or about the time the rate increase is
requested with adjustments to eliminate short term peaks in vessel values, is
the proper method for determining the reasonable value of the property being
used for the public." The Board did not say why it adopted market value as a
rate base or why it rejected Puerto Rico's contention that this base is grossly
excessive and rates should be based on prudent investment less depreciation.The Department of Justice urges on behalf of the United States that the rate
base question cannot be resolved on the present record. We agree. The Ad-
ministrative Procedure Act requires all decisions to state not only findings and
conclusions but also "the reasons or basis therefor, upon all the material issues
of fact, law or discretion presented on the record * * *" § 8(b), 5 U.S.C. § 1007(b).
The Board "should make the basis of its action reasonably clear. We cannot
find that it did so here." *Radio Station KFH Co. v. Federal Communication
Commission*, 101 U.S. App. D.C. 164, 166, 247 F. 2d 570, 572; *Pacific Far East
Line, Inc. v. Federal Maritime Board*, 107 U.S. App. D.C. 155, 275 F. 2d 184. *Cf.*
Secretary of Agriculture v. United States, 347 U.S. 645, 654.The Board's order is therefore vacated and the same remanded for the Board
to reconsider and clarify the rate base question. The Board should also pass
upon the Commonwealth's argument that it is not fair to rate payers to let an
accumulated depreciation reserve be depleted and depreciation charges thereby
increased.¹ The Board acted under § 18 of the Shipping Act, 1916, c. 451, 39 Stat. 735, as amended,
46 U.S.C. §§ 801, 817, and § 3 of the Interoceanic Shipping Act, 1933, c. 199, 47 Stat. 1426,
as amended, 46 U.S.C. §§ 843, 845. This proceeding for review is brought under the
Judicial Review Act of 1950, c. 1189, 64 Stat. 1129, as amended, 5 U.S.C. § 1031 *et seq.*

The motion to dismiss Puerto Rico's petition for review in No. 15846 is denied. Puerto Rico's motion to dismiss the petition for review in No. 15847 is granted. *Vacated and remanded.*

Item 15—Page 78

How much investigation is made and how is evidence weighted by the Federal Maritime Board in making a determination on a requested rate increase?

Protests by affected local shippers and Government bodies against offshore domestic rate increases are always given attentive consideration. In formal cases involving offshore domestic rates, State and other local government bodies are welcome to intervene, and the practice has been, in general, that they have intervened and presented evidence as to the impact of the proposed rate change on the local economy.

The Board has long been aware that steamship service is a factor in the economy of the domestic offshore areas. Recently, in its decision in docket No. 807, *United States Atlantic and Gulf-Puerto Rico Conference Increases in Rates* (mult. op. decided April 28, 1960, pp. 9-10), the Board made special findings as to the effect of increased steamship rates on the economy and living standards of Puerto Rico.

The needs of the economy of the domestic offshore areas for lower freight rates must be weighed against the constitutional right of the carriers to rates that will not deprive them of a minimum fair return on their investment. The Board must also balance against the need for low freight rates the need for continuing steamship service, and therefore must allow a rate structure which will not drive carriers out of the trade. Accordingly, the Board allows what it considers a fair return on investment, endeavoring to hold these down to their lowest reasonable values. In recent cases, it has determined such fair return to be not more than 7½ percent of the market value of the owned property the carrier actually devotes to the trade plus working capital.

Item 16—Page 79

What, if any, evidence is there that high domestic freight rates may be conducive to imports into offshore domestic areas via foreign-flag vessels from foreign ports? Specific reference is made to steel cargoes and other construction materials being imported into Alaska aboard Japanese ships.

The Trans-Pacific Freight Conference of Japan which covers traffic moving from Japan to Alaska quotes open rates on iron and steel angles, bars, channels, plates, rods, rails, sheets, etc., subject to a minimum per 2,240 pounds or 40 cubic feet of \$14 to Anchorage and \$18.20 to other ports.

The rates of Alaska Steamship Company for moving such property from Seattle or Tacoma to Seward or Valdez (Anchorage is not served direct) is \$46.57 per 2,240 pounds (quoted as \$1.89 per 100 pounds plus 10 percent).

An examination of records of the Census Bureau reveals that in 1959 the only movement of metal from Japan to Alaska was classified as metal manufactures and parts, 311 short tons moving to Sitka. The Corps of Engineers report for 1959 indicates 12,822 short tons of metal manufactures and parts and 6,259 short tons of steel mill products moved to Alaska from the Pacific Northwest. Thus it appears that less than 2 percent of such materials moving into Alaska in 1959 originated in Japan. Reports of the domestic movement in 1960 are not available; Census records indicate that during January through October 1960, the movement of this type commodity totaled 1,872 short tons of which 1,403 short tons were iron and steel pipe and tube. The port of discharge is not indicated on the reports. Because of this small volume of the movement of steel from Japan to Alaska, it cannot be concluded that any differences in freight rates has had a significant impact on the source from which the cargoes were obtained.

DOMESTIC OFFSHORE SHIPPING

TUESDAY, MARCH 7, 1961

U.S. SENATE,
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
SUBCOMMITTEE ON MERCHANT MARINE AND FISHERIES,
Washington, D.C.

The subcommittee was called to order, pursuant to adjournment, at 10:16 a.m., in room 5110, New Senate Office Building, Hon. E. L. Bartlett presiding.

Senator BARTLETT. The committee will be in order.

It is the committee's very special privilege this morning to hear as the first witness Dr. Fernós-Isern, Resident Commissioner from Puerto Rico, a factual as well as eloquent witness on all matters having to do with the great commonwealth.

Dr. Fernós, we welcome you.

STATEMENT OF DR. A. FERNÓS-ISERN, RESIDENT COMMISSIONER OF PUERTO RICO

Dr. FERNÓS. May I proceed?

Senator BARTLETT. Yes; surely, Mr. Commissioner.

Dr. FERNÓS. Mr. Chairman, I appreciate the opportunity to appear before your committee briefly to present some pertinent facts concerning maritime transportation between Puerto Rico and continental United States.

I understand that later in the hearing—in fact today—the committee will hear a representative of the Puerto Rico Economic Development Administration, who will present the views of the Governor of Puerto Rico, the Honorable Luis Muñoz Marín, and will go into the matter in more detail.

The Foraker Act of 1900, the first Organic Act approved by Congress for Puerto Rico, provided in section 9 of that act, that—

the coasting trade between Puerto Rico and the United States shall be regulated in accordance with the provisions of law applicable to such trade between any two great coastal districts of the United States.

This provision was continued by the Organic Act of 1917, known as the Jones Act, by virtue of its section 58 which provided "that all laws or parts of laws applicable to Puerto Rico not in conflict with any of the provisions of this act, are hereby continued in effect."

This section 58 of the Organic Act of 1917 was, in turn, continued as part of the Puerto Rican Federal Relations Act, referred to by section 3 of Public Law 600, 81st Congress. It was within the framework of Public Law 600, 81st Congress that the Commonwealth of Puerto Rico was created by the people of Puerto Rico and proclaimed

on July 25, 1952. Thus, the provisions of section 9 of the act of 1900 concerning intercoastal shipping remain in effect today.

Under the Merchant Marine Act of 1936, both the operating and construction cost differential subsidies are limited to foreign trade.

It is generally agreed that the operation of U.S.-flag vessels is substantially more costly than the operation of ships under foreign flags. Consequently, tariff rates for American vessels operating in foreign trade would have to be substantially higher than that of foreign vessels, were it not for the differential cost Federal subsidy paid to U.S. vessels engaged in foreign trade. That is to say, the subsidy permits American-flag vessels to meet foreign vessels in freight rate competition; otherwise they would not be able to compete.

There is no competition with foreign vessels in coastwise shipping. Neither is there a subsidy. Freight rates are supposed to be geared to the total cost of construction and operation. In other words, while the cost of maintaining the U.S. merchant marine in foreign trade is paid partly by its American users and partly through general taxation, the cost in coastwise shipping is borne exclusively by its users.

The impact of this situation on offshore domestic areas is not the same as it pertains to continental U.S. users of coastwise shipping for obvious geographical and logistic reasons. In the mainland trade, there is no competition between U.S. vessels and foreign trade registry vessels, but there is competition between U.S. vessels and overland transportation; namely, railroads and truck lines. That is to say, users have a choice between coastal transportation and overland transportation. This has resulted in the reduction to minimal proportions of the actual coastwise trade between ports in the mainland. But in what pertains to offshore areas, it is obvious that there is no such alternative. All transportation must be by sea, regardless of freight rates.

This situation should be approached with full appreciation of its practical impact on the offshore areas. These areas are insular, or noncontiguous peninsular. Either an ocean or a foreign country separates them from the mainland. Ocean transportation is their lifeline. At the same time, since they are included within the U.S. tariff system and are a part of the U.S. common market, most of their outside trade is with the United States proper. They depend on U.S. shipping for this trade. It is obvious that they should carry a proper share of the burden of maintaining and protecting the American merchant marine. But for the reasons above stated, the burden these areas carry is proportionately much greater than the burden carried by the mainland.

Because of ocean transportation costs, the economic development of these areas is affected. It evidently must add to the cost of living. The cost of living in Alaska has been found to be 25 percent higher than Washington, D.C.; the cost of living in Hawaii has been found to be 17.5 percent higher than Washington; and the cost of living in Puerto Rico has been found to be 12.5 percent higher than Washington. Let me point out that this represents considerable expense to the Federal Government, because a cost-of-living differential payment is made to Federal employees in these areas. These Federal employees are compensated to the degree that their living costs are higher than in Washington, D.C.

On the other hand, transportation costs are reflected in production wages paid in Puerto Rico. Most of the material for Puerto Rico industrial plants is shipped from continental United States to Puerto Rico, and manufactured products must then be carried back from Puerto Rico to the mainland. In order to meet competition and offset transportation costs, wages must be lower than in the mainland. It has not been possible to apply the minimum wage law in Puerto Rico on the same basis as in continental United States. The combination of a lower wage and a higher cost of living results in a lower level of existence.

Where an adjustment in wages to compensate for costs of transportation is not feasible, industrialization is handicapped.

Domestic trade consists in fact not of one, but of two categories: Domestic coastwise trade and domestic noncontiguous trade. They cannot be treated identically because their situation and circumstances are different.

It is in the national interest and it is fair that the offshore areas should have the same opportunity for development and well-being as the continental areas insofar as this is possible. Nature has placed them in an unfavorable position because of distance and geographical isolation; manmade laws should not add to their natural limitations. Although they should carry a proportionate share in support of the U.S. merchant marine, they should not be called upon to assume a disproportionate share, lest their growth and development be stunted and their welfare impaired.

I shall conclude with a comment with regard to a special situation which concerns Puerto Rico. The present service given by the various shipping lines is freight service, with some limited and unsatisfactory passenger service on these ships, a maximum of 12 passengers per ship. The tourist trade is one of the developing trades in the Caribbean, but other than by freighters there is no passenger shipping service between Puerto Rico and the United States, either regular or tourist. Tourists can reach Puerto Rico only by air or by freighter, except for those who occasionally may visit Puerto Rico on cruise ships. Whoever lives in Puerto Rico can only get out of the island either by airplane or on freighters. The effect of this situation was dramatized by the recent strike against the airlines. All the rest of the Caribbean has tourist and regular shipping service.

Various suggestions might be made in this respect. First, subsidized regular American lines with passenger service and plying between the United States and countries neighboring Puerto Rico, now bypassing Puerto Rico, might be allowed to make San Juan a port of call without loss of subsidy. Second, American tourist ships cruising the Caribbean with subsidy might be allowed to carry passengers from the mainland to Puerto Rico and from Puerto Rico to the mainland without loss of subsidy. Third, foreign-flag ships might be allowed to carry passengers between Puerto Rico and the United States.

Thus, Puerto Rico might have regular passenger service plus some additional service, especially during the tourist season.

I thank this committee for the time it has given me.

Senator BARTLET. Thank you, Commissioner Fernós, for a very well reasoned statement.

You made a suggestion here, inferentially at least, which had not yet come to the attention of the committee, and that is that if an arrangement could be made here to accommodate the situation which you describe and which is the genesis of the problem before the committee, it could result in a saving to the Federal Government, because if transportation costs are lowered, the cost of living in these areas might be lowered and the Federal Government would thereby be able to lessen or eliminate the cost of living allowance to Federal employees.

Dr. FERNÓS. And the Federal employees would not suffer by that because their differential payment is geared to the high cost of living. If the cost of living is so much higher than Washington, that is what they get, that percentage. So they always would get a differential if, in spite of better transportation or less expensive transportation they would have a higher cost of living there anyhow. But the chances are that the cost of living would be reduced and therefore the differential would be correspondingly reduced if geared to the cost of living.

Senator BARTLETT. I think that is a very important consideration for the committee, because it could serve as a large offset to whatever additional costs might be accumulated by reason of any payment made to these carriers.

How long is it, Dr. Fernós, if you recall, since you have had regular passenger service to Puerto Rico?

Dr. FERNÓS. We had no passenger service, of course, during the war. We had had up to the Second World War, but after the war there was an attempt on the part of the Bull Insular Line to run a passenger-service boat. I remember the name was the *Puerto Rico*. But I think it is over 10 years now that we haven't had any, because they discontinued the service.

Senator BARTLETT. Of course, the service provided by the freighters—12 passengers each as a maximum—is inconsequential as far as carrying any number of people to the islands?

Dr. FERNÓS. Very small; and also, although I have traveled in them and I can say that the staterooms are pretty comfortable, there are no recreational or other amenities of sea travel, and, naturally, because they are freighters.

Senator BARTLETT. How many days does that trip take from San Juan to New York by freighter?

Dr. FERNÓS. About 3½ days.

Senator BARTLETT. Mr. Goding?

Mr. GODING. I have one question.

You mentioned here among possible suggestions on the passenger service, the possibility of allowing American tourist ships cruising the Caribbean with subsidies to be allowed to carry passengers—presumably without loss in subsidy. Is that now possible? I didn't know that we subsidized the cruise vessels.

Dr. FERNÓS. If a cruising ship is boarded by somebody in New York and that ship is to make San Juan a port of call, of course, the passengers may land, but they are supposed to go back to the boat and continue with their cruise. I don't know if anyone just wanted to stay in San Juan and then come back by air or some other way could do it; but the cost of the transportation would be for the whole cruise.

As I understand, the shipping lines could not sell a ticket just for New York-San Juan transportation, just for that much. That is my understanding.

Senator BARTLETT. Thank you very much, Dr. Fernós. We appreciate your coming over.

Mr. Moscoso, director, economic development administration, will be the next witness.

STATEMENT OF HON. LUIS MUÑOZ-MARÍN, GOVERNOR OF PUERTO RICO, READ BY TEODORO MOSCOSO

Senator BARTLETT. Do you have a prepared statement?

Mr. MOSCOSO. No, sir. I have a message from the Governor of Puerto Rico which I wish to read and then I shall have an extemporaneous message to make.

Senator BARTLETT. Will you please identify yourself for the record.

Mr. MOSCOSO. I am Teodoro Moscoso, economic development administrator for Puerto Rico.

Senator BARTLETT. I may elaborate a little bit, if I may, upon that introduction.

One of the first men I met in Puerto Rico was dynamic Teodoro Moscoso, head of the Puerto Rico Industrial Development Company. This organization was set up by the insular government in 1942 to bring industry to the island and thus reduce unemployment.

Through his resourcefulness and energy, Mr. Moscoso has induced 100 industries, large and small, to locate on the island, thus furnishing about 14,500 new jobs. Other industry has arrived independently to create more work.

Mr. Moscoso's first big development job back in the war years was to build a government-owned glass factory to manufacture bottles.

Now that constitutes a quotation. As a matter of fact that was when your job was relatively new. As you come across old magazines—I found this in a dentist's office dated April 1951, and although it doesn't pertain directly to the subject matter of the hearing, I know it would be most interesting if we had the story of what has happened in the decade since this was published, but however that may be, I want to congratulate you upon a splendid job in this Operation Bootstrap.

Mr. Moscoso. Thank you, Mr. Chairman.

I read Governor Muñoz-Marín's statement addressed to the committee.

Senator BARTLETT. Yes, sir; if you can get me away from flattering you, you can. Yes, sir; indeed.

Mr. Moscoso (reading):

My dear Mr. Chairman and committee members, I deeply regret my inability to be present today. There is no single problem of greater economic consequence to the people of Puerto Rico than the problem which you have determined to investigate and remedy: the deepening crisis of our offshore shipping services.

For over half a century, Puerto Rico has been in closest association with the Federal Union, first as a territory, since 1917 as U.S. citizens and since 1952 as a self-governing Commonwealth. Basic to the relationship has been freedom of trade between Puerto Rico and the States. The consequence of free-

dom of trade has been that Puerto Rico is now integrated into the economy of the mainland. Almost half of everything we produce is shipped to the States each year. Over half of all we consume is exported from the States to Puerto Rico. The Commonwealth is one of the best customers of U.S. mainland industry and agriculture.

For this movement of vital goods we depend practically exclusively on maritime transport. We have nothing else—no trucks, no railroads, no pipelines—to move the goods which we must sell, and import the commodities we must have, for survival as a viable company. We are, as you know, concentrating our energies on a unique program of economic development in Puerto Rico—Operation Bootstrap. Operation Bootstrap must succeed if we are to meet our goal of a decent standard of living for all the people of Puerto Rico. But whether Operation Bootstrap succeeds or fails depends to a large degree upon whether the Commonwealth of Puerto Rico is served by a merchant marine of maximum efficiency and minimum cost.

Our deepest concern is with the high and mounting cost of our present services, and the looming threat that these costs will increase to levels beyond our capacity to pay, when new vessels are introduced into the service, as I am advised they must be shortly. These increasingly costly services are provided in vessels of U.S. registry. Vessels of foreign-flag registry are very much less costly, we understand. Thus, the law restricting our vital services to U.S. vessels imposes a very heavy and inequitable cost burden on the people of the Commonwealth of Puerto Rico, a burden which we calculate at more than \$10 million per year.

This inequitable burden could be lifted from our shoulders by an amendment to the law permitting the operation of foreign vessels. If, however, national interest considerations prevent this, then some other remedy must be found, such as, perhaps, a system of subvention, so that the costs of these national interest considerations are borne equitably and evenly by all citizens of the United States.

The people of the Commonwealth of Puerto Rico are deeply gratified that your committee has set out to remedy this vital problem. I have asked Mr. Teodoro Moscoso, the administrator of our economic development administration, to present this communication to you, on behalf of the Commonwealth government and to extend the resources of the Commonwealth government in every way in cooperation and aid of your program.

Gov. LUIS MUÑOZ-MARÍN.

Senator BARTLETT. The committee appreciates this expression from the Governor, and for the record I will say that it is indeed a very deep interest, to my personal knowledge, which has been reflected not only in the presentation of this statement which you have just read, but which was long since generated.

When the Governor was here in January, I recall that he participated in at least two meetings devoted to discussion of this very subject. Governor Egan, of Alaska, and Governor Quinn, of Hawaii, were also present, and it should be recorded that the three Governors are intensely concerned about the maritime shipping problems in their respective areas.

You may proceed.

Mr. Moscoso. Mr. Chairman, from the biographical notes that you were kind enough to read, you will know that I have been living with this problem for quite a number of years and it has become increasingly burdensome to the industrial development program.

The net income of Puerto Rico in 1959 was \$1,300 million. Now, during the fiscal year 1960 we brought in from the United States \$750 million worth of goods, and we shipped to the continental United States \$600 million worth of goods. Now if you add this two-way movement of oversea shipments, you will see that they add to a total which is larger than the entire net income of Puerto Rico.

Now, I think that there are very few areas in the world that can match that kind of a situation.

In the case of the continental United States, the total import and export trade of the United States, both over land and over water is less than 10 percent of the national net income. In the case of Puerto Rico, it is over 100 percent. In other words, shipping to us over the ocean lanes is from 10 to 12 times more important than it is to the economy of the United States. You can see why we give so much attention to this problem.

The industrialization program, as the chairman mentioned awhile ago, was originally initiated to try to solve the problem of unemployment in Puerto Rico. I am sorry to say that even with the strides we have made, we are still quite far from solving that problem. Our unemployment rate now stands at 14 percent of the labor force. That is a very substantial proportion.

The ocean and freight rates and the increases we have been suffering over a period of time are of great magnitude. Since fiscal 1947-48, these rates have gone up close to 100 percent. In the last 4 years alone the increases have been in the magnitude of 29 percent. During the same period, during these past 4 years, the foreign-flag costs have increased, according to the United Nations Secretariat, less than 1 percent. The rate increases in the United States-Puerto Rican trade over the last 10 to 12 years have roughly been three times the increase of the U.S. wholesale price index.

Now, I notice that one of the witnesses from Hawaii, yesterday, mentioned a comparison similar to this, except that the comparison was made between shipping costs of Hawaii and the Honolulu consumers cost index. In this case, I am using as a basis of comparison, the U.S. wholesale cost index, and you can see that the figure indicates an increase three times faster in shipping costs than in the U.S. wholesale cost price index.

The present freight rates really impose an inequitable burden on Puerto Rico. As it is well known by the committee, foreign-flag vessels cost about one-half to build and operate than U.S.-flag vessels. We have estimated that to Puerto Rico alone, this additional cost represents about \$10 million per year. However, this impact on Puerto Rico must be viewed in the light of the fact that our net income per capita is about a fourth of the average net income per capita in the United States. So the \$10 million really must be compared to a figure closer to \$40 million if you are going to look at it from the point of view of our much lowered net income per capita.

The impact differential in subsidies in the U.S. mainland is about 89 cents per capita, that is, the cost of the maintaining of the subsidy program of U.S.-flag vessels in foreign trade. Whereas the \$10 million excess cost in the Puerto Rican shipping represents about \$4.28 per capita. In other words, it is costing Puerto Rico about five times more per capita than it is costing the mainland citizens. However, again since our net income is about a fourth of what the mainland net income is, you really have to multiply this by four to get the true impact in the lives of the people of Puerto Rico. In other words, it is costing, on the basis of our much lower net income per capita, about 20 times more to support this differential between the shipping costs of American-flag vessels and what we could get if foreign-flag vessels were allowed to ply between Puerto Rico and the United States.

This, of course, has heavily affected the shipments to Puerto Rico from mainland suppliers. It is already affecting the shipment of American-made automobiles. I notice that the Hawaiian gentleman, yesterday, mentioned that very same situation. We are starting to see that in Puerto Rico, also.

As a matter of fact, a considerable number of our automobiles are foreign made today. The vessels we are now using are, as you are all aware, obsolete or obsolescent and they will have to be retired very soon. We all recognize that up to now the trade has been obtaining a type of subsidy by being able to acquire these vessels from the reserve fleet at a considerably lower cost than what it would be if they had to buy new vessels. Even assuming that we were able to obtain construction subsidy for the vessels which will be replaced in this trade, I can see where the impact of this subsidy would not be sufficient to maintain freight rates at a level which would allow these off-shore areas to develop adequately.

The alternative is either we continue operating these obsolete vessels which, of course, would be almost worthless in case of an emergency, or we replace them at high domestic cost, which, of course, will increase the rates. These rate increases may probably go beyond a point where we are able to pay for them. We must have some kind of a release. We must have an operation of the lowest cost carrier regardless of flag and a subsidy to enable domestic carriers to compete. We must also strengthen our regulatory procedures and our standards.

I think that it has been well brought out by other witnesses that have come before this committee that the regulatory functions of the Maritime Commission are in a clash with the promotional functions of the Commission, and I am afraid that that is something that will have to be resolved sooner or later.

I notice that Mr. Gruening brought that out very forcefully yesterday.

Now, we have prepared a study, copies of which are available, on Puerto Rico's problems with the U.S. maritime laws. This study was prepared almost 2 years ago, but it has been brought up to date, as of January 1961. Copies of it will be available to the members of the committee.

I must say that the first time we tried to bring this matter to the attention of the Executive, we were assured in a letter by President Eisenhower of June 16, 1959—

that the review of the U.S. maritime policies, which I have asked the Secretary of Commerce to undertake, will include a careful consideration of the difficulties faced by the Commonwealth of those in shipping. This review embraces not only the Merchant Marine Act of 1936, but all other significant aspects of Federal policy affecting the merchant marine.

Now, this was June 16, 1959. This letter was received by the Governor of Puerto Rico as a result of the transmittal of the original study of the problems of the U.S. maritime laws insofar as they affect Puerto Rico.

Now, the Department of Commerce prepared a report dated March 1960, called "Federal Transportation Policy and Program," and the

only mention which I can see which pertains to this particular problem is the following, and I quote:

The economic problems of the noncontiguous States and territories arising from the high shipping costs and these protected trades have been called to our attention and it has been suggested that either foreign-flag participation in these trades or subsidy must be provided. These issues turn however on broader considerations than those of transportation policy herein discussed.

I am very happy, Mr. Chairman, that you have taken the initiative in this committee to study this very, very important problem which affects the life of the noncontiguous areas of the United States, and I am sure that as a result of the activities of your committee, we will now get positive action.

Thank you very much.

Senator BARTLETT. We thank you.

My only regret is that every member of the full committee was not here to hear your statement. It was very convincing. How is Operation Bootstrap proceeding?

Mr. Moscoso. I am afraid between what we can now call a recession and the high shipping rates, we are not doing as well as we had expected this year. Our promotions are much slower than we had anticipated.

How much of that is due to the recession and how much of that is due to the fact that high shipping rates are making it very difficult for certain industries to establish themselves in the island, we have not been able to find out as yet. We are looking into the problem continuously, as you can see from the report that I have filed with the committee, and we hope to have an answer shortly.

But I must say that everything that we can do to make Operation Bootstrap successful should be done because it is the only hope we have in Puerto Rico of achieving a decent standard of living for our people.

Senator BARTLETT. Well, if we can refer to Americans as being customers of Americans in this sort of trade, Puerto Rico must rank very high in respect to imports of American goods and exports to the United States in the whole worldwide scheme of things.

Mr. Moscoso. Yes, sir. We purchased approximately \$800 million from the United States in the past year and we shipped about \$600 million. Of course, there is a difference there which the balance-of-trade gap is closed by invisible exports such as tourist dollars which are spent in Puerto Rico and now that I mention tourist dollars, I am very happy to see Dr. Fernós brought out the fact we do not have passenger service to Puerto Rico. We have not had it in the last 8 years.

If you are unable to fly for medical reasons or for psychological reasons, the only way you can get down to Puerto Rico and come back is by using a freighter, and one of the 12 staterooms which are normally available in freighters, except that these staterooms are usually set aside for large shippers that use the freighter services of these carriers.

Senator BARTLETT. How many lines are serving Puerto Rico?

Mr. Moscoso. We have Bull, Sealand, Waterman, Lykes, Alcoa, and one more company the name of which I do not recall now, and probably a smaller company that services primarily the—oh, yes, Is-

brandtsen, which also services us on a round-the-world service. Those are seven companies.

Senator BARTLETT. What is your situation as to adequacy and frequency of service?

Mr. MOSCOSO. We have reasonably good frequency of service, yes. That has not been our particular problem.

Senator BARTLETT. How many people are there in Puerto Rico?

Mr. MOSCOSO. The island has 2,380,000 inhabitants—2,380,000 inhabitants and it has an area of 3,500 square miles which gives a population density of about 650 per square mile.

Senator BARTLETT. That is very, very high in terms of thickly settled countries of the world, isn't it?

Mr. MOSCOSO. One of the highest in the world, yes, sir.

Senator BARTLETT. Is the population increasing rapidly?

Mr. MOSCOSO. It has been increasing rapidly, at the rate of approximately 2½ percent per year. This has forced the migration of a considerable number of Puerto Ricans in search of jobs to come to the United States. A number of them have come into New York. Fortunately now they are spreading all over the country, primarily in the northwestern section of the Nation. During the past few years, however, the rate of migration has come down considerably, primarily due to the fact that not enough jobs have been available. This is a good indication that the Puerto Ricans will only migrate if they can get jobs.

Senator BARTLETT. It isn't because the jobs are available at home?

Mr. MOSCOSO. It is because jobs are not available at home. We have not been able through Operation Bootstrap to create sufficient jobs to take care of not only of the backlog but also of the increase in the labor force every year.

One of the difficulties that we face, Mr. Chairman, is the fact that at the same time that we are industrializing we have been rationalizing or mechanizing our agriculture, so we have been destroying or pushing people out of jobs in as large numbers as we have been creating new jobs for them.

Senator BARTLETT. Do you have any personal explanation for the fact which you stated that American shipping costs are going up with such great rapidity as compared with slow increases on the part of foreign carriers?

Mr. MOSCOSO. There are undoubtedly a number of reasons for that, sir. The merchant seamen of the United States are extremely well paid as compared to foreign seamen. I am very happy that is so. The only complaint which I have is that Puerto Rico is probably the less able of several areas to pay these wages.

The other reason, of course, is that almost everything that pertains to maritime transportation has been going up. Fuel, all the services that they use, the construction of piers and docks by some of the steamship companies, et cetera.

Senator BARTLETT. You mentioned the unemployment rate in Puerto Rico as being 14 percent. Is that a seasonal factor?

Mr. MOSCOSO. No, sir, this is the yearly average. We have times when this drops, that is, at the time when the sugar season is at its high peak. But this is the average throughout the year.

Senator BARTLETT. What is the per capita income in Puerto Rico?

Mr. MOSCOSO. Now \$565.

Senator BARTLETT. How does that compare, if you know, with Mississippi?

Mr. MOSCOSO. It is about one-half of that of Mississippi and about a fourth of the average per capita income of the whole United States.

Senator BARTLETT. But it has been increasing very dramatically in the last decade?

Mr. MOSCOSO. It has been, but it also has been increasing here in the States. We are really low men on the totem pole.

Senator BARTLETT. You said, as I recall, shipping costs have gone up three times as much as U.S. wholesale prices—in what period?

Mr. MOSCOSO. In the last 12 years.

Senator BARTLETT. In the last 12 years?

Mr. MOSCOSO. The last 12 years, yes, sir.

Senator BARTLETT. While testifying yesterday, the Chairman of the Federal Maritime Board suggested to the committee that there would be need to evaluate as a unit, as it were, all of the factors that enter into these increased costs. Did you have an opportunity to read his statement?

Mr. MOSCOSO. I read it last night, sir, late last night.

Senator BARTLETT. You will recall then, he said that freight rates by themselves constitute only one element of many and I should like to ask you if you care to answer—what weight you would give to those suggestions that Chairman Stakem made?

Mr. MOSCOSO. Over the years we have been looking into this problem and we know pretty much how much an impact freight rates have on Puerto Rican costs. It is rather simple to take our trade figure and to take our freight bill and work out the cost of moving that freight in and out of Puerto Rico.

Senator BARTLETT. Do you know, of your personal knowledge, what consideration was given to those factors by the Federal Maritime Board in respect to proposed recent rate increases?

Mr. MOSCOSO. If they have taken into consideration the impact on the economy of Puerto Rico?

Senator BARTLETT. Yes.

Mr. MOSCOSO. I have my doubts about that, Mr. Chairman. I don't really know, but I have my doubts about that. Sometimes I believe that they are strictly concerned with the profit-and-loss statements of the carriers.

Senator BARTLETT. You feel that perhaps Senator Gruening had a point when he informed the committee yesterday that these two responsibilities didn't always meet and blend, promotional and regulatory?

Mr. MOSCOSO. I think it is very difficult to blow hot and cold out of the same side of your mouth. I think that perhaps we are asking them to do the impossible. Maybe this should be separated into two different agencies.

Senator BARTLETT. You don't believe, as I gathered from your statement, that application of a construction differential for these trades would cure these ills?

Mr. MOSCOSO. No, sir, I don't think it is sufficient, because right now for all intents and purposes we have almost subsidized construction of these vessels by virtue of the fact that the carriers have been able to acquire them at a relatively low cost. I remember seeing

the testimony of the attorney general of Hawaii where he listed the value of the vessels now being used by the Matson Line. I can assure you that those vessels today, if replaced by new vessels, would probably cost anywhere from 5 to 10 times what is now the value of boats.

Senator BARTLETT. By itself, that might only serve to aggravate an existing bad situation?

Mr. MOSCOSO. Yes.

Senator BUTLER. Did you say that each citizen of the United States now pays, whether he knows it or not, and I suspect he does not, 89 cents of his tax money for subsidization of U.S.-flag carriers?

Mr. MOSCOSO. Eighty-nine cents per capita for the entire subsidization program, and we pay \$4.28 in Puerto Rico.

Senator BARTLETT. Of course, to calculate what it might cost if a program of the nature you recommended were applied for the benefit of Puerto Rico and Guam and Hawaii and Alaska would be virtually impossible on the basis of data available to you. You don't know what that would cost, do you?

Mr. MOSCOSO. No, I don't know what that would cost.

Senator BARTLETT. That isn't your business to inform us, of course.

I was very interested when you said that the Governor of Puerto Rico had called this situation to the attention of the executive department as far back as 1959, because the situation was already then bad, and that the report that was made ducked the whole proposition, didn't go into it at all, in spite of the assurances the Governor had that it would receive closer inquiry.

Mr. MOSCOSO. Yes, sir.

Senator BARTLETT. You never heard why it is that the inquiry was not made?

Mr. MOSCOSO. I have no idea, Mr. Chairman, why this thing was not given the attention it really merits. I am almost sure that this was due to the fact that your committee had not taken a hand in the matter. I feel quite confident that the results are going to be much different from now on.

Senator BARTLETT. I must say, not in a questioning manner, but in a declaratory one, I have never been able to understand why this committee should have to initiate the inquiry, because it is properly, in my opinion, the responsibility of the executive agencies.

You said the fleet serving Puerto Rico is becoming obsolete and obsolescent?

Mr. MOSCOSO. Yes, sir.

Senator BARTLETT. You are an economist. As I understand it, you are professionally an economist?

Mr. MOSCOSO. No, sir; I am a pharmacist.

Senator BARTLETT. Pharmacist?

Mr. MOSCOSO. Yes, sir.

Senator BARTLETT. You haven't had much chance lately to mix any drugs, have you?

Senator BUTLER. What is that cigarette—you think for yourself? Viceroy.

Senator BARTLETT. Right here, I need them today.

You are going to qualify in my judgment as an economist anyway. If nothing is done in this area—

Mr. MOSCOSO. Pardon me.

Senator BARTLETT. If nothing is done in this area, if we fail to enact any legislation, if otherwise no action to alleviate is taken, what is going to be the consequence, in your judgment, so far as Puerto Rico is concerned?

Mr. MOSCOSO. The consequence will be that rates are going to continue to increase because it is almost impossible to reduce costs with these obsolete vessels. I can see that wage rates are going to continue to increase among the seamen. It will be necessary to increase them as time goes on. There will be no possibility of increasing the productivity in these vessels because of their obsolete characteristics, and, therefore, it will be the consumer in Puerto Rico who will have to pay the price.

Senator BARTLETT. What will this do to your program of industrialization?

Mr. MOSCOSO. The industrialization program is already suffering from these increases in rates. One of the things that it has done is that it has forced us to limit ourselves to certain industries that are not affected too much by increases in freight rates. It almost virtually forces us into that, anything that is heavy and bulky, in which the raw materials are heavy and bulky or in which the finished product is heavy and bulky, is almost out of the question.

We have had to limit ourselves to light manufacturing, to electronics, light metal manufacturing, and things of that kind which, of course, hampers us tremendously.

Senator BARTLETT. You are required to import a considerable percentage of your foodstuffs; are you not?

Mr. MOSCOSO. Yes.

Senator BARTLETT. How do the people live, with an average income of less than \$600?

Mr. MOSCOSO. We have been doing what we can in order to reduce those costs.

Since the ships apparently are not going to be changed unless something is done within the next few years, we have been trying to better the loading and unloading facilities at the docks.

For instance, our main industry is sugar, and we now are shipping all of our raw sugar to the United States in bulk. That has reduced costs.

We are now shipping in wheat instead of bagged flour and we are milling in Puerto Rico. We are now shipping in the raw materials for our cattle and poultry feed in bulk, and that has also reduced costs considerably.

Rice, which is the main staple in our diet, is also being brought in in bulk and we have been able, in that way, to hold the line on costs, but we cannot go any further. I do not think that there are very many more things that we will be able to ship in in bulk, so insofar as rationalization, as the term is concerned, I think we have about reached the limit.

Senator BARTLETT. Then you told the committee that freight rates have increased 100 percent, almost, since 1947-48.

Mr. MOSCOSO. That is right.

Senator BARTLETT. And 29 percent in the last 4 years?

Mr. MOSCOSO. That is right.

Senator BARTLETT. If this trend continues, under existing arrangements, inevitably this will mean a decline in the standard of living

for Puerto Ricans, the average Puerto Rican who does not have now a very high standard.

Is that a fair assumption?

Mr. Moscoso. That is a fair assumption for two reasons: First, the items of consumption for Puerto Ricans will increase considerably in price, because as I mentioned to you, over 50 percent of everything we consume has to be shipped in by boat, and it will also reduce the standard of living because I do not believe that the industrialization program can continue at the rate it is doing today if freight rates continue to increase at that fast a pace.

Senator BARTLETT. I have read this study which you alluded to entitled "Puerto Rico's Problems With the United States Maritime Laws," dated January 1961, and I believe it is so valuable, that it ought to be incorporated as part of the record.

If there is no objection, it will be included.

(The study referred to appears as appendix A, p. 324.)

Senator BUTLER. I would like to ask one or two questions, Mr. Moscoso.

I must first beg your pardon for not having been here during your entire testimony.

You referred to an 89-cent subsidy per annum for each man, woman, and child in America?

Mr. Moscoso. That is right, sir.

Senator BUTLER. You also referred to the high wages paid to American seamen?

Mr. Moscoso. Yes, sir.

Senator BUTLER. What is the relationship between the two? I don't know the point that you were trying to make.

Mr. Moscoso. I am not trying to imply that the entire reason for the high shipping rates is due exclusively to the high wage costs. There are other reasons including the fact that our vessels are thoroughly obsolete.

The only point of contact between one figure and the other is as follows: The 89 cents is the result of the dividing the cost of the subsidy program—

Senator BUTLER. That is the construction differential?

Mr. Moscoso. No; the operational subsidy.

Senator BUTLER. Just the operational subsidy alone?

Mr. Moscoso. Which is about \$150-some-million a year, by the population.

Senator BUTLER. Does that take into account the recapture under the Merchant Marine Act?

Mr. Moscoso. No, sir; this is just exclusively the operation—

Senator BUTLER. The money is paid out and you do not deduct from that any money that the Government recaptures under provisions of the law?

Mr. Moscoso. I believe that this is a net figure, as far as I know.

Senator BUTLER. This is a net figure?

Mr. Moscoso. Yes, sir.

Senator BUTLER. And the purpose of that figure is what—why do you cite that figure? What do you do it for?

Mr. Moscoso. This figure is the cost of the subsidy program adopted through the Maritime Administration for the purpose of permitting U.S.-flag vessels to compete in foreign trade in order to

have a ready fleet, in order to accomplish the purposes of the Maritime Act.

Senator BUTLER. In other words, that subsidy puts the American merchant marine operator on precisely the same basis as his foreign competitor?

Mr. MOSCOSO. That is right.

Senator BUTLER. But it gives him no advantage and he suffers no detriment by reason of it?

It merely puts him in a position to compete on equal terms with a foreign competitor?

Mr. MOSCOSO. That is right.

Senator BUTLER. If he makes more than that amount of money, he has to pay some back to the Government under the provisions of the act?

Mr. MOSCOSO. That is right.

Senator BUTLER. You are for that, are you, for the subsidy?

Mr. MOSCOSO. I am for that; yes, sir.

My only contention is this, that the same subsidy should apply to the shipping freighters in the offshore areas of the United States.

Senator BUTLER. Let me get your reasoning on that.

Mr. MOSCOSO. The offshore areas of the United States are forced by the cabotage laws to trade exclusively in American flatbottoms. The purpose again is to have a ready fleet. Of course, it goes back to 150 years ago and merchantilism, but the modern concepit is that this is being done in order to help the United States have a ready fleet in case of an emergency.

Now, our contention is just the same as we pay a subsidy to American vessels which trade in foreign trade, there should be a subsidy given to American vessels that apply to offshore areas, otherwise the burden is inequitably distributed.

In the case of Puerto Rico, we have found if we were allowed to trade in foreign-flag vessels, we would pay \$10 million less.

Now in an economy such as ours, where the net income per capita is one-fourth that of the United States, that has the equivalent impact of \$40 million freight bill, which we have to pay in addition to what normally would be paid, if we did not have to use American-flag vessels. And that price, \$4.28, multiplied by 5, gives us a total of about 20 times more.

Senator BUTLER. Thank you, sir.

Senator BARTLETT. Mr. Grinstein?

Mr. GRINSTEIN. Mr. Moscoso, yesterday Chairman Stakem of the Maritime Board suggested that the committee study other costs besides shipping that are added to consumer goods, such as retail and distribution costs. Has Puerto Rico made a study of that?

Mr. MOSCOSO. Yes, sir. Prof. John Kenneth Galbraith did a very fine study. I think he is going to be the Ambassador to India. Professor Galbraith made this study about 8 years ago and it is called Marketing Efficiency in Puerto Rico. It was done under the auspices of the Social-Scientific Research Center of the University of Puerto Rico and results have been published in a book by Harvard University Press.

We acted on the basis of that report and whereas 8 years ago, 6 years ago, Puerto Rico did not have a single supermarket, today we

have 30. We have some of the largest retail exchanges in the United States operating in Puerto Rico today.

We have modernized, by the way. We also have drug chains that have come into Puerto Rico to compete with our local drugstores. We have in every possible way stimulated competition to a point where quite a number of Puerto Rican merchants are almost complaining that there is too much competition. Well, that was bound to be expected and Professor Galbraith said that would happen.

In other words, we have been doing something about the distributive trades—knowing quite well that there might be some hidden costs there that were increasing our costs of living.

You will notice that the cost-of-living allowance allowed Federal employees has been reduced in the case of Puerto Rico in the past few years and I think that is partly due to this program of commercial modernization.

Mr. GRINSTEIN. Mr. Moscoso, has the Commonwealth protested the rate increases over this, I guess, beginning in 1947-48?

Mr. MOSCOSO. Vociferously.

Mr. GRINSTEIN. All of them?

Mr. MOSCOSO. Every one.

Mr. GRINSTEIN. These protests, I take it, were based not only on rate formula and standards to be applied but also impact of the economy needs and industrial development?

Mr. MOSCOSO. Now, one case before the court, as a matter of fact, already has been remanded to the Federal Maritime Board for review.

Mr. GRINSTEIN. This base on standards to be applied in ratemaking formula?

Yesterday Senator Gruening testified that there was an absence of standards on the part of the Federal Maritime Board in the rate proceedings. Do you have any view on that?

Mr. MOSCOSO. Well, we have a view and that has been expressed in our briefs before the courts to the effect that we do not think that they should use a market value for establishing a base for the rate-making. We think that it should be cost of acquisition less depreciation and I believe that the courts have seen fit to have the Board review its method of figuring the base rate.

Senator BARTLETT. Mr. Bourbon?

Mr. BOURBON. Mr. Moscoso, I was reading recently in one of the maritime journals about a new service which you were getting down there, I think it may have been from T & T Trailer Co., the people who had the unfortunate experience with the *Carib Queen*, in which they were supposed to have gotten away from conventional vessels and taken some LST's, removed the propulsion units, and were taking them down with tugs. Their idea was that they could do that with an 8-man crew on a tug, where it would be 35 or 40 on a ship. Now are you familiar with that operation?

Mr. MOSCOSO. I know the operation a little bit; yes, sir. I have seen them operate in and out of San Juan.

Mr. BOURBON. I was wondering whether you could say whether you had gotten any lower rates because they had been able to operate so much more effectively?

Mr. MOSCOSO. The rates are slightly lower than the usual freight rates. Of course, you have to carry a full freighter.

Mr. BOURBON. One other thing, last year, the last Congress passed a bill to give you some passenger service to the Virgin Islands by hydrofoil and by the time we got the bill through, we found the man had decided not to operate out of your place. His reason was that your Commonwealth had not lived up to certain promises made to him about berthing facilities, et cetera, so now he is up in Puget Sound. Was he correct in saying that the reason he didn't use the law that we passed was that after making him certain promises you didn't fulfill them?

Mr. MOSCOSO. I think that he was partly right, the proportion being maybe 10 or 15 percent right. We were a little bit derelict in constructing the facilities, primarily due to the fact that his estimate of cost was way below what it actually turned out to be when we went out on bids. But the facilities were finally built for him and if he does not give us that service, we propose to buy the hydrofoils ourselves and provide that service.

Mr. BOURBON. One other question: How long does it take by boat to go from Miami to San Juan?

Mr. MOSCOSO. From stateside.

Mr. BOURBON. From Miami?

Mr. MOSCOSO. From Miami, I think it would be about 3 days. I wouldn't know. I know the New York-San Juan much better; that is 3½ days.

Mr. GRINSTEIN. You do have containerized shipments down there?

Mr. MOSCOSO. Yes, we are very lucky to have been able to establish the containerized service, which started about a year and a half ago, after quite a bit of difficulty, coming to an agreement with the labor unions. But, it is now operating and we have great hopes that eventually it will mean a reduction or at least a holding of the line insofar as freight rates are concerned.

Now, this is the kind of a breakthrough in maritime transportation that probably should have been inspired or encouraged quite a number of year ago. Much more of that I believe has to be done, especially with the problem of the noncontiguous areas prominently in mind.

Mr. BOURBON. Do you find the containerization is less expensive?

Mr. MOSCOSO. Less expensive for quite a number of products and, as a matter of fact, as we gain experience with the movement in containers, I believe that we are going to find that with the exception of a few cargoes, most of the goods that we move back and forth can be moved in containers.

Mr. BOURBON. Is Sealand the only concern that uses containers?

Mr. MOSCOSO. Yes, Sealand is operating in Puerto Rico.

Mr. BOURBON. That is all I have.

Senator BARTLETT. Do you have any questions, Mr. Goding?

Mr. GODING. I have only one question.

In your economic industrial development program, you have made quite a number of studies. Have you studied the failures as well as the successes and the reason for them? Do you have any figures relating to shipping costs as a factor in closings?

Mr. MOSCOSO. We have a complete analysis made every year of all the factory closings and, in a number of instances, that has been given as one of the reasons for their having to close, primarily, when it is a heavy product. I remember in the case of automobile spring

operation, where the steel had to be brought in, and then the springs had to be distributed, the manufacturer claimed that was one of the reasons why he had to close down.

Now, one of our biggest difficulties, however, is not with the industry that we already have, but with the industry that has not come in yet, convincing them that they can operate with the specter of a freight increase staring them in the face in the very near future.

Senator BARTLETT. Mr. Moscoso, it was testified here yesterday by a representative from Hawaii that the pineapple industry there is being hurt by foreign competition, and he related that one big pineapple factory on one of the islands is about to close down because pineapples from Asia are being shipped to the United States at a lower cost than the Hawaiian producers can meet.

Are you in any comparable situation?

Mr. Moscoso. Yes, sir; we have a pineapple cannery in Puerto Rico and they found themselves with a very soft market a year and a half ago and we asked our representative in Europe—we have a small office in Frankfurt—to see if he could dispose of some of his inventory in Europe.

He is a very knowledgeable businessman. He knows the European market quite well and for almost 3 months he attempted to sell the pineapples and he was faced with this competition from Taiwan, to be specific. Their price was almost half of what we could sell it for.

Senator BARTLETT. Do you think this was partially or altogether on account of higher freight rates?

Mr. Moscoso. No, sir; partly due to freight.

There were other factors involved, but it was partly due to freight.

Senator BARTLETT. Partly due to freight?

Mr. Moscoso. Yes, sir.

Senator BARTLETT. Now the fact of the matter is, is it not, that together with all the benefits Puerto Rico enjoys by being under the American flag, it also suffers a discrimination here in that you are required to abide by the U.S. maritime laws. Otherwise you could have foreign carriers serving?

Mr. Moscoso. Yes, sir.

Senator BARTLETT. And the people of Puerto Rico bear the entire burden for maintaining this merchant marine that serves the Commonwealth?

Mr. Moscoso. We would be willing to bear a reasonable share of that burden, just like any citizen of the United States. We are not trying to shirk our duty here, all that we say is that it should not be any heavier than what it is on the shoulders of any other citizen of the United States.

Senator BARTLETT. Thank you for a most excellent statement.

You have been a first-class witness.

Now, it is Alaska's turn and I believe the witness representing the State of Alaska is Mr. Burke Riley, executive assistant to Governor Egan.

Do you have a prepared statement, Mr. Riley?

Mr. RILEY. I have, Mr. Chairman.

Senator BARTLETT. Do you have any copies for the committee?

Mr. RILEY. That I don't know.

Senator BARTLETT. We will take a 5-minute recess and perhaps you will have copies of the statement.

(Short recess.)

Senator BARTLETT. The committee will be in order.

Mr. Riley, I apologize for the delay in hearing you and it is high time that we hear a witness from the 49th State and the biggest State. You may proceed.

STATEMENT OF BURKE RILEY, EXECUTIVE ASSISTANT TO THE GOVERNOR OF ALASKA

Mr. RILEY. Mr. Chairman, for the record, my name is Burke Riley. I am executive assistant to Gov. William A. Egan of Alaska and appear for him.

I should like to convey Governor Egan's regrets at not being able to be here personally. He believes the problems under consideration by this committee to be extremely important and would be here in person were it possible for him to leave Alaska at this time.

May I express my appreciation on behalf of the State of Alaska for this opportunity to appear. I know of no problem in Alaska more deserving of our collective efforts and attention than the critical problem of adequate and economical transportation. This problem is of highest priority and greatest urgency. Its proper solution is vital to the development of Alaska.

I should like particularly to thank the senior Senator from Alaska, the Honorable E. L. Bartlett, for initiating these hearings. I am advised that it was Senator Bartlett's persistent efforts, with the support of his able and distinguished colleague, Senator Ernest Gruening, which brought about this extremely worthwhile investigation. This is especially gratifying. It is a dividend of statehood. We in Alaska know that with Senators Bartlett and Gruening on the job in Washington our problems will have an attentive and sympathetic audience by the U.S. Senate.

I am of the impression that these hearings were called to consider a basic issue of national policy. That issue is whether the noncontiguous domestic areas of the United States such as Alaska, Hawaii, Puerto Rico, and Guam are to be forced to continue to bear the cost of national defense measures adopted for the benefit of the entire Nation. I refer to the policy of restricting waterborne commerce exclusively to American bottoms between those areas and other parts of the United States without benefit of any Government assistance. The continuance of that policy is unjust. Moreover, the cost of its continuance is becoming intolerable for the areas involved.

While I speak specifically about Alaska, the other noncontiguous domestic areas face the same problem. Those areas are rapidly approaching an economic crisis of great magnitude and that crisis in large measure is a result of the high cost of transportation. The ultimate question is whether the economies of these areas shall be allowed to develop and flourish or, instead, shall continue to be retarded by an outmoded and stultifying national policy. Certain characteristics of the Alaska trade must be borne in mind in considering its shipping problems.

Like the other noncontiguous areas, Alaska's carriers are faced with the problem of seasonability of the trade and an unbalanced movement. The difference is one of degree. In the Alaska trade the bulk of the northbound movement occurs in a period of approximately 6 months, from April through October. Other maritime trades are generally faced with the same problem but over a span of differing months.

Like the other trades, the Alaska trade has one port or area of major importance in terms of volume of traffic. Thus, in the Alaska trade the port of Seward with its command of the so-called rail belt receives the greatest portion of northbound cargo. Following Seward come the ports of Valdez, Kodiak, Ketchikan, and Juneau. These would compare, in importance, to San Juan, Mayaguez, and Ponce in the Puerto Rican trade.

Alaska receives no service whatever from subsidized vessels operating over connecting links with subsidized trade routes. Consequently, Alaska has no shipping company operating to and from any of its ports with vessels constructed or acquired with the aid of construction-differential subsidies.

The physical characteristics of Alaska require that year around, regular water line service be supplied to several areas of the State because there is no other way of bringing in the necessities of life and commerce. These areas include southeastern and southwestern Alaska, Kodiak Island, Bristol Bay, and the Bering Sea.

Finally, Alaska stands alone, with most of its backhaul traffic bound inextricably to one commodity, fish, which by nature and resource management is limited to perhaps 30 to 60 days during the summer months.

So far as Alaska is concerned, it is of utmost importance to reduce or at least stabilize the high costs of transportation. Approximately 95 percent of all consumer goods used in Alaska must be imported by water, rail, air, or truck. The overwhelming proportion of such imports comes by water, and water transportation rates have risen incredibly.

It has been mentioned already in these hearings, that within the last 10 years, waterborne freight rates in the Alaska trade have increased 56.4 percent.

Since January 1, 1958, water rates have increased by 32.8 percent.

The cost of transportation is, of course, a part of the landed cost of the product. The high cost of transportation is an element in the high cost of labor, and in turn in Alaska's having the highest cost of living of any State in the Nation.

Alaska is making great efforts to develop its economy, with particular reference to the development of its natural resources. Progress is being made, but not because of the transportation picture. If transportation and associated costs continue to rise, new and prospective industry will be priced out of the market before really starting. That must not happen.

The high cost of our water transportation is attributable directly to the national policy of requiring shipments between Alaska and the other States to be made on U.S.-flag vessels. I have no quarrel with that policy. But if we are to maintain the policy of restricting ocean transportation between the noncontiguous domestic areas and other

ports of the United States to U.S.-flag vessels built in American yards and manned by American crews, we must be willing to recognize that the cost of such a policy is a national obligation.

To impose the entire cost of this policy on the citizens of Alaska, Hawaii, and Puerto Rico is not only unconscionable but also ineffective. It has resulted in the deterioration, rather than the promotion, of a sound merchant marine, and at the same time has frustrated the economic development of those areas.

Since 1898 the American coastwise trade has been expressly reserved to U.S. vessels, and so far as Alaska is concerned, earlier statutes had been interpreted to the same effect. In 1900, the Foraker Act extended the coastwise shipping laws to trade between Puerto Rico and the continental United States. Thus, while these areas in terms of geography and economics are not part of the domestic coastwise trade, legalistically and artificially they were so made.

Meanwhile, the cost of American shipping has risen spectacularly. In the subsidized trades those increases have been absorbed by the Nation, in the noncontiguous domestic trades these costs have been imposed entirely on the traffic to those noncontiguous areas.

The tremendous rise in the cost of American shipping as compared with foreign shipping has been recognized by the Congress. In 1936, in the interests of preserving a maritime fleet for war, subsidies were extended to U.S.-flag operators in foreign trades.

Consequently, domestic coastwise shipping in the continental United States has virtually disappeared. Transportation by truck and rail has become more efficient in those years, and there is now almost no reserve domestic fleet.

The people of the offshore areas were not so fortunate. They received no subsidy by the 1936 act. But they were unable to turn to the more efficient methods of land transportation.

They have had to rely on maritime transportation. And they are now paying the penalty in the form of higher rates.

At the present time, the entire burden of limiting these trades to the U.S. flag is borne by the traffic of these areas.

Now this outmoded system is falling apart. The most direct evidence of the evils of the present policy has been its impact on the cost of living in the areas affected. The Ward Index of Consumer Prices in seven Alaskan cities, published November 15, 1958, shows the following comparison in cost-of-living index based on Seattle, 1956, as 100.0: Nome, 159.3; Fairbanks, 154.6; Anchorage, 143.7; Seward, 131.4; Juneau, 129.0; Sitka, 135.8; and Ketchikan, 127.1. As alarming as those figures are, the corollary differentials in the landed cost of capital goods is more alarming in their threat to the development of Alaska.

I am not familiar with the cost of living in Hawaii and Puerto Rico, yet I know that they labor under a similar burden. A comparative cost-of-living survey released by the U.S. Civil Service Commission in February 1960, showed the following comparisons for the year 1959 with Washington, D.C., a notoriously high cost-of-living area as 100.0: Honolulu, 117.6; San Juan, 111.9. The same study showed Anchorage, 147.8; Fairbanks, 152.0; and Juneau, 133.1.

Unfortunately, this problem, created in great measure by high transportation costs is accelerating rather than diminishing. These trades will soon face a massive problem of vessel replacement, which

at current U.S. construction costs would impose backbreaking burdens.

Under present legislation there is no vessel replacement program required of carriers in the noncontiguous domestic trades. Generally speaking the carriers have not undertaken new vessel construction. By and large, they have acquired vessels from the reserve fleet of the United States, thus diminishing the value of that reserve source. Obviously, such a program cannot be followed indefinitely.

In the Alaska trade the problem is particularly acute. Most of the vessels in that trade were built during the war and are already obsolete.

Various possible solutions have been advanced for these problems of high transportation costs and vessel replacement.

Mr. Clarence G. Morse, former Maritime Administrator, and Chairman of the Federal Maritime Board, appeared before this committee on February 16, 1960, and suggested two alternatives: one, to subsidize the noncontiguous trades and the other to permit foreign-flag vessels to operate to the noncontiguous domestic areas. The same suggestions were made in the Department of Commerce's report to the President in March 1960, entitled "Federal Transportation Policy and Program."

The elimination of the protective cabotage restrictions and the opening up of the domestic noncontiguous trades to foreign-flag participation might go far toward solving our high transportation cost problem. This, however, would collide with long-established national policy of attempting to maintain and preserve a healthy merchant marine.

On balance I think it would be better, if possible, to adhere to our policy of subsidizing U.S.-flag vessels, provided that legislation could be developed that would lower waterline freight rates and insure that the benefits of such savings are passed on to the rate-paying public.

In light of factors discussed, I should like to make some general recommendations both about the procedure to be followed in developing curative legislation and with respect to the content of the legislation itself.

First, as to procedure, I should like to take the liberty of suggesting to your committee that it would be extremely worthwhile to undertake several specific case studies without, however, deferring legislative action based on the facts that cannot be established.

I would recommend that the members of your committee and its staff select the principal carrier in each of the noncontiguous trades and actually go back to the beginning of its service and trace its history to date. It would be significant to establish, for example, what equipment was purchased and dedicated to the trade, the price at which such equipment was acquired, the replacement experience of the carrier, the depreciation policies followed, the profits taken from the trade or the losses incurred, the operating problems entailed in maintaining efficient service, the existence or lack of competition and the differential in cost of service between such U.S.-flag lines and foreign-flag lines rendering comparable services. I strongly believe that if such actual case studies were undertaken, it would be possible to gather enough basic data to write legislation that would serve the

needs of the areas involved, protect the legitimate interests of the carriers and take into account the requirements of national defense. I would hope that this case-by-case approach need not take too much time or delay legislation, the need for which is already apparent.

Studies should also be made of the effect on all parties of the institution of cargo van and unitized cargo equipment, and particularly, in the Alaska trade, of the relationship between contract carriers and common carriers of cargo.

As to the form which legislation should take, I would suggest generally:

1. Extension of the construction differential subsidy provisions of the Merchant Marine Act of 1936 to vessels operating in the non-contiguous domestic trades.

2. Payment of operating differential subsidies to vessels engaged in these trades based on a comparison of operating costs incurred in comparable foreign-flag operations.

3. Adoption of realistic rate regulatory standards to insure that the benefits of subsidies are, in fact, passed along in the form of lower rates, with the carriers entitled to a reasonable return on net investment. However, policy standards should be established limiting such fair rate of return to the actual capital investment based on the time actually employed in the common carrier service.

4. Enlargement of legal, accounting, and administrative staff of the Federal Maritime Board, so that adequate help is available to Board members to check statements and documents filed and to analyze and report on significant facts in timely, searching manner.

5. Revision of reporting procedures to show all intercompany and affiliated company transactions clearly in consolidated as well as separate statements of parent holding, subsidiary and affiliated companies.

6. Elimination of the interest-free use of funds subject to refund by the carriers while investigations are in progress in line with practice in other Federal agencies.

7. Extension of the statutory suspension period in connection with rate increase investigations, as contemplated by S. 804 sponsored by Senators Bartlett and Gruening.

8. Except in unusual circumstances, requiring that reports and statement filed by all carriers be available to the public.

9. Establishment of an organized vessel replacement program for the noncontiguous trades through institution of the construction subsidy program with present safeguards against abuse.

10. Certification of the entry into and abandonment of service within the trades on the basis of public convenience and necessity. The carriers should be reasonably protected against uneconomic competition while required to render adequate service at reasonable rates.

I have touched on certain general considerations to be taken into account in developing legislation to correct the shortcomings of present policy. I am confident that legislation embracing these general principles would be of substantial benefit to the carriers as well as to the general public.

It is my sincere belief that the enlightened self-interest of the carriers lies not in increasingly higher freight rates, but in a conscientious effort at lowering rates to stimulate economic development

in the offshore domestic areas. This effort to be wholly useful will require a corresponding legislative effort along lines indicated.

It also seems clear to me that a legislative program to permit the construction of new and modern vessels would serve the best interests of national defense. The vessels in use in the offshore trades were built during World War II. The defense program, if it needs U.S.-flag vessels in these trades, needs vessels that are modern, efficient, and readily available in time of emergency.

It is the purpose of the State of Alaska to state the problem as known and experienced in Alaska—yet as noted earlier in these proceedings, the problem is general to the several areas mentioned and is national in its significance. Its solution requires a change in national policy.

While I do not presume to testify as an expert, I have attended many maritime hearings and I will venture the guess that when all the testimony is in on this occasion from Government, from the carriers, shippers and from the public, it will show in many areas of discussion a unanimity seldom found in a discussion of coastwise maritime matters.

This, I believe, should be cogent and compelling.

Thank you again for this opportunity to appear. The State of Alaska is grateful for your efforts and stands ready to cooperate with your committee in every way.

Senator BARTLETT. Thank you, Mr. Riley.

Do you have any questions, Mr. Grinstein or Mr. Bourbon?

Mr. BOURBON. Just to keep the record straight, where the witness said the carriers have not undertaken new vessels under construction and there has been none, I might observe a group in St. Lawrence have built two container vessels and American Hawaii has asked for mortgage help to build three container vessels at a cost of about \$30 million.

Mr. RILEY. I stand corrected and will ask approval for amendment and revision of my statement.

Senator BARTLETT. Mr. Goding?

Mr. GODING. I have no questions.

Senator BARTLETT. Mr. Riley, your statement noted that in the last 10 years, waterborne freight rates in the Alaska trade have increased 56.4 percent. Those increases are not as great as the rate boosts for Hawaii and Puerto Rico, according to testimony previously supplied to the committee. I suppose as to the effect on the economy, we would have to know the original base upon which the increases were made, but can you tell the committee what the last increase was in percentage terms and when it was applied?

Mr. RILEY. Well, it was applied within the last year and a half, if my memory serves me—relatively recent in any event.

Senator BARTLETT. Let me interrupt you. You have pretty well stated in here the percentages. You said that since January 1958, the increase has been 32.8 percent. That includes the latest?

Mr. RILEY. That includes the latest, that is right.

Senator BARTLETT. Mr. Riley, you have stated that the cost of living in Alaska is higher than anywhere else in the Nation. You have presented some rather horrifying figures in that respect. Earlier,

Commissioner Fernós-Isern, testifying in behalf of Puerto Rico, stated this:

The cost of living in Alaska has been found to be 25 percent higher than Washington, D.C. The cost of living in Hawaii has been found to be 17.5 percent higher than Washington, and the cost of living in Puerto Rico has been found to be 12.5 percent higher than Washington.

In reference to the 25 percent figure for Alaska, is it not a fact that that determination relates only to the upper limit of the so-called cost of living allowance which the Federal Government may pay to its employees in Alaska and does not necessarily relate at all to actual cost of living?

Mr. RILEY. That is true, Senator Bartlett. It bears no relationship to the indexes over the years. There is no one figure that could be reached that is applicable to all of Alaska unless it were an average, but at least according to the latest Ward Index, I find no community has as little as 25 percent, although the Puerto Rican figure corresponds roughly with mine. I have 111.9.

Senator BARTLETT. That is to say that even in Ketchikan, Alaska, which according to this Ward Index, found the cost of living there to be 27.1 percent higher than Seattle, the Federal employee could not be compensated sufficiently under the law to meet that added cost of living?

Mr. RILEY. Not within the 25 percent.

Senator BARTLETT. Is this high cost of living having a detrimental effect upon the present economy of Alaska?

Mr. RILEY. It certainly has, in many ways. The employment of labor by the householder, for example, is rendered far more difficult. The wage rate must bear a certain relationship to the cost of living.

Senator BARTLETT. Mr. Riley, will you speak a little louder, please?

Mr. RILEY. The effect of such higher living costs, the highest in the Nation, are felt in every part of life and endeavor in Alaska because it reaches everyone right at the purse. One could multiply examples. I don't think that is the purpose of the question.

Senator BARTLETT. What has been the main industry, if that is the right description, which I doubt, in Alaska during the post World War II period?

Mr. RILEY. For the last several years it has been the construction industry and in the construction trades you find appreciably higher hourly rates than in most other fixed, hourly rates of pay. In construction, the Federal Government, being the prime builder, has felt at every turn these appreciably greater wage rates to the point where it has cost every builder, including the Government, far more to build in Alaska than it would any place else.

Senator BARTLETT. The Federal Government has been engaged principally in this area in military construction?

Mr. RILEY. Almost altogether military related or military.

Senator BARTLETT. The necessity for building these defensive installations speedily has tended, has it not, to elevate the wage structure faster than otherwise might have been the case?

Mr. RILEY. It has, primarily because of seasonality of the construction period; weather conditions prevent a year around construction program in many areas; the need for haste has been quite uneconomic, I should say, and in turn the wage scales have reflected all these factors.

Senator BARTLETT. Have those wage scales been translated in measure out of economic necessity to the civilian economy? If I don't make myself clear, let me say this. If a given craftsman is paid a given sum on a military construction job, does that tend to force up the wages of the clerks in service industries in a given community close by?

Mr. RILEY. Indeed it does because the amount of money in circulation has a great deal to do with costs as well as with other factors that tend to elevate costs, and the man in the service industry is directly affected by the money going into a community in large payrolls of the construction industry.

Senator BARTLETT. Would it be correct then, in your opinion, to say that the inflation which has been noted throughout the country, particularly, let us say, in the last 15 years, has been felt in Alaska in exaggerated form?

Mr. RILEY. Altogether.

Senator BARTLETT. Then on page 3 of your statement, you said this, and I quote:

Alaska is making great efforts to develop its economy, with particular reference to the development of its natural resources.

Now, is it not true, Mr. Riley, that those resources in large measure or perhaps altogether, must be competitive with like resources elsewhere in this land?

Mr. RILEY. They must. For the most part they are of the extractive industries. We have seen it illustrated in lumber and pulp, in Alaska salmon, competing with foreign-caught salmon. In every respect, when they cannot compete the Alaskan products remain unsold. Transportation is a large element, of course, in getting those resources, those products to market. In turn, the labor costs, which we were alluding to earlier, that go into the extraction or the processing of those resources, compound the problem of competitive position for Alaskan products.

Senator BARTLETT. Would you say the competitive disadvantage for Alaska in the use of these natural resources increases with the spread of the cost of doing business between the other States and the 49th State?

Mr. RILEY. I think that is quite apparent, Senator.

Senator BARTLETT. If Alaska can't develop its natural resources, what can it turn to in aid and abetment of its economy?

Mr. RILEY. The entire industrialization of Alaska is dependent, as I see it, on the utilization and development of its resources: water, mineral, fish, agriculture in lesser degree, and if those resources cannot be utilized and there is any cessation of Federal spending, we will certainly be up against it.

Senator BARTLETT. Then your presentation hinges upon a belief on the part of the State of Alaska that Alaska can play its proper role in the national economy only when it is placed in a competitive position to do so and this cannot be arrived at with ocean freight rates on a constant rise?

Mr. RILEY. Precisely. We are increasingly in a bind of rising costs and competitively fixed prices for the goods we have to sell.

Senator BARTLETT. Mr. Riley, elsewhere and later in your statement, you made specific suggestions which we welcome, but I did note that you would not urge the committee to delay any legislative action

which it might be disposed to initiate until the case studies which you urged had been made. Do you think they are absolutely essential to a determination on the part of the committee as to need for corrective legislation?

Mr. RILEY. I think that there are many areas of substantial agreement from the testimony I have heard in the last 2 days as to which the committee could perhaps proceed at once. Other areas may require the gathering of additional data and I think that the most reliable means of gathering that information will be by case studies of the principal carriers serving each of the trades.

Senator BARTLETT. Have you yourself lived long in Alaska, Mr. Riley?

Mr. RILEY. Some years, 23.

Senator BARTLETT. You live in Juneau?

Mr. RILEY. Yes, presently.

Senator BARTLETT. Do you find that the average citizen is compensated adequately to take care of this added cost of living which is discovered there in one of the most southerly Alaskan cities?

Mr. RILEY. I think in Juneau and most Alaskan communities, life is very marginal in an economic way, that most people just get by, if indeed they stay in the black.

Senator BARTLETT. Aside from Federal employees, for whom special arrangements are made, I have often heard that the Alaskan citizen has a special tax problem because he must get a high income in order to subsist, but he has to pay his income taxes based upon the higher wage or salary rate. Do you believe that is a problem here?

Mr. RILEY. That feeling is generally entertained by non-Federal employees who recognize that they must have a higher dollar figure to subsist, and among those non-Federal employees there is an awareness that living costs to the Federal employee, are no greater or no less than their own, but Federal employees have a cost of living differential which is not taxable and, therefore, is advantageous to the one category. That feeling is natural. In Juneau, for example there are many people in government.

Senator BARTLETT. Take one commodity, for example, do you know the cost of a quart of milk in Juneau?

Mr. RILEY. It varies, about 40 cents now.

Senator BARTLETT. Is that considerably higher than in Seattle, do you know?

Mr. RILEY. I don't know for a fact. I should say it is about double. Now, that is guesswork, just my memory.

Senator BARTLETT. That must make it economically difficult for the parents of small children.

Mr. RILEY. Let me put it on this basis, Senator Bartlett, and this is not a valid comparison because many years have elapsed, but I used to purchase buttermilk for a nickel in Seattle and it is now 35 cents in Juneau. I was struck by the difference.

Senator BARTLETT. This must be an especial problem for the parents of small children buying all this milk.

Mr. RILEY. I think I caught the implication.

Senator BARTLETT. I have no further questions.

Mr. Grinstein?

Mr. GRINSTEIN. Are you having an increase in barge traffic from the United States to Alaska?

Mr. RILEY. I cannot say whether the entire State is having an increase. I do know Alaskan Freight Lines has recently come into Juneau and I don't know of any recent cessation of service elsewhere.

Mr. GRINSTEIN. Are they operating under a Federal Maritime Board tariff?

Mr. RILEY. That I do not know. I just cannot answer the question.

Senator BARTLETT. Mr. Goding?

Mr. GODING. Of industrial cargoes, say in pulp, specifically, how much of the traffic moves on the common carriers?

Mr. RILEY. It is my impression that none does, speaking of the products moving. Now the incoming material for construction of plant probably is another matter. I would suppose that common carriers have brought in a share of the construction materials. I can't tell you of my own knowledge that that is true.

Mr. GODING. The pulp export is mostly on contract?

Mr. RILEY. Yes.

Senator BARTLETT. Thank you, Mr. Riley, and when you return to Juneau, I wish you would convey to Governor Egan our gratitude for having had the State so ably represented at this important meeting.

Mr. RILEY. Thank you, Senator Bartlett.

Senator BARTLETT. We have Mr. Kendall and Captain Beck last on the agenda so I think we can complete our hearing this morning.

Thank you, Mr. Kendall and Captain, for appearing. You may proceed.

STATEMENT OF LANE C. KENDALL, COMMERCIAL SHIPPING ADVISER, ACCOMPANIED BY CAPT. CHARLES B. BECK, USN, DIRECTOR, WATER TRAFFIC DIVISION, MSTs, AND JOSEPH DALY, OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE, INSTALLATIONS AND LOGISTICS

Mr. KENDALL. Mr. Chairman, it is a pleasure to be here. I am representing the Military Sea Transportation Service. I am the commercial shipping adviser to commander, Military Sea Transportation Service. I am here to supply information on the operation of MSTs between the United States and the noncontiguous States and territories of the United States.

I wish to explain very briefly the role of MSTs in the movement of passengers and cargo. By its charter, MSTs is the single manager for ocean transportation for the Department of Defense. It does not generate any cargo of its own, nor does it, under normal circumstances, handle any commercial business. The Army, Navy, Marine Corps, and Air Force are our main customers. They inform us of their requirements for transportation by sea and it is our responsibility to ship them on appropriate commercial or MSTs-controlled vessels.

There are 16 transports in active operation at this time and 1 transport is on loan to the New York State Maritime College. This fleet of 17 transports was determined by the Joint Chiefs of Staff to be the minimum number to be maintained in full operational status to take care of immediate mobilization requirements. Even if these ships are not used to carry troops and dependents they still must be continued in a state of full operational readiness at considerable ex-

pense to the taxpayers, with no compensating return. To benefit in peacetime from the existence of this fleet, the transports are used by the Department of Defense to carry military personnel and their dependents between the United States and military outposts around the world. Fourteen of the 16 transports are fitted to carry dependent women and children in what MSTS calls cabin-class accommodations. Additionally, they have berths for 1,200 to 2,000 troops, depending upon the individual ship. The remaining two transports in operation carry troops and troop officers only, and have a normal capacity of about 3,100 men each. There is no commercial American-flag shipping with the troop-lift capability of these 16 ships. They provide rapid, safe, and economical transportation for large numbers of military personnel, and are essential to the Department of Defense.

About three-quarters of the cargo offered to MSTS by the shipper services, and by that term "shipper services," we mean Army, Navy, Marine Corps, and Air Force, is allocated to American-flag commercial steamship companies. The balance is carried in vessels controlled by MSTS. These controlled ships are predominantly Government owned and MSTS operated, but some of them are chartered from American operators to meet specific transportation requirements. This controlled fleet, insofar as possible, is employed to carry cargo on routes not regularly served by American liner operators, or to handle many cargoes, such as ammunition and unit lifts, which are not truly susceptible of transportation in berth-service vessels, and the Arctic and Antarctic operations.

The operations of MSTS are governed by the 1904 law requiring that American-flag ships be used to transport Government cargoes when American-flag service is available, and by the 1954 law directing that at least half of all military cargo be lifted in American commercial shipping. In addition, the Secretaries of Defense and Commerce signed an agreement in 1954 by which MSTS was directed to support the American merchant marine to the maximum extent practicable. Following these directives, and to keep the nucleus fleet at the smallest size consistent with the responsibilities placed upon MSTS, about 75 percent of our business is channeled to the privately owned American maritime industry.

A basic reason for maintaining the nucleus MSTS fleet is to meet the requirements of the shipper services for transportation of goods on routes where commercial service under the American flag is not adequate in frequency, capacity, or ports of call. For example, from San Francisco, three Government-owned "reefers" are operated for us by an established liner-service company, and serve Hawaii, the Aleutian Islands, Guam, Okinawa, and Japan at approximately fortnightly intervals. The roll-on roll-off ships *Comet* and *Taurus* are operated by MSTS to provide a highly specialized service for the Army. These ships run between New York and France, carrying self-propelled or wheeled vehicles fully loaded with high priority cargoes deemed essential to the military readiness of troops in the European theater. There is no commercial counterpart for these vessels.

I would like to emphasize that MSTS carries only cargo sponsored by the armed services, or appropriate Government departments, and it is constantly working to insure that its nucleus shipping offers minimum competition to the privately owned American merchant fleet consistent with the military mission to be performed. It does provide

an indispensable form of transportation to remote points, such as the Aleutian Islands, Pacific atolls, and the Caribbean outposts, as well as highly specialized shipping service for which there is no commercial counterpart.

We have a continuing concern that there be adequate American-flag shipping service between the continental United States and the non-contiguous territories and States. A substantial volume of tonnage moves under military sponsorship in these trades; we are happy to see it carried in privately owned American ships.

This committee may be interested in the fact that in calendar year 1960 MSTS arranged to move a total of 434,908 measurement tons of cargo from the Pacific coast to Hawaii. Of this, berth-service operators carried 273,447 measurement tons, and MSTS vessels handled the balance of 161,461 measurement tons. A substantial proportion of the MSTS tonnage was aircraft transported in MSTS-operated, cargo-aircraft carriers, for which there is no commercial counterpart. We booked 95,835 tons of cargo by commercial carriers to Alaska, and sent 58,417 measurement tons by controlled ships like the LST-822, which had to discharge much of its loads over the beach. No commercial capability of this sort was available. Also, we sent a quantity of refrigerated cargo by the three reefer ships previously mentioned because there was either insufficient commercial space or the schedules of the commercial carriers were not satisfactory to the shipper services.

Our passenger business to the noncontiguous States and territories is substantial. Except for Hawaii, no commercial passenger ship service to these areas is provided by American steamship lines, and MSTS has filled this gap at low cost to the taxpayer and to the satisfaction of the services whose personnel we have carried.

In fiscal 1960, our passenger business was:

	Outbound		Inbound	
	Cabin	Troop	Cabin	Troop
Alaska (Whittier and Kodiak).....	1,790	1,128	1,590	988
Aleutians.....	271	282	244	647
Guam.....	1,922	1,588	2,294	1,720
Hawaii.....	12,166	4,534	13,981	5,952
Puerto Rico.....	1,503	1,842	2,017	1,678
Total.....	17,652	9,374	20,126	10,985

Since September 1960, because of the restrictions on travel funds in the military departments, they have not booked any commercial passenger space through MSTS.

In summary, may I say that the Military Sea Transportation Service, as the single manager for ocean transportation for the entire Department of Defense, has a keen interest in all matters relating to the economic well-being of the privately owned American merchant fleet. It desires that there be as extensive American-flag service as is determined to be economically feasible. It is constantly aware of the importance to the American merchant marine of military-sponsored cargo. Under the concept establishing the single manager for ocean transportation, efficiency and economy must be sought by MSTS at all times. We want the lowest possible transportation rates we can

negotiate with the carriers, but we accept the fact that these rates must be fair and reasonable.

Senator BARTLETT. Thank you, Mr. Kendall.

Do you have any questions, Mr. Grinstein?

Mr. GRINSTEIN. Mr. Kendall, it has been stated during the course of the hearing that the cabotage laws which restrict trade between the domestic noncontiguous areas and the main United States are supported mainly by national defense reasons. They want a ready reserve of ships available. Is this consistent with the thinking of the Department of Defense and Department of the Navy?

Mr. KENDALL. Yes, sir; we need an immediately available fleet of merchant-type vessels which can be mobilized in the event of emergency and the existence of these ships in the restricted trades is, of course, a mobilization potential. We are concerned, however, in the decline of ships in the protected trades.

Mr. GRINSTEIN. Mr. Kendall, Mr. Stakem, in behalf of the Federal Maritime Board said the Board is constantly in contact with the Department of Defense in being advised as to how many ships are needed. Could you tell us how many American-flag ships are required under domestic noncontiguous trade for defense purposes?

Mr. KENDALL. No, sir; I have not made a study along that line.

Mr. GRINSTEIN. Could we get that material for the record?

Mr. KENDALL. I will try, sir, and see if we can find it. It may be classified material, sir, but I will see that it gets out.

Mr. GRINSTEIN. Thank you.

During the course of the hearing, it has been pretty clearly developed there is a conflict between the needs of the carriers for higher rates to meet operating and replacement costs and, on the other hand, the need on the part of the noncontiguous areas for either stable rates or lower rates. If the rates were to remain the same then the carriers would not be in good economic health. If the rates continue to go up, then the areas served will be penalized. Does the Department of Defense or Department of Navy have any recommendations to make to the committee which might be helped in resolving this impasse?

Mr. KENDALL. I think that properly belongs in the field of maritime policy and should be stated by Mr. Stakem as the Chairman of the Maritime Board. They make the policy in that regard; we do not.

Mr. GRINSTEIN. Mr. Stakem is advised as to how many ships are required for national defense purposes in this trade?

Mr. KENDALL. I assume so.

Mr. GRINSTEIN. Would the Department of Defense or the Department of Navy have any objection to allowing foreign-flag ships into domestic noncontiguous trade; in other words, opening up our cabotage laws?

Mr. KENDALL. This is a matter of high policy, sir, and I do not think I am in a position to make a statement. This is a Defense Department position and, frankly, I didn't know that was one of the question which might be asked, so I did not clear that with the Department of Defense.

Senator BARTLETT. Parenthetically, I might say, you never know what questions are going to be asked here and neither do we.

Mr. GODING. I have a question that is somewhat related. You say that the Department of Defense has a keen interest in matters relating to the economic well-being of the privately owned American

merchant marine—this is the whole merchant marine—and desires there be as extensive American-flag service as is determined to be economically feasible. I would think that the interest of the Defense Department would run a little bit beyond what you might call bed-rock economic feasibility or we might not have a merchant fleet of any description. Do you have any comment?

Mr. KENDALL. The Department of Defense, sir, is concerned that there be a merchant fleet under the American flag which can be mobilized in the event of emergency. The Department of Defense is not a subsidizing organization; it does not make national defense policy with regard to the merchant marine, its size or the amount of money which the Government is prepared to advance to keep this merchant marine in existence. Therefore, the matter of the size of the merchant marine and amount of subsidy to be paid which would involve this matter of economic feasibility is something which probably is determined by the Maritime Board.

We do realize, of course, that there are economic limitations on the size of the merchant marine which the Defense Department might like to have in the event of mobilization. We are deficient, for example, in the number of passenger ships which are in commercial operation at the present time viewed from the mobilization standpoint. We are not authorizing anybody to build ships at the Department of Defense expense.

Mr. GODING. The fundamental purpose behind the existing subsidy program is maintenance of a fleet irrespective of economic feasibility. That is the only thing I wanted to bring out. There are certain defense goals, certain mobilization requirements and they cannot be weighed on the scales of economic feasibility or we might be in a bad situation.

Mr. GRINSTEIN. Mr. Kendall, when you are supplying material for the record, I wonder if you could also supply the views of the Department of Defense or the Department of Navy on the increasing use, as we understand it, of tug and barge service between mainly the United States and Alaska, as to the utility of these tug and barges in the event of a national emergency as opposed to the utility of self-propelled vessels presently serving?

Mr. KENDALL. I will do my best to comply with that, sir.

Senator BARTLETT. Mr. Kendall, you said in your statement that under normal circumstances, the MSTs doesn't handle any commercial business. I take it that you do so under the most extraordinary circumstances when an emergency arises?

Mr. KENDALL. This is correct, sir. In any event, the commercial cargo which we would handle would have to be authorized by a Government department, which in turn would ask the Department of Defense to sponsor it to us so that we, in no way, set up a commercial competition with the carriers.

Captain Beck has a comment in this regard.

Captain BECK. I think the best example, and I am not sure of the dates, but some years ago, there was a strike in Hawaii and the military department, the Department of Defense, did transport in MSTs vessels considerable food products for Hawaii.

Senator BARTLETT. Upon a determination that an emergency had arisen?

Captain BECK. That is correct.

Senator BARTLETT. Mr. Kendall, on page 5, you noted tonnage to Alaska and said 58,000 tons plus had been sent up there by controlled ships like the LST-822, and, of course, that was a very large proportion of the total tonnage, because commercial carriers didn't carry twice that amount, only 95,000 tons. This is my question, did all of that LST cargo go to situations like those found in the Aleutians?

Mr. KENDALL. The figures which I have here, sir, were for the calendar year 1960. At that time, the LST-822 was carrying cargo into Whittier and discharged over the beach. The volume of tonnage which this particular vessel handled was about 7,500 tons. The rest of the cargo was refrigerated cargo which was taken up to the Aleutians by these controlled reefers, which are operated for us by a commercial carrier.

Senator BARTLETT. I am wondering why an LST would be put into Whittier because commercial ships are available for service there, or were available for service there, when the Army controlled the facility. They had a big dock. They didn't have to land over the beach.

Mr. KENDALL. It probably, sir, lay in the nature of the cargo. It might have been very heavy, wheeled equipment, engineer equipment, which could not be lifted out of the ship with the facilities available either at the port or with the ship which might possibly have been nominated for the job.

Senator BARTLETT. I wonder if you would be good enough to file with the committee a supplementary statement relating to the LST-Whittier operation?

Mr. KENDALL. Certainly, I will be glad to.

Senator BARTLETT. Now, going back to the question raised by Mr. Grinstein, which is essential to our study and inquiry and action, if any, I take it that you gentlemen are here merely to inform us of the operations of the MSTs and cannot go into policy decisions that might involve, for example, the size of the fleet needed in the event of national defense?

Mr. KENDALL. This is correct, sir.

Senator BARTLETT. Of course, we will have to know, it is essential that we know how close to the goal the U.S.-flag fleet engaged in foreign trade is to the need in case of a national emergency; the value, if any, of a larger domestic offshore fleet in being and other considerations which would have an essential bearing upon this subject. I don't know that we should properly ask you to obtain this information for the committee in open session or otherwise because that may not be your province, but in any case, this the committee must know before it can even hope to proceed.

Mr. KENDALL. Mr. Bartlett, I have just been informed by Mr. Daly from the Office of the Assistant Secretary of Defense, that it is his opinion that the Chief of Naval Operations has written recently to Senator Butler, giving him this type of information. We will look into this, sir, and find out about it.

Senator BARTLETT. This was a personal letter to Senator Butler?

Mr. DALY. Yes, sir.

Senator BARTLETT. Then, I take it, the information is not classified?

Mr. DALY. Certain of the questions you have asked, sir, are definitely classified, but general conclusions as to the overall adequacy of elements of the merchant marine would not necessarily be classified.

Senator BARTLETT. I suggest that since these hearings are going to be resumed at a later date, the committee will require this information, and perhaps some of it you would be willing to give us in executive session, if necessary. But in any case, we will have to have it before we hope to legislate and we will have to have it broken down, as Mr. Grinstein suggested to me, with special reference to the off-shore areas, the very problem with which we are dealing.

Mr. DALY. If I can offer, sir, I believe the technicians in our office would be very happy to consult with your staff as to what type of information can be acceptable to you and readily made available.

Senator BARTLETT. These are welcome words.

Thank you, gentlemen, very much for your appearance.

Mr. KENDALL. It has been a pleasure to be here, sir.

(The following letter was subsequently submitted for the record:)

DEPARTMENT OF THE NAVY,
MILITARY SEA TRANSPORTATION SERVICE,
Washington, D.C., March 28, 1961.

HON. WARREN G. MAGNUSON,
Chairman, Senate Committee on Interstate and Foreign Commerce,
New Senate Office Building, Washington, D.C.

MY DEAR SENATOR MAGNUSON: Pursuant to the request of Senator Bartlett made to Department of Defense representatives, I am happy to supply to your committee the following information relating to the movement of military passengers and cargo to noncontiguous States and territories:

The first question was: "What was the nature of the cargo carried to Alaska in noncommercial ships in calendar year 1960?"

In calendar year 1960, the Military Sea Transportation Service (MSTS) transported in MSTS-operated or MSTS-controlled ships a total of 58,417 measurement tons (M/T) of cargo destined to Alaska and the Aleutian Islands for the Department of Defense (DOD). This tonnage was divided in this manner:

	Measurement tons
Household goods and general cargo.....	32,727
Vehicles (including privately owned cars).....	21,328
Aircraft.....	277
Ammunition.....	901
Refrigerated cargo.....	3,184
Total.....	58,417

This cargo was not subject to shipment in common-carrier vessels for a variety of reasons, such as priority of delivery which did not permit waiting for the next commercial ship; "unit lift," meaning the cargo of a military organization which had to move at one time; exceptionally heavy cargo beyond the capability of the commercial carriers to handle; delivery to points when berthing facilities for conventional shipping either were inadequate or nonexistent, and lack of commercial service to outlying destinations. The following analysis will explain these points:

	Measurement tons
"Reefer" cargo to Aleutian Islands.....	3,184
Mobile Construction Battalion (MCB) 9, unit lift to Adak.....	6,056
MCB moves to Adak and Kodiak.....	1,865
Locomotives (extra-heavy lift) on USNS <i>Brostrom</i>	2,805
Locomotives and heavy-lift vehicles to Kodiak and Adak on USNS <i>Gammon</i>	4,818
Cargo carried in USNS <i>LST-822</i> , including heavy engineering equipment for over-the-beach delivery.....	13,057
Total.....	31,785

The second question was: "What is the Navy's opinion as to the practicability in wartime of barge operations for transportation of cargo to Alaska and Puerto Rico?"

The complete answer to this question involves two separate considerations. First, the construction and use of barges to supply these noncontiguous areas would require considerably less steel per ton of cargo carried than self-propelled vessels. The expansion of existing barge service in time of war also would release for oversea operation oceangoing ships which otherwise would have to be assigned to service the noncontiguous areas. The military desirability of using barges would depend on the nature of the cargo requiring transportation, the schedule which could be followed by a barge service, the availability and capability of tugs, the capabilities of the barges themselves, and the cargo-handling facilities in the ports of call.

The second consideration encompasses the vulnerability of a barge-tow to submarine, surface, or air attack. The characteristics of such an ocean tow do not permit any evasive action, and its low speed makes it a prime target for hostile attack. The element of luck in accomplishing the voyage must enter into the planning of transoceanic barge operations to greater extent than for self-propelled equipment.

Despite these reservations, the DOD interposes no objection to the continued development of barge transportation from the United States to the noncontiguous States and territories.

The third question was: "What is the position of the DOD on the use of foreign-flag shipping in trades between the main and noncontiguous States and territories of the United States?"

The DOD does not favor the admission of foreign-flag shipping into these trades. The volume of cargo generated at any given time on a specific route will support only so many ships. To introduce foreign ships would broaden competition, and would mean a reduction in American ships. Such a reduction would be contrary to DOD desire for a strong and substantial American merchant marine.

The fourth question was: "What is the DOD position on the adequacy of the American merchant marine for mobilization purposes? How close to the goal of readiness for an emergency does the present U.S.-flag fleet come?"

In the most recent study made of transportation requirements and capabilities for emergencies, the DOD concluded that the American merchant marine was not sufficient to meet minimum needs of the DOD. When ships of foreign (Panama, Honduras, Liberia) registry but owned by American citizens and under effective U.S. control, are counted along with American-flag tankers, the tanker fleet becomes marginally adequate. Dry cargo types and passenger ships were found to be inadequate, both in numbers and in quality. A comprehensive resurvey of transportation requirements is now underway and is to be completed this summer. A definitive answer to the question can better be made after study and analysis of this survey.

The fifth question was: "What is the DOD position as to the number of ships that should be assigned to the trades between the mainland and noncontiguous States and territories?"

The DOD regards the ships assigned to these trades as particularly valuable because of the probability that most of these ships will be relatively close to our shores at all times and thus readily available in an emergency. No attempt has been made, however, to express this desirability in a numerical formula. We regard all American-controlled ships as desirable for national defense purposes.

Sincerely yours,

ROY A. GANO,
Vice Admiral, U.S. Navy,
Commander, Military Sea Transportation Service.

Senator BARTLETT. Since Puerto Rico and Alaska and MSTs have been heard from this morning, the committee will stand in recess until 10 a.m. on Monday, the 13th of March.

Thank you all for appearing.

(Thereupon, the hearing was adjourned at 12:30 p.m., to reconvene on Monday, March 13, 1961, at 10 a.m.)

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DOMESTIC OFFSHORE SHIPPING

MONDAY, MARCH 13, 1961

U.S. SENATE,
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
SUBCOMMITTEE ON MERCHANT MARINE AND FISHERIES,
Washington, D.C.

The subcommittee was called to order, pursuant to adjournment, at 10:15 a.m. in room 5110, New Senate Office Building, Hon. E. L. Bartlett presiding.

Senator BARTLETT. The committee will be in order.

This is the third day of hearings on the problems of ocean trading with Alaska, Hawaii, Puerto Rico, and Guam. Previous witnesses from the areas concerned and Government offices have very ably set out issues of concern to the committee.

Today's testimony will be from the carriers operating in the trade between the mainland States and offshore States and territories. Views and materials recorded in this hearing will provide the committee with another side of a complex story.

Let me say to you gentlemen who have come from so far away, and those who have come from near points, I wish to express the thanks of the committee for your having taken time out from busy schedules to come to Washington and appear before us. This is certainly an indication of the importance of the problems, as well as the spirit of cooperation needed for a solution of them.

The first witness this morning will be Mr. Randolph Sevier, president of the Matson Navigation Co. We are glad to have you here, Mr. Sevier. You may proceed as you desire.

STATEMENT OF RANDOLPH SEVIER, PRESIDENT OF THE MATSON NAVIGATION CO.

Mr. SEVIER. Mr. Chairman, I am Randolph Sevier, president of Matson Navigation Co. I wish to express my company's sincere appreciation to the committee for the opportunity of presenting our views on Hawaii's domestic ocean shipping system and its problems.

This is a large and complex subject, not only vital to Hawaii and the steamship companies in the trade, but to the Nation as well. To cover it adequately requires a presentation of some length and detail. The principal points, however, are briefly reviewed in this summary statement, with supporting statistics and narratives contained in an appendix. We respectfully request permission to file a supplementary statement later to cover points raised in the 2 previous days of hearings which are not touched upon here.

(See letter of Mr. Pessel, p. 324.)

Senator BARTLETT. If there is no objection, that permission is granted.

Mr. SEVIER. Thank you.

There are six principal points in this presentation:

First, the present vigorous character of Hawaii's economy.

Second, the essentiality of regular, dependable steamship services to an island State, as has been provided by Matson.

Third, the impact on Hawaii's economic well-being of freight rates required to maintain such regular service.

Fourth, the aspects of Hawaii's shipping system which makes its strength and adequacy matters of national concern.

Fifth, the specific problems faced by Matson, the principal carrier in the trade for nearly 80 years.

Finally, some areas where Hawaii's ocean shipping system may be strengthened by assistance from the Federal Government.

I. The Hawaiian economy is vigorous and growing: Hawaii entered the decade of the 1960's as the Nation's newest State and brought into the Federal Union a strong economy. During the past decade, in particular, this island economy has experienced a growth unprecedented in its history and matched by few other areas in the United States. In a recent freight rate hearing, Gov. William F. Quinn said, in part:

These islands have recorded remarkable economic advances in the past decade. And there is no doubt that the pace of growth has quickened substantially since Hawaii became a State and that our economy will continue to grow at an accelerated pace during the next 10 years. Upon the growth of the economy are based our hopes for higher standards of living for our people.

And in the same proceeding, State Senator Randolph Crossley, of the State of Hawaii, said:

The growth of the territory, and now the State of Hawaii, as a whole over the past 10 years has been a healthy, substantial, and steady growth.

A few statistics give some idea of the magnitude of this growth. Between 1952 and 1958, gross production of the State increased from \$1,141,304,000 to \$1,400 million. The average annual rate of growth was greater than that of the mainland. Total personal income increased from \$893 million in 1954 to an estimated \$1,209 million in 1959, an increase of 44.5 percent, compared to a 34.5 percent increase nationally.

Per capita income in Hawaii has also been rising, the rate of growth being about the same for the United States as a whole. It is virtually at the national average, despite the fact that the percentage of persons below usual employment age is materially greater in Hawaii than in the Nation as a whole. This has the effect of depressing abnormally the indicated per capita income. Among the 50 states, Hawaii ranks fourth in annual output per farm worker, seventh in per residence use of electricity, and eighth in life insurance per capita.

Dr. James H. Shoemaker, director of business research, Bank of Hawaii, a recognized specialist on the general economy of Hawaii, in 1960, commented on the future status of the economy as follows:

I would say that there is in my view no question but what there will be a substantial advance in this economy.

And Dr. Thomas K. Hitch, director of the department of business research, First National Bank of Hawaii, also a recognized expert in this field, in his study entitled "A Brief Review of Hawaii for the Businessman," said he expects the per capita income in Hawaii to continue to grow at about the national rate. According to him, Hawaii "is to the businessman a prosperous (3-percent unemployment rate), affluent, modern, progressive, and diversified economy."

Perhaps the most recent comment on the State of Hawaii's economy is contained in a report by Dean Witter & Co., investment bankers, dated February 20, 1961, which, in part, said:

Hawaii's rate of growth in the past 5 years has been nearly twice that of the U.S. mainland, and about on a par with that of California. Moreover, the dynamic forces in the Hawaiian economy have remained strong enough to overcome the downpull of the current mainland recession and to push business in the 50th State further ahead, even though at a slower pace than in 1959 and early 1960 * * *.

Therefore, it is not surprising to find the islands' 1960 retail sales 11.3 percent ahead of 1959, as compared to a lean 2-percent increase on the mainland, and unemployment at a low 3.4 percent of labor force, as against a recent 6.8-percent recession figure for the United States * * *.

The full account by Dean Witter is attached as exhibit No. 1.

II. Matson's essential Hawaiian service: Hawaii, it must be remembered, is a unique State. It is the Nation's only island State, separated from the other 49 by 2,100 nautical miles of ocean. It is almost totally dependent on commerce with other areas, mostly the mainland United States, to support its vigorous and growing economy. This commerce moves, and for the foreseeable future must continue to move, by but one means of transport—ocean shipping.

A Dean Witter & Co. special study in 1960 describes Hawaii's economic profile, in part, as follows:

Insufficiently endowed with raw materials, these small islands could never have attained a high living standard on the basis of a self-contained economy. Both economics and politics worked powerfully toward transforming Hawaii from a primarily agricultural self-contained economy in the early 19th century into an economy highly specialized and fully integrated with the mainland's economy in the 20th century. Hawaii has been the perfect illustration of an economy concentrating on its best potentialities, thereby raising its living standards to about the level of the larger area it primarily serves, namely the United States.

The islands' commanding geographical location, their good soil and climate, and their scenic beauty have become the main determinants of their economic destiny. The same is true, in a negative way, for their principal weaknesses—the lack of ores, coal, and minerals, and of a domestic mass market. The result to date has been an economy highly specialized in certain services—primarily defense and tourism, and in some agricultural specialties—mostly sugar, pineapple, and related food processing industries with limited activity in other fields of manufacture. Ancillary services such as public utilities, transportation, and banking have developed in step with the islands' economy and are up to modern mainland standards.

And Dr. Shoemaker, in a 1959 report on Hawaii, says:

The integration of Hawaii's economy into that of the United States is not new. It began more than a century and a half ago with the early trade relations of American sailing ships that stopped in Hawaii for provisions and sandalwood en route to China. Trade gradually rose until 1872. Thereafter, with the growth of sugar exports (and later the admission of Hawaii as a Territory), commercial, financial, and trade relations expanded at an accelerating pace—never more rapidly than during the past decade.

From the beginning, the growth of the economy of the islands has been directly geared to such expansion. Hawaii's last decade as a Territory thus has been

the gréatest decade of growth in production, income, and employment. In some ways, Hawaii is today as fully integrated into our national economy as is any State.

At this point it would seem proper to ask: What has been the character of the ocean shipping service that has made possible this integration of an island economy with the mainland United States?

Hawaii has received, for the most part from Matson as the principal carrier in the trade for nearly 80 years, frequent, dependable, and specialized steamship service which has connected the islands to the Pacific, gulf, and Atlantic coast ports, making it possible to market its two principal products—sugar and pineapple—and in turn to obtain from the mainland United States the goods it has needed to support its growing population, its tourist industry, the vast Defense Establishment, as well as its basic agricultural economy.

Through the years the Matson freighter fleet has had many configurations. Today it consists of 20 cargo vessels, including 6 C-3's with capacity for 75 containers on deck, the all-container C-3, *Hawaiian Citizen*, which carries 408 containers, 2 elongated C-4's, the *Californian* and *Hawaiian*, each with a capacity for 286 containers and which carry bulk sugar (16,000 tons) and molasses (3,000 tons) from Hawaii to California. Frequency of service from mainland U.S. ports is geared to tonnage requirements. From San Francisco, sailings average nearly three per week. From Los Angeles, service frequency exceeds one sailing per week, and from Northwest ports there is a sailing approximately every 2 weeks.

Matson and Isthmian Lines, under a joint service, provide a 14-day sailing frequency between Hawaii and Atlantic coast and gulf ports, and a 28-day frequency to South Atlantic ports from Hawaii.

In 1960 Matson operated 247 round freighter voyages between the continental United States and all the ports in the Hawaiian Islands. These vessels, averaging a call at Honolulu every 1½ days, carried a total of 3,893,000 revenue tons during the year.

In addition to those voyages, we made 58 round-trip voyages with our passenger liners, the *Lurline* and *Matsonia*.

No other island community of comparable size and remoteness enjoys such a regularity and frequency of service as Hawaii receives from Matson.

As a result, in the postwar era the Matson freighter has become Hawaii's floating warehouse. Goods, in large volume, go directly from mainland warehouses to shipside, and from the docks in Hawaii to store shelves, eliminating multiple handling, reducing inventories and costly warehousing. In land-scarce Hawaii, the diminution of the need for warehouse space as well as the elimination of costly multiple handling, and other costs inherent in large-scale warehousing, holds down the price to the ultimate consumer. If such frequent service should cease, these benefits would cease.

III. The impact of freight rates: Keeping in mind both the State of Hawaii's economy and the principal freight service that sustains it, the following questions appear proper to explore: What has been the impact of the freight rates? Have they constituted a burden on the economy?

It would appear quite obvious that, to date, the level of rates for Hawaii's essential freight service have not had a serious, adverse effect on the economy.

Proof of this is found in the vigorous growth of the economy during the past decade. The reason freight rates have not retarded growth is simply that, contrary to assertions heard from time to time, the ocean cost of transportation is not a large part of the retail price at which common household items are sold in Hawaii.

For example, of the average 1959 Honolulu retail price of a 1-pound can of salmon (66.3 cents), the freight rate accounted for 2.01 cents; of the price of a pound of coffee (98.6 cents), the freight rate accounted for 3.7 cents; for a No. 303 can of peas, the average price was 25.4 cents, the freight cost, 1.87 cent; for a 12-ounce can of lunch meat, the average price was 55.8 cents, the freight cost 1.73 cents. Other examples are shown on exhibit No. 3, attached.

While freight rates have risen, on the average, 150 percent since 1946, the added cost, when placed against common commodities that go into most Hawaiian homes, it is not large nor burdensome. For instance, these increases from 1946 on some common commodities are as follows: about three-fourths of a cent on a pound of rice, a No. 1 can of soup, and a pound of potatoes, and about 2 cents on a pound of coffee. The appendix contains several exhibits on this subject so it is not necessary to burden the committee with further statistics. Exhibits 2 and 4 contain some very interesting information.

We are aware that its residents may consider Hawaii to be a high cost of living area.

However, Dr. Hitch, in the study referred to earlier, commented upon the question of whether Hawaii is a high cost of living area by reason of its remoteness and dependence upon transportation from the mainland, in the following statement:

Most businessmen and economists who have been faced with this question have concluded that lighter clothing and no winter clothes, the need for less substantial housing and no heating, and the ready availability of attractive and inexpensive recreational areas counterbalance, largely if not entirely, the higher cost of imported consumption goods and the higher value of residential land.

Of 10 mainland cities, according to consumer price studies, 9 experienced larger increases in consumer prices than Honolulu did for the period 1947-49 to 1960. This is covered in greater detail in exhibit 4-A.

In any event, the price and freight rate data shown in the exhibits indicate that the effect of ocean freight rates on Hawaii's cost of living has been overemphasized.

Since Hawaii's cost of living, however, is a much debated and much misunderstood topic, it may be a proper endeavor to have a study made of the impact of transportation costs on the cost of goods to the ultimate consumer in Hawaii. I have noted with interest that such an inquiry—the relation of freight rates to the cost of offshore living—has been mentioned by another witness and has been the subject of committee questioning. It certainly appears to be a logical area of committee interest.

IV. Hawaii shipping is of national concern: Now I would like to take up the fourth point—the aspects of Hawaii's shipping system which makes it eminently in the national interest, which has been touched upon by nearly every witness at this hearing. Matson Lines fully supports the national policy expressed in the Merchant Marine Act of 1936, concerning domestic ocean transportation.

This policy says that the United States should foster the development and encourage the maintenance of a merchant marine sufficient to carry and maintain the flow of its domestic waterborne commerce at all times, capable of serving as a naval and military auxiliary in times of or in national emergency, owned and operated under the American flag and manned by U.S. citizens insofar as may be practicable, and composed of the best equipped, safest and most suitable types of vessels constructed in the United States.

This is the policy which Matson, as Hawaii's privately owned principal carrier, has followed consistently. We believe it is sound and should be continued.

Certainly the well-being of the 50th State, which supplies 10 percent of the Nation's sugar, and 75 percent of its pineapple, supports a key Defense Establishment, utilizes about \$500 million worth of goods annually from many of the States on the mainland, is of concern to more than just its 630,000 citizens, including the military. Because ocean shipping is so fundamental to the strength of the economy, it is most commendable that this committee of Congress interest itself in the problems.

A modern, efficient domestic freight fleet, not subject to being bottled up in foreign ports in time of war, is of vital importance to the Nation's defense posture. The history of the Matson fleets in World Wars I and II is ample evidence of the role this branch of the Nation's maritime industry has played, and must continue to play, in the Nation's emergencies.

President Kennedy, then Senator Kennedy, in a letter dated June 29, 1960, to Senator Magnuson, emphasized the importance of the domestic merchant marine of this country when he stated:

When the United States entered World War II, the domestic merchant fleet was taken over almost in its entirety by the Government, for military logistics purposes. In any future emergency the need for such a fleet, ready at hand to serve defense needs, would be equally urgent. But there may not be any such fleet to requisition, from present indications, if we stand idly by.

If the domestic merchant fleet, so strategic to the Nation's economy and to its defense, is to be kept alive—and it must be—Government must lend a hand.

V. Matson's problems in the Hawaiian service: From this broader view of Hawaii's shipping problems, I would like to channel your attention to some of those faced by Matson, as the States' principal ocean freight carrier.

One that Matson shares with U.S. industry in general is that of spiraling costs of doing business.

The two principal elements of freight service costs are cargo handling and vessel operating. Cargo handling is the largest, amounting to about 48 percent of the total cost of moving Hawaii's commerce. This is followed by vessel expense which, including depreciation, averages about 39 percent. The principal component of these expenses is labor, which accounts for approximately 56 percent of total cargo handling and vessel expense. Unlike the foreign commerce of the United States, which involves low cost cargo handling in foreign ports, domestic commerce is burdened with high cost handling at both ends of the voyage. Expensive cargo handling equipment and terminal facilities are also required in both places. Cargo handling expense per ton, including labor and other costs, increased 167 percent from 1946 to 1961. Although there have been some price fluctua-

tions, bunker fuel oil prices have been moving upward materially during the past decade. And our war-built freighters, which have been operating from 16 to 18 years, each year become more expensive to maintain. Vessel operating costs per day since 1946 to date have increased 115 percent.

Because labor has been such a large part of our increased cost problem, Matson, in concert with much of American industry, has sought, where possible, to replace labor with capital when such programs would mean suitable savings.

This is not always an easy course, for it brings in its wage sociological and financial problems of some magnitude. Two examples of how Matson has tried to relieve the pressure of the growing cost burden are the freight container service and the all-auto carrier.

In the fall of 1956 Matson Lines organized the first integrated research department at the top management level of any American-flag steamship company. This was done in recognition of the need for careful study of the cause and effect of postwar cost increases, and the necessity for practical measures to stem the tide of further cost increases. Matson's long history of maritime innovation in the Hawaiian trade has been stimulated not by competitive forces, but by or sincere interest in Hawaii's continuing welfare.

Our research department's analysis of the cost of providing Hawaii's ocean transportation indicated that cargo handling of general merchandise moving from the Pacific coast to Hawaii offered the most important opportunity for reduction of expenses. This led Matson to pioneer its present large scale containerized shipping service between San Francisco, Stockton, and Los Angeles port areas in California and Honolulu.

Cargo may be loaded and sealed in a container at a shipper's warehouse in a California port area, and the goods not touched until the container is unsealed and unloaded at the consignee's warehouse in Honolulu. The resulting savings in cargo handling, vessel operations, damage and pilferage have enable Matson to name container rates below the rates charged for carriage of cargo in conventional loose stowage.

In exhibit 4-B, we have compared actual freight charges paid to Matson by the shipper on typical container service shipments with what his costs would have been for carriage in loose stowage. Since the container rate includes pickup service, wharfage, and insurance, in addition to ocean haul, these items are added to the ocean rate for conventional service, which does not include them. The savings shown in exhibit 4-B range from over 13 percent to above 31 percent.

Matson's present investment in this container system, including ship conversion costs and lease obligations on containers and chassis, now totals \$17,800,000.

The carriage of automobiles in the Hawaiian trade posed special problems for manufacturers and dealers as well as for Matson.

In January 1961 Matson completed conversion of the C-3 type SS *Hawaiian Fisherman* and placed into service the Nation's first oceangoing automobile carrier. This "floating garage," designed by our own engineering staff, will sail throughout the year on a 14-day turnaround, carrying up to 464 automobiles on each voyage from San Francisco and Los Angeles to the islands. This is covered in greater detail in exhibit 5.

These two problems—rising labor costs and the need for offsetting technological improvements—are subordinate, however, to a third: the inability of Matson to produce a fair and reasonable return to its shareholders in rendering the scope of service with the specialized equipment the Hawaiian economy requires, while at the same time providing for an adequate ship replacement or modernization program.

From 1952 through 1960, earnings on our combined Pacific and Atlantic-Gulf Hawaii freight service operations have averaged but \$800,000 annually. Actual losses were suffered in 1952, 1959, and in 1960. On the average, during the past 9 years, these earnings have been at about one-fourth the level found reasonable by the Federal Maritime Board in docket 808, decided in December 1957 after 1 year of hearings.

It is obvious that such a low earnings record will make difficult the replacement of the present fleet, even by conversion or modernization of older vessels, let alone by construction of new freighters. To replace the present Matson fleet employed in the trade is a staggering financial undertaking. The cost of new construction, depending on vessel types, would range from \$178 million to \$268 million. This is covered in greater detail in exhibit 6.

In September 1959 Matson filed a rate increase, following the standard of reasonable earnings laid down by the Board in docket 808. The Federal Maritime Board permitted the increase, docket 869, to go into effect, subject to investigation, with the proviso that any portion finally disallowed be refunded to the ratepayers. Hearings were held in four cities. They were lengthy and costly, not only to Matson, but to the Board and to the public. The case is now submitted for decision. The cost and consumption of personnel time of such hearings are understandable, but pose added burdens for a regulated company.

At this time it seems well to mention that we are filing for a further rate increase of 10 percent within the next several days, even though our previous request is still to be decided by the Federal Maritime Board. The 10-percent increase is necessary to offset operating losses caused by increased operating costs which have occurred since September of 1959. In 1960, for example, Matson lost \$35,000 before taxes on its Hawaiian freight service on a gross revenue of \$71 million. Obviously we cannot continue to operate this service at a loss.

Under present conditions, Matson, as Hawaii's principal freight carrier, does not rate high as an investment risk.

Investment risk characteristics of Matson's freighter operations in Hawaiian service include the following:

1. The earnings record of freighter operations in Hawaiian trade does not reflect financial soundness and is not conducive to attraction or retention of capital.
2. Matson's freighter operations have been subject to competition, strikes, steadily increasing costs, and a lag in rate adjustments following wage increases.
3. During the past 9 years, Matson has retained, on the average, only 1½ cents out of each freight revenue dollar.
4. Matson's prospects for significant growth in net revenue-producing tonnage are limited by lack of any prospect of material growth

in exports from Hawaii to the mainland. We have attached as exhibit 7 some further information on this point.

The final Hawaii trade shipping problem I wish to set before the committee involves our passenger liner service. The *Lurline* and *Matsonia* are the last nonsubsidized liners flying the U.S. flag. They provide, in our estimation, not only an essential service to Hawaii's tourist industry, by giving tourists the choice of more than one mode of transportation, but are of vital importance to the U.S. defense posture. Both ships served notably as troop transports in World War II, are popular first-class modern vessels, and could again serve the Nation in any emergency.

The principal problem with these liners is the apparent lack of concern for their defense importance exhibited by the military. In September of 1960, after very short notice, approximately \$1 million worth of Government business, on which the company had based its annual operating income for the balance of that year, was suddenly withdrawn. Efforts to date to restore this traffic to these vessels have been unavailing. For the past several years we have enjoyed approximately \$3 million worth of Government business, being principally the dependents of military personnel moving between Hawaii and California ports.

The same kinds of high-cost operating problems detailed earlier also affect these two liners. The question of maintaining them both in the Hawaiian service in the face of these costs is a most serious one—and one to which Matson still does not have a suitable answer. Part of it rests with the Government. There is a narrative attached as exhibit 8 which goes into this in greater detail.

Before taking up the final item—areas of possible Federal assistance—I would like to summarize the principal points I have made about Hawaii's ocean shipping system and its problems:

Hawaii, as the Nation's only island State, is unique in that it must depend almost entirely on ocean transportation for the transport of its essential commerce.

Hawaii's economy has grown and prospered because this ocean transportation system has provided a pattern of schedules, ships, and specialized equipment, geared to the specific needs of its island economy.

Matson has been the principal carrier in Hawaii's ocean transportation system, investing private capital for more than 75 years to assure its continuance, but in recent years has not been able to earn a suitable return.

Emerging problems are of such a nature that the future course and development of Hawaii's ocean transportation system appear to be increasingly matters of national interest.

Matson has embarked on several programs designed to reduce the pressures of rising costs. All require substantial capital. The prospect for attracting added new capital into the venture of providing ocean transportation for Hawaii is not bright.

Passenger liner service, essential to the national defense posture and to the tourist economy, faces serious problems, partially because of the withdrawal of military dependents traffic.

VI. Suggestions for Federal assistance: In considering possible Federal assistance to Hawaii's domestic shipping system, the problems of which are national in scope, this fundamental fact should be

foremost: The paramount need of the Hawaiian economy has been and will continue to be, regular, frequent, dependable, and modern shipping service.

It is Matson's position that this need can be met best by a carrier or carriers devoted exclusively to serving the Hawaiian trade at reasonable rates. By reasonable rates we mean rates sufficient to meet operating costs and to provide a fair return, which will enable these carriers, as part of the Nation's free enterprise system, to retain and attract the capital necessary to continue to provide the Hawaiian trade with adequate capacity and improvements as maritime technology advances.

Opening the trade to subsidized carriers, whose service to Hawaii would be incidental to their principal foreign trade routes, would have a serious adverse impact on domestic carriers serving only Hawaii. In the scramble for premium cargo, chaotic rate situations would develop, service would deteriorate, and the Hawaiian economy would be the loser.

Briefly, may I expose the hidden fallacies in this suggested approach to Hawaii's shipping future. Experience reveals that through carriers would:

1. Serve only one Hawaii port, carrying only the fast handling high revenue cargo;
2. Siphon this cargo from the domestic carriers, thus endangering rate levels, frequency of service and full range of Hawaiian port calls on the part of the domestic carriers;
3. Serve only at the convenience of the carrier, based on Far East trade conditions, not the necessity or convenience of the Hawaiian trade.

Present laws which restrict domestic shipping in the Hawaiian trade to U.S. flag carriers must be continued as an essential part of our Hawaiian defense posture.

Upon this premise, the following means of providing Federal assistance to the Hawaiian shipping system are offered at this time. Such assistance could be provided at little or no cost to the taxpayer:

1. Simplify and streamline ratemaking procedures. At best there is some delay in recovery by the carriers of cost increases, since their impact must be felt before increased rates can be filed. Collection of anticipated cost increases is not permitted, however firmly management may be convinced of their certainty. We were pleased to learn the Federal Maritime Board is planning to study ways of simplifying and streamlining ratemaking procedures.

2. Enactment of legislation under which water carriers in these domestic offshore trades may voluntarily establish through routes and joint rates with carriers subject to the jurisdiction of the ICC and to that of the CAB, covering through movement of shipments between mainland interior points and Hawaii. Joint rates would immediately afford shippers single-carrier responsibility, simplifying shipping arrangements, tracing, and claims. Joint rates should also make possible a reduction of transportation costs to shippers, justified by improved coordination in handling through shipments by participating carriers.

3. It is congressional policy of long standing, that terminal area pickup and delivery service by motor vehicle, incidental to interstate rail and water transportation, is regulated as part of such line haul transportation, rather than as separate motor carrier service. We think this policy applies to water carriers such as Matson, operating under the Shipping Acts, as well as to carriers subject to the Interstate Commerce Act. However, certain drayage carriers claim this policy does not apply to the Hawaiian trade and seek thereby to preclude Matson from offering pickup and delivery service within the terminal areas of the ports it serves. Only if the application of this principle to container service in the Hawaiian trade be preserved can shippers and consignees realize maximum savings in transportation costs. We urge enactment of legislation which will make it clear that in the Hawaiian trade container pickup and delivery service, within our port areas, is regulated as part of our water transportation, in order to put our trade on a basis comparable with that of the transportation between the first 48 States.

4. Consider a Federal program of port modernization for Hawaiian ports, including the possible transfer of military piers 39 and 40 in Honolulu to the State Government. Such a program would in many ways parallel the Federal assistance now given to airport and air terminal construction and modernization. It should be established in order to develop and enlarge the port facilities that will be required to support modernized ships and systems of cargo handling. Such port facilities would then be available in time of national emergency, for port facilities, in offshore areas at least, are of national as well as local concern.

5. Amend the Vessel Exchange Act in order to give the domestic operator a priority on the purchase of turned-in subsidized freighters and assistance in defraying costs of purchases and modernization. This suggestion recognizes the stern reality that new construction for the Hawaiian trade is almost financially impractical and that the modernization of existing vessels, under the proper circumstances, currently offers the best method of fleet replacement.

6. Federal subsidies for the domestic offshore trades have been suggested by several witnesses before this committee. This would involve a basic change in national maritime policy and would require extensive study. Beyond what I have already said, we do not have a position on this subject. If legislation on domestic subsidies is prepared, we will be pleased to testify concerning it.

In concluding, I wish to thank you again for this opportunity of appearing before you to discuss the shipping system and problems of the Hawaiian trade. I wish to assure you that utmost in cooperation will be afforded by the management of the Matson Navigation Co. in an endeavor to find long-range and orderly solutions to these very complex problems. We are confident that with the joint efforts of the Federal and State Governments, labor, management, and users of transportation service, workable solutions can be developed.

(Exhibits 1 through 8 follow:)

SEVIER EXHIBIT NO. 1
 Senate Merchant Marine and
 Fisheries Subcommittee
 3/13/61

DEAN WITTER & CO. INVESTMENT BANKERS

SAN FRANCISCO
 LOS ANGELES
 NEW YORK
 CHICAGO

48 MONTGOMERY STREET - SAN FRANCISCO 8, CALIF. - EXBROOK 2-7211

MEMBERS: NEW YORK STOCK EXCHANGE - PACIFIC COAST STOCK EXCHANGE - MIDWEST STOCK EXCHANGE - AND PRINCIPAL COMMODITY EXCHANGES
 RESEARCH DEPARTMENT

February 20, 1961
 133 ff

HAWAIIANA

Hawaii and Hawaiian Companies One Year Later
 (A Brief Followup to Our Extensive 1960 Reports)

Hawaii's rate of growth in the past five years has been nearly twice that of the United States mainland, and about on a par with that of California. Moreover, the dynamic forces in the Hawaiian economy have remained strong enough to overcome the down pull of the current Mainland recession and to push business in the Fiftieth State further ahead, even though at a slower pace than in 1959 and early 1960.

The tourist trade continues as one of the principal expansionist forces in Hawaii, with 1960 arrivals 21% above 1959 (1959 was 41.7% ahead of 1958). In recent months, obviously under the influence of the Mainland recession, tourist growth has somewhat leveled off, but it is likely to show renewed vigor when the United States economy turns up later in 1961.

In addition, military expenditures - the largest single item in Hawaii's economy - was again up about 10% in 1960. Thirdly, construction in 1960, stimulated by the rising number of tourists and permanent residents and by increased government spending, exceeded the prior year by 28%, dollarwise. Oahu building permits, indicating the more immediate construction trend, continue well above 12 months ago.

Therefore it is not surprising to find the Islands' 1960 retail sales 11.3% ahead of 1959, as compared to a lean 2% increase on the Mainland, and unemployment at a low 3.4% of labor force, as against a recent 6.8% recession figure for the United States.

It would be foolish to think that the economic skies around the Islands are entirely without clouds and safe from occasional showers but they probably will continue to show a bias toward "fair weather conditions."

One of Hawaii's immediate problems resides in the current renegotiation of the labor contracts in the sugar industry. This year happens to be the first one when the State's sugar output could recover to more normal levels from the effect of the 1958 strike. Even so, the expected production of about 1,100,000 tons would still fall short of Hawaii's first quarter quota of 1,215,412 tons (on an annual rate). While the Mainland sugar industry is expanding plantings to benefit from the elimination of Cuban sugar from U. S. markets (though the gap is to be primarily filled from foreign sources) Hawaii now is in no position to benefit likewise from this situation. Despite the recent brief walkout of

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 DEAN WITTER & CO.

labor in some plantations, labor and management are mostly expected to have learned their lesson and to get together in a new contract without a new and disastrous strike.

Technologically, the Hawaiian sugar industry is in the lead. It may have solved the mechanization of sugar cane harvesting which would eliminate the cost of cleaning the cane, reportedly as high as milling costs on many plantations. On the other hand, the economic use of bagasse as a raw material for paper in Hawaii will have to wait for another substantial increase in the State's population and market.

There are other short range problems: Tremendous as the growth in tourism has been, the number of hotel rooms has recently increased even more rapidly - in 1960 alone from 7,266 to 9,627 - with the result that recent occupancy rates in major hotels have been relatively low. However, if the Hawaii Visitors Bureau's forecast turns out to be correct that tourist arrivals by 1965 will be about twice the 1960 number of 295,400, the present imbalance in hotel space would soon be corrected. Oahu's well known land problem - only 11% of the Island acreage is owned by private parties holding less than 5,000 acres each - will again make headlines as holdover land laws expire next August 21 and a new land code must be enacted by that time. Despite the differences between a Democrat-controlled State House and a Republican-controlled Senate and Governorship, a constructive compromise seems likely. Connected with the land problem is the rather startling upthrust in Oahu's real estate prices in recent years, which could cause temporary problems if Hawaii's boom should level off for a more extended period at some time.

We think that these, and other problems, will not prevent Hawaii from having a very promising future, and mention them only for the sake of drawing a balanced and realistic picture. We believe that the positive factors will enable the Islands to enjoy a continued good basic growth trend - though perhaps at a less hectic rate than in the past few years, as -

1. the Fiftieth State has a young and eager population, with high educational and living standards, and unhampered by acrimonious racial strifes;
2. speedier and more complete transportation facilities are provided between the Mainland and the Fiftieth State, and also between the latter's various islands;
3. a growing population and domestic market stimulates domestic manufacturing and farming;
4. substantial land on Oahu is being made available to the economy, mostly on a rental basis;
5. tourism continues a vigorous uptrend and begins to inject new life into the "outer islands" of Hawaii, Kauai, and Maui; and

6. other service industries - such as banking, insurance, and public utilities - have to keep up with the needs of a rising number of residents and tourists.

With the long term outlook good, and Hawaii's economy fully resistant to the current Mainland business recession, it is not surprising to find nearly all Hawaiian stocks selling at historically respectable levels. However, most of them - with the exception of the leading utility and bank stocks, and American Factors - have not yet regained their 1960 highs. The following are some brief comments on a number of Hawaiian stocks.

Castle & Cooke - Considering merger with two undisclosed Mainland companies after merger with Dole and Columbia River Packers in April. Management considers Mainland acquisitions and land development most promising. There has been some discussion - though nothing final - about large scale future development of some of the company's extensive landholdings in Hawaii. Company has no immediate plans for subdividing its potentially valuable 6,556 acre Blackhawk Ranch in Contra Costa County, California. Management is confident that it will soon sell its 160,000 shares of Honolulu Oil, now worth about \$12 1/2 million, to replenish its working capital and use the balance for other corporate needs. Since earnings potential can probably be lifted materially above the \$2.00 to \$2.50 per share historical level, stock around 40 seems not out of line for long range commitments; listing likely after Dole merger. More information may appear in Proxy Statement to be issued in March.

American Factors - We understand 1960 earnings, exclusive of Pioneer Mill and Oahu Sugar, were up from the 1959 figure of \$1.27 per share. Merchandising, together with insurance and other services, accounts normally for about two-thirds of earnings; the rest comes from sugar. Expects to close deal with Sheraton Co. for first hotel on company's Maui luxury resort development which will eventually have 10 hotels. Also planning new resort on Kauai. Some relatively minor earnings dilution in case of full conversion of \$8 million 5% convertible notes. Around 30, stock is reasonable long term speculation on land developments and sugar recovery.

C. Brewer - 1960 earnings were depressed by poor sugar operations; however, this year sugar crops should be back to more normal levels - union-management relations, and weather permitting. Company has contract to develop Iran sugar industry and is negotiating management contract in Ecuador. Will acquire large sugar operation in Puerto Rico including 8,800 acres of fee cane land and five sugar mills with 230,000 ton annual capacity (110 day season) which it hopes to make profitable. Financed by \$18.8 million 6 1/4% loan from Prudential, with no payback in next five years. Stock at 35, quite high on 1960 depressed earnings, is a speculation on the Puerto Rican venture.

Oahu Railway & Land - Its tugs provide regular freight service between the State's islands. Some property leases coming up for renewal on more favorable basis. Company's docks may be taken over by State; standing on the books at \$6 million, they are

believed to have a real market value of perhaps \$30 million or more. Stock at 55, with an earnings potential of around \$3.20 and paying \$2.40 a year, is selling at about one-half estimated real asset value.

Lewers & Cooke - A merchandiser of building materials benefiting from current construction boom. Have recently gone into tract housing developments; built 200 houses in 1960 and grossed \$3.6 million on them; plan to build 300 houses this year and 500 yearly thereafter. Company owns nearly 15 acres next to the new Ala Moana Shopping Center worth perhaps four times its book value of \$370,000. Stock at 22 has thin market (about 380,000 shares outstanding) but seems attractive at about 11 times 1960 earnings which we estimate at \$2.00 per share or slightly better.

Hawaiian Telephone - (See Report of March 28, 1960). Expects telephone additions at annual rate of 5-7% in next five years; 1961 capital outlays \$14-15 million. To issue \$7 million bonds soon, sell \$5 million equity later this year on rights basis, which may keep 1961 earnings in neighborhood of last year's \$1.50 or slightly below. Intends to split stock 2-for-1 and raise dividend slightly. (Recent price: 29, current yield 3.7%).

Bank of Hawaii - (See Report of April 25, 1960). Company has extended its outstanding growth record last year when net operating earnings climbed to \$6.78 per share from \$6.14 in 1959, and net to \$7.52 from \$6.63. Despite the easing in interest rates and a slowdown in Hawaii's growth rate, some further earnings progress seems likely this year. The stock is deservedly attuned to growth. (Recent price 120, yield 2.0%, also paid 8% stock in 1960).

First National Bank of Hawaii - (See Report of July 15, 1960). In the last few years, First National - the former Bishop National Bank - has definitely stepped up its pace in various ways, and last year, the earnings improvement was impressive: Net operating earnings of \$4.05 versus \$3.25 in 1959, and net of \$3.01 as against \$2.78. Some further earnings increment seems likely in 1961. (Recent price 50, yield 2.8%).

Dean Witter & Co. and/or its partners may in the normal course of business have a position in some of these securities.

RAB:in/SF

SEVIER EXHIBIT NO. 1
SENATE MERCHANT MARINE AND
FISHERIES SUBCOMMITTEE - 3/3/61

MATSON NAVIGATION COMPANY
PACIFIC COAST/HAWAIIAN ISLANDS
FREIGHT COST PER SELLING UNIT
CURRENT RATES

COMMODITY	AVERAGE WT. OR CUBIC MEASUREMENT OF SHIPPING UNIT	SHIPPING UNIT	FREIGHT COST PER UNIT
Coffee	1,315 Cuft. per Carton	24/18 Regular per Carton	\$.0353 per can
Coffee	1,188 Cuft. per Carton	24/6 oz. Instant per Carton	.0318 per jar
Pork and Beans	31 lbs. per Carton	48/8 Cans per Carton	.0083 per can
Tomato Juice	.802 Cuft. per Carton	24/2 Cans per Carton	.0215 per can
Canned Peaches	.804 Cuft. per Carton	24/2 Cans per Carton	.0216 per can
Canned Peaches	1,136 Cuft. per Carton	24/2-1/2 Cans per Carton	.0305 per can
Canned Peas	.666 Cuft. per Carton	24/303 Cans per Carton	.0179 per can
Canned Corn	.666 Cuft. per Carton	48/16 oz. Cans per Carton	.0191 per can
Canned Salmon	1,429 Cuft. per Carton	24/303 Cans per Carton	.0179 per can
Lima Beans	.666 Cuft. per Carton	24/1 Cans per Carton	.0113 per can
Soup, Canned	.42 Cuft. per Carton	48 Talls per Carton	.0138 per can
Evaporated Milk	1,03 Cuft. per Carton	50 lbs. net weight	.0130 per lb.
Onions	50.5 lbs. per sack	30 dozen per case	.0843 per dozen
Eggs Large (Refrigerated Stowage)	53 lbs. per case	30 dozen per case	.0501 per dozen
Eggs Large (Ordinary Stowage)	2,35 Cuft. per case	10/5 lb. packages per bale	.0626 per 5 lb. pkg.
Flour, 5 lb. Packages	51 lbs. per bale	30/18 prints per Carton	.0402 per lb.
Butter (Refrigerated Stowage)	31 lbs. per Carton	30/18 prints per Carton	.0130 per lb.
Butter (Ordinary Stowage)	.605 Cuft. per Carton	36/18 packages per Carton	.0521 per lb.
Cheese (Refrigerated Stowage)	39.25 lbs. gross wt. per Carton	36/18 packages per Carton	.0129 per lb.
Cheese (Ordinary Stowage)	.721 Cuft. per Carton	48/18 packages per Carton	.0518 per lb.
Bacon	52 lbs. gross per Carton	1 Bale Net - 60 lbs.	.0575 per lb.
Meat Carcasses (Beef Loin)	60.7 lbs. gross per bale	24/8 oz. packages per Carton	.0644 per package
Corn Flakes	2.4 Cuft. per Carton	48/18 Cans per Carton	.0154 per can
Canned Dog Food	1.15 Cuft. per Carton	12/6 oz. Cans per Carton	.0123 per can
Baking Powder	.23 Cuft. per Carton	24/11 oz. Cans per Carton	.0134 per can
Beer, Canned	.502 Cuft. per Carton	24/26 oz. packages per Carton	.0247 per package
Salt, Table	.92 Cuft. per Carton	Loose	.952 per tire
Automobile Tire, Passenger	23.14 lbs. each	50# per sack net	.0124 per lb.
Feed, Animal or Poultry	50.5 lbs. per sack	One Unit per Carton	18.03 each
Radio - Phonograph	28 Cuft. per Carton	One Unit per Carton	14.23 each
Washing Machine	22.1 Cuft. per Carton	39 lbs. net per Carton	.0251 per lb.
Oranges and Lemons	40 lbs. per Carton	12/5th Bottles per Carton	.0691 per bottle
Whiskey	1,186 Cuft. per Carton	12/5th Bottles per Carton	.0445 per bottle
Wine (Sherry)	.833 Cuft. per Carton	100 lbs. net	.013 per lb.
Potatoes	101 lbs. per sack	12/5 lb. packages	.0636 per 5 lb. pkg.
Rice, 5 lb. packages	61 lbs. gross per bale	55 gallons per barrel	.0315 per quart
Lubricating Oil - Automobile	10.75 Cuft. per barrel	12 pails per Carton	.1608 per pair
Men's Shoes	3 Cuft. per Carton	One 9 Cuft. unit per Crate	21.11 per unit
Refrigerator, Household	32.78 Cuft. per Crate	Average 48 shirts per Carton	.0671 per shirt
Men's Shirts	5 Cuft. per Carton		

SEVIER EXHIBIT NO. 3
SENATE MERCHANT MARINE AND
FISHERIES SUBCOMMITTEE - 3/13/61

MATSON NAVIGATION COMPANY
Annual Average Retail Food Prices
Honolulu Vs. U.S. City Averages (1959)
and Ocean Transportation Cost

Commodity Items	U.S. City Average Retail Food Prices 1959 (2)	Honolulu Average Retail Food Prices 1959 (2)	Diff.	Ocean		Reference
				Transportation Cost Per Unit (See Note)		
acon, Sliced 1 lb.	\$.651	\$.849	\$.198	\$.0525 (1)		52¢ Gross per ctn-48/1# pgs.
almon, Pink 16 oz.	.622	.663	.041	.0201		1.429 cuft per ctn-48/16oz cans
utter 1 lb.	.759	.835	.076	.0408 (1)		31¢ Gross per ctn-30/1 lb prints
beese 1 lb.	.981	.674	.093	.0528 (1)		39.25¢ Gross per ctn-36/1# pgs.
ilk, Evaporated 1 1/2 oz.	.153	.176	.023	.0146		1.04 cuft per ctn-48/1 1/2 oz cans
otatoes 1 lb.	.066	.116	.090	.0136		101¢ per sack - 100¢ net
nions 1 lb.	.112	.125	.013	.0136		50.5 lbs per sack-50¢ net
eaches, Can #2 1/2	.353	.409	.056	.0320		1.136 cuft per ctn-24/2 1/2 cans
orn #303	.192	.243	.051	.0187		.666 cuft per ctn-24/303 cans
was #303	.202	.254	.052	.0187		.666 cuft per ctn-24/303 cans
lour, Wheat 5 lb.	.544	.742	.198	.0659		51¢ Gross per bale-10/5# pgs.
offee 1 lb.	.744	.986	.242	.037		1.315 cuft per ctn-24/1# cans
amch. Meat, can 12 oz.	.512	.558	.046	.0173		23¢ Gross per ctn-24/12 oz pgs.

Note: Includes current ocean rate, plus wharfrage at Pacific Coast port of shipment and Honolulu.

1) Refrigerated cargo moving in refrigerated cargo space.

2) Source: State's Exhibit No. 61, FRB Docket 869, June 16, 1960

SEVIER EXHIBIT NO. 4
SENATE MERCHANT MARINE AND
FISHERIES SUBCOMMITTEE - 3/13/61

MATSON FREIGHT RATE INCREASES

SINCE 1946

With Example Commodity Unit Costs

Eff. Dates	Gen. Mdse. Rate (Per Ton)	RICE 100.5# per sk.	MENS SHOES 4 CF per ctn. 12 prs. per ctn.	POTATOES 101# per sk.	SOUPS 48/#1 can .856 CF per cs.	COFFEE 24/#1# 1.289 CF
7/1/46	\$ 10.30	\$.5175	\$ 1.03	\$.5201	.00459 per can	\$.01383
3/10/47	12.35	.6206	1.24	.6237	.00551 "	.01658
9/1/48	13.60	.6834	1.36	.6868	.00606 "	.01826
2/1/51	15.00	.7537	1.50	.7575	.00669 "	.02014
1/14/52 (surcharge)	16.12	.8100	1.61	.8140	.00716 "	.02165
3/1/53	17.50	.8794	1.75	.8837	.00780 "	.0235
3/1/55	18.55	.9321	1.85	.9368	.00827 "	.0249
2/11/57	20.31	1.0205	2.03	1.0256	.00905 "	.02727
7/15/57	21.00	1.0552	2.10	1.0605	.00936 "	.02819
1/20/58	22.90	1.1507	2.29	1.1565	.01021 "	.03074
9/14/59	25.76	1.2944	2.57	1.3009	.01148 "	.03458
Total Increase 7/1/46 to 9/14/59		.0077 per lb.	.13 per pr.	.0078 per lb.	.00689 per can	.02075 per lb

Sevier Exhibit No. 4 A
Senate Merchant Marine
and Fisheries Subcommittee
3/13/61

CONSUMER PRICE INDEX
for
TEN U.S. MAINLAND CITIES, HONOLULU, AND TOTAL U.S.

September, 1960

(1947-1949 = 100)

San Francisco	133.0
Chicago	130.4
Los Angeles	129.8
Baltimore	128.7
Atlanta	127.9
St. Louis	127.4
Philadelphia	127.2
Total U.S.	126.8
New York	125.5
Detroit	125.4
<u>Honolulu</u>	<u>125.1</u>
Cincinnati	124.8

Note: Honolulu Consumer Price Index base has been shifted from March 15, 1943 = 100 to 1947-1949 = 100.

Sources: Honolulu Consumer Price Index -
State of Hawaii
Department of Labor & Industrial Relations
Bureau of Research & Statistics
Honolulu, Hawaii

Consumer Price Index for cities other than Honolulu -
U.S. Department of Labor,
Bureau of Labor Statistics

Note: For the month of December 1960 (1947-1949 = 100), the Honolulu Consumer Price Index was 126.1 and the total U.S. Consumer Price Index 127.5.

SEIVER EXHIBIT NO. 4-B
 Sheet 1
 Senate Merchant Marine
 and Fisheries Subcommittee
 3/13/61

COMPARISON OF TRANSPORTATION COSTS ON
 REPRESENTATIVE SHIPMENTS - CONTAINER VS.
 CONVENTIONAL SERVICE

BAKERY GOODS, VIZ: CRACKERS OR COOKIES

971 Cases - 16,222 lbs. 1290 Cubic feet

TARIFF NO. 1-N, ITEM NO. 5 (Conventional Stowage)

LOCAL DRAYAGE (1)

16,222 lbs. @ \$.32 per 100 lbs. \$ 51.91

SAN FRANCISCO WHARFAGE

1290 Cubic feet @ \$.80 per 40 cubic feet \$ 25.80

OCEAN FREIGHT CHARGES

1290 Cubic feet @ \$25.76 per 40 cubic feet \$830.76

HONOLULU WHARFAGE

1290 Cubic feet @ \$.45 per 40 cubic feet \$ 14.51

INSURANCE

32.25 Tons @ \$.50 per ton \$ 16.13

TOTAL \$939.11

TARIFF NO. 14, ITEM NO. 220, (ZONE 1/CFS)- CONTAINER SERVICE*

16,222 lbs. @ \$4.40 per 100 lbs. \$713.77

Saving per Tariff No. 14 \$225.34
 Per cent of total costs under Tariff No. 1-N 31.57%

* CL shipments do not require marking; rate includes pickup, wharfage and insurance.

- (1) City Carriers Tariff No. 1-A, Item No. 360-I, Rate Basis B, 3rd class.

SEIVER EXHIBIT NO. 4-B
Sheet 2
Senate Merchant Marine
and Fisheries Subcommittee
3/13/61

ADDITIONAL EXAMPLES OF SAVINGS UNDER CONTAINER SERVICE
(Calculated in Same Manner As Sheet 1.)

ORIGIN PORT	COMMODITY	WEIGHT (Pounds)	FREIGHT COSTS		
			Conventional	Container	\$ Savings
San Francisco	Bottles	11,853	\$ 809.27	\$ 673.25	\$ 136.02
San Francisco	Canned Food	81,223	1,469.56	1,116.82	352.74
San Francisco	Coffee	32,642	970.88	824.21	146.67
San Francisco	Feed, Animal	39,809	590.77	469.75	121.02
San Francisco	Rice	40,200	586.52	500.49	86.03
San Francisco	Sodium Hypochlorite Solution	75,756	1,434.14	1,098.46	335.68
Los Angeles	Bar Soap	39,668	1,203.57	1,036.06	167.51
Los Angeles	Beverage, Malt	150,104	2,928.50	2,493.59	434.91
Los Angeles	Cottonseed Oil Meal	202,000	3,002.73	2,383.60	619.13
Los Angeles	Liquid Asphalt	40,824	637.06	540.04	97.02
Los Angeles	Paint	96,403	1,599.71	1,407.48	192.23
Los Angeles	Shingles	42,636	672.36	562.80	109.56

NOTE: Container rate includes pick-up at shipper's place of business, wharfage at San Francisco or Los Angeles and Honolulu, and insurance. As conventional ocean rate does not include these items, cost of drayage at origin port, wharfage and insurance obtained separately are included in conventional cost.

SEVIER EXHIBIT NO. 5 - Sheet 1
SENATE MERCHANT MARINE AND
FISHERIES SUBCOMMITTEE - 3/13/61

HAWAII'S SPECIAL FREIGHT SERVICE REQUIREMENTS

Although the development of the container and automobile services have been the most dramatic post war changes, there were a number of other important Matson improvements made through the years to meet the specific transportation requirements of the Hawaiian trade.

Just prior to World War II, Matson was instrumental in construction of a bulk sugar loading facility at Kahului, and a discharging gantry at Crockett, to eliminate the handling of raw sugar in bags. These proved to be successful, and after the war, Matson constructed a second bulk loading facility at Hilo and operated four discharging gantries at Crockett. All raw sugar now moves from Hawaii in bulk. In addition, Butterworth equipment was installed in deep tanks to reduce the time required and the cost of cleaning them, enabling C3's to carry bulk fuel oil to the Islands for power plants, and molasses to the Pacific Coast in the same tanks. Special bronze fittings were added to carry aqua ammonia in bulk for use as fertilizer in the Islands. Refrigeration boxes were modified to carry concentrated fresh frozen pineapple juice at minus 10° temperature to new mainland markets. Procedures were developed with shippers to carry papaya and fresh pineapple in chilled space, making it possible for Hawaii to develop an entire new market for its tropical fruit products. The lumber trade was assisted in the development of packaged lumber, cutting down transportation costs and reducing losses.

EXHIBIT NO. 5
Sheet 2

Matson is studying many other innovations in the constant battle to stem the rising tide of operating costs. Each of these changes takes ingenuity, patience and money. Problems imposed by national, state and local laws and regulations, labor practices and requirements, and plant procedures and equipment of shippers and consignees, do not permit overnight solutions.

SEVIER EXHIBIT NO. 6 - Sheet 1
MERCHANT MARINE AND
FISHERIES SUBCOMMITTEE - 3/13/61

REPLACEMENT COST OF HAWAIIAN SERVICE VESSELS

Under Federal laws, vessels engaged in domestic Hawaiian trade are restricted to those built in shipyards located in the United States. When it becomes necessary to replace Hawaiian trade vessels with new vessels, it will be necessary to have them constructed or modernized in American shipyards, paying American costs.

Vessel replacement is not a new problem for Matson. It has been faced many times during 79 years of operation in the Hawaiian trade.

In 1887 Captain Matson and his associates constructed the first LURLINE with a cargo capacity of 640 tons. Three more sailing ships were added, including the RODERICK DHU equipped with a cold storage plant and electric lights. The 3,630 ton ENTERPRISE, the company's first steamer, purchased in 1901, was rebuilt for the Hawaiian trade. The second LURLINE with 8,000 tons capacity was followed by the WILHELMINA in 1909, the 8,500 ton MANOA in 1913 and the first high-powered gear, turbine driven vessel on the Pacific. Other firsts have included the FALLS OF CLYDE, the first oil tanker in the Hawaiian trade, the external Sperry gyrofin stabilizers installed on the MONTEREY and MARIPOSA, in Australian trade, which were the first for any passenger liner, the HAWAIIAN CITIZEN which was the first all-container ship in the Pacific, the HAWAIIAN FISHERMAN which was the first automobile carrier in the Pacific, and the MATSONIA's new internal flume stabilizing system, the first for any passenger liner.

EXHIBIT NO. 6
Sheet 2

Matson's W.W. II fleet was requisitioned by the Government for war use. In the immediate post-war years Matson acquired 15 C3 type vessels and two Liberty type vessels for \$20,352,880. In addition approximately \$8,038,165 was spent between 1947 and May 31, 1955 on special facilities required to serve the trade. Since that time there have been several sales and acquisitions so that the cost of the present fleet of 20 cargo vessels with modifications, improvements and conversions is \$41,554,672.

In looking to the future it appears quite probable that the Hawaiian service may have to be sustained by a program of modernization of old vessels, rather than the construction of new. Should the time come, in the foreseeable future, when a new fleet of freighters is required by the trade, it is of interest to consider the possible cost of such a program. The cost of replacing the present fleet with new vessels would be many times the acquisition cost of the present fleet.

Some concept of the magnitude of the cost replacement problem can be formulated on the basis of the testimony of a naval architect and marine engineer presented by Matson as a witness in the FMB hearing Docket 869 (concerning the cost of replacing the Matson fleet). This testimony was reviewed by the Maritime Administration's experts on ship construction and it was stated on the record that they were satisfied as to the reasonableness of the costs developed.

The witness's study was based on a fleet of 22 vessels consisting of 14 C3's, of which six were fitted with special deck

EXHIBIT NO. 6
Sheet 3

container equipment, three AP3 type vessels, two Liberty type vessels, one C3 converted to a full container ship, and two C4's converted to combination bulk container ships. The pre-war domestic cost of such vessels, as shown in the Federal Register, was compared with estimated construction costs of new Maritime Administration designed vessels, using American shipyard bids opened in 1959 and 1960.

Pre-war construction cost of a Liberty was \$1,278,000 compared with the estimated 1960 construction cost of \$8,550,000 for a replacement of the Freedom type, 670% of pre-war cost.

Pre-war construction cost of a Victory was \$2,130,000 compared with the 1960 construction cost of \$10,550,000 of a replacement of the new Clipper design ship, 495% of pre-war cost.

The pre-war construction cost of a C3 was \$2,460,000 compared with the 1960 construction cost of \$11,550,000 for a replacement of the new Seafarer design, 470% of pre-war cost.

Reproduction of the 22 vessels in the January, 1960 freighter fleet, that is, building new vessels using the C3, Victory and Liberty designs, would cost \$178,559,430. Replacement cost of the January, 1960, fleet with the new design Seafarer, Clipper and Freedom type vessels, and three special types for the container ship and bulk-container combination ships, would be \$272,144,000. Replacement of the January, 1960, fleet with three Seafarers without facilities to carry containers on deck, five Seafarers equipped to carry containers on deck, two bulk container ships, two Clippers and four full-container ships would cost \$268,332,000.

EXHIBIT NO. 6
Sheet 4

The designs and the number of ships in each design selected by the witness were used for his own calculations in order to prepare the study and present the testimony in proceeding. Due to the changing requirements of the trade and changing cost factors, replacement vessels actually selected for Hawaiian trade may be of substantially different design, and substantially different in number.

His findings, however, do emphasize the tremendous increase that has occurred in recent years in the cost of constructing new vessels with modern equipment specially designed to fit the requirements of the Hawaiian trade. A comparison of these estimates can be made with the bids which were opened on February 8, 1961, in New York City in the offices of the Federal Maritime Board for construction of three container ships for American Hawaiian Steamship Company. The proposed vessels would be approximately 900 feet in length, 101 foot beam, 24 knots, 60,000 shaft horsepower, twin-screw and would lift 1,000 30' x 8' x 8' containers between New York harbor and Los Angeles and San Francisco on a nine-day turnaround. The apparent low bid was \$21,400,000 for the first ship, \$20,600,000 for each of two, and \$20,350,000 for each of three. The apparent high bid was \$24,988,000 for the first ship, \$23,173,000 for each of two, and \$22,452,000 for each of three.

Another example of present-day costs is the contract signed recently between States Line of San Francisco and the FMB with the National Steel and Shipbuilding Company of

EXHIBIT NO. 6
Sheet 5

San Diego for construction of two mariner type freighters at more than \$11,000,000 each. In each case, \$71,000 was added for national defense features.

While no exact figures can be given today on the cost of replacing the present Hawaiian fleet with new vessels, it is apparent to Matson management, and others also, that the cost will be extremely high - probably prohibitive.

SEVIER EXHIBIT NO. 7 - Sheet 1
MERCHANT MARINE AND
FISHERIES SUBCOMMITTEE - 3/13/61

THE COMPETITION FOR CAPITAL

The offshore domestic shipping business, just as any other regulated business, is entitled to an opportunity to earn a rate of return which will produce for its shareholders a return commensurate with what they could receive on investments in other businesses having corresponding risks. The return must be sufficient to assure the financial integrity of the business and enable the company to attract capital. To provide the FMB a basis for findings respecting the fair rate of return, Matson caused a study of its freight service operations in the Hawaiian trade to be made by an investment analyst, who testified in both Dockets 808 and 869. He acquainted himself with the economics of such operations sufficiently to enable him to evaluate them from an investment viewpoint in comparison with other types of business enterprises. Comparing price earnings ratios and dividend yields of 125 industrial companies, 24 utility companies and 5 shipping companies, the analyst found that investors expect a greater return for their investment in the shipping industry than they do for their investments in utilities or industrials. He further found that the risks attendant to an investment in Matson freight operations are very much greater than those in the gas and electric utility field. Gas and electric companies have shown a generally steady growth resulting from increasing population and greater consumption per customer.

The prospects for growth in Matson's freight operations are limited. Such growth as Matson may expect in its freight operations will be primarily in its westbound cargo, without a compensating growth in its eastbound cargoes,

which are principally sugar, molasses and pineapple. The result would be a further aggravation of the imbalance which presently exists between westbound and eastbound cargo, with a corresponding adverse effect on the economics of Matson's freight operations.

Insofar as stability of earnings is concerned, the record of Matson's freight operations is extremely poor in relation to that of gas and electric companies. During the period from 1952 through 1959, Matson's earnings fluctuated widely, with a loss in 1952, followed by its highest level of earnings in 1953 during the period. Then in 1954 there was a drop in earnings of more than 50%. Substantial recovery in 1955 was followed by a steady decline thereafter. In 1959 Matson operated at a substantial loss. No significant gas or electric utility has experienced a comparably poor and spotty earnings record during this period.

If offered the same rate of return on common equity, considering Matson's earnings record and prospects, an investor would obviously choose a gas or electric utility in preference to Matson.

The risks of industrial manufacturing concerns vary widely from industry to industry and from company to company. However, investors, by their low valuations of shipping industry stocks, have clearly indicated that risks of investment in shipping are higher in relation to earnings received than the risks in manufacturing enterprises.

SEVIER EXHIBIT NO. 8 - Sheet 1
MERCHANT MARINE AND
FISHERIES SUBCOMMITTEE - 3/13/61

THE PASSENGER LINER PROBLEM

Prior to 1901, passengers in the Hawaiian trade traveled in cabins on freighters. In that year Matson introduced the SS ENTERPRISE, first oil-burning steamer in the Pacific. It was equipped with comfortable accommodations for 22 passengers. The service grew, and prior to World War II Matson operated two large passenger liners, the LURLINE and MATSONIA. The LURLINE was built in 1933 at a cost of about \$8 million, with accommodations for over 700 passengers. The MATSONIA, formerly the MALOLO, was built in 1927 and had accommodations to carry 575 passengers and 2,000 tons of express cargo.

The reconversion period after the war and transition to peacetime operations were difficult for the shipping industry generally, and for the Hawaiian trade in particular. The government was committed to restore the LURLINE and MATSONIA to their former condition after their wartime use, but it was apparent that passenger vessels to serve Hawaii and elsewhere in the post-war era would have to meet entirely new standards of modern design and comfort to keep pace with the competition of air transportation.

Matson made the decision to modernize the MATSONIA promptly to provide Hawaii at the earliest possible moment with an interim service during the time required to rebuild and reactivate the LURLINE. The LURLINE was returned to service in April of 1948. The conversion cost exceeded \$19 million, which included a settlement received from the U.S. Government of about \$6,250,000. Subsequent modernization has cost an additional \$400,000. Shortly after the LURLINE was returned to service in April, 1948, the MATSONIA was

EXHIBIT NO. 8
Sheet 2

retired from the trade and sold.

The LURLINE operated on a schedule of maximum utilization. It carried in excess of 40,000 passengers each year between the mainland and Hawaii. By mid-1950, there appeared to be a need for a second liner to support the demand of a constantly growing Hawaiian tourist economy, despite the growth of air traffic. The SS MONTEREY, which Matson had sold to the Government, was purchased back as a running mate to the LURLINE. After extensive reconversion at a cost of over \$20 million, the SS MATSONIA made her maiden voyage to Hawaii in June, 1957.

The LURLINE and the MATSONIA are now operating in Hawaiian trade. The LURLINE has 720 salable berths, and on the basis of 29 round voyages per year, an annual passenger capacity of 41,760. The MATSONIA has 730 salable berths, and on the basis of 30 round voyages per year, an annual passenger capacity of 43,800. These two vessels have a total capacity of 42,780 one-way passengers per year.

Passenger travel between the mainland and Hawaii has increased substantially in the past five years, as forecast. However, two factors have developed which make it very difficult to predict the future volume of passengers moving on ocean liners between the mainland and Hawaii. The first is impact of jet aircraft on the traveling public, and the second involves a change in the policy of the Defense Department with respect to the carriage of military personnel and their dependents.

EXHIBIT NO. 8
Sheet 3

There has been a substantial growth in passengers moving between California and Hawaii, and in the inroads made by jet aircraft on the increasing volume of Hawaii bound travelers. The Civil Aeronautics Board is now processing applications by a number of air carriers to by-pass Pacific Coast points and provide non-stop jet flights between interior mainland points and Hawaii. The effect on passenger liners of such expanded operations, if permitted, is yet to be felt.

The second factor involves the decision by the Department of Defense to move almost all military personnel and their dependents between the mainland and Hawaii by air instead of on commercial ocean liners. From 1957 to September, 1960, Matson carried 9633 such passengers per year on the average. Since the adoption of the air lift policy, we do not carry any military passengers.

Passenger service problems are further complicated by rising operating costs. The average daily vessel expense cost of operating a passenger liner during 1960 in Hawaiian trade was \$18,708, not including depreciation, advertising, mortgage costs and vessel layup expense. The cost of labor, including crew wages and benefits, is the largest single component of this daily expense, averaging 52.4%.

The financial results of our domestic passenger service reflect the effect of these rising costs and the loss of passengers

EXHIBIT NO. 8
Sheet 4

due to the competition of jet aircraft and the change in Defense Department policy on the carriage of military personnel and their dependents.

In 1956 Matson operated the LURLINE at 96% occupancy which is a higher load factor than any experienced in other U.S. passenger trades. The net profit after taxes was only \$393,615. This was, indeed, a wholly inadequate return on a sizeable investment in passenger service, particularly considering the risks involved. In 1957 with the addition of the MATSONIA, which doubled our service during the last half of the year, Matson nevertheless achieved an occupancy of 84% for both vessels for the entire year. In that year there occurred a net loss after taxes of \$319,936. In 1958 occupancy was increased to 90%, but, due to increasing costs, the loss grew to \$629,000. In 1959 sales efforts were increased to build passenger business, resulting in a 96% occupancy on the LURLINE and MATSONIA and a net profit of \$649,000 after taxes.

In 1960 the number of jet flights between the Pacific Coast and Hawaii increased greatly, and the change in the Defense Department policy on transportation of military personnel and their dependents occurred. Occupancy on the LURLINE and MATSONIA dropped to 70%. Because of increased fares and some success in cost controls, the two liners showed a net profit, but only \$247,000 after taxes.

Senator BARTLETT. Thank you, Mr. Sevier. I should like to note first for the record that the subcommittee is honored this morning by the presence with us of Hawaii's senior Senator, Senator Fong, who at the opening of these hearings last week appeared before us and offered a most useful statement on this subject. We are glad to have you with us, Senator Fong.

Senator FONG. Thank you, Mr. Chairman.

Senator BARTLETT. Of course you will be given the privilege later on of asking any questions that you may desire.

Mr. Sevier, I congratulate you upon the statement which you have just made, and I want to say that when you return home, if anyone accuses you of not having done your homework before you appeared before the committee, you can get affidavits to the contrary from all of us.

Mr. SEVIER. Thank you, sir.

Senator BARTLETT. I think the fact that we are operating here on this complex problem in a very temperate climate, even though not a subtropic one, is made evident by the fact that not even Senator Fong screamed when you said another 10-percent rate increase was going to be requested. In another day it might have been otherwise.

Mr. SEVIER. We wished to inform you.

Senator BARTLETT. Senator Butler, would you care to start?

Senator BUTLER. Mr. Chairman, I want to congratulate Mr. Sevier on a very learned discussion of a very difficult problem. I feel that some of these matters could probably be handled better on an individual basis. Taking some of these suggested aids from the Federal Government would seem to be feasible, and handling them on the basis of individual legislation where they could be more thoroughly gone into.

I know that just last year we had a situation with the railroads which was somewhat similar to the first point that you make, simplification and streamlining the ratemaking procedures. We did that for the railroads and it seems to be working very well. It is a fact that before you catch up with the benefit of the new rate that you have lost a considerable amount of money. The railroads have the same experience.

I was not aware of the fact that you could not have pickup and delivery services by motor carriage at the beginning or end of a shipment. I think certainly we could very well look into that and see what could be done.

It seems to me, Mr. Sevier—I don't know whether you agree with me or not—that from the facts and figures which you have submitted—of course I haven't had an opportunity to study them—your problem is almost one of some type of aid through legislation by the Federal Government. You have pared yourself down to the bone in vessel maintenance and other costs. And as you have pointed out, a lot of these costs are above and beyond your control. They are inflicted upon you and you must pay them or cease to do business.

I have very much enjoyed this exposition and I will be very sympathetic in my approach to it, and I hope that my good friend from Hawaii will do the same which I am sure that he will. I think facts and figures speak for themselves.

On some of the other suggestions that you have made, which are of considerable interest to me, I don't know about these two piers. Are they the berthing piers that you now regularly use in Hawaii?

Mr. SEVIER. They were piers constructed, Senator Butler, just prior to World War II. In fact I think they were completed at the outbreak of the war.

Senator BUTLER. And you berth there?

Mr. SEVIER. No. They are used solely for military cargo. Some of our freighters do call there to deliver military cargo, but they are confined to use by the military services. And I might add, they have minimum use. Very little use is made of them. They are idle most of the time.

Senator BUTLER. I think that is something that the Senator from Hawaii will have something to say about, and will probably have legislation at a future date.

Mr. SEVIER. I know that there was—2 or 3 years ago—a study made by a committee representing the Army, Navy, and Air Force, concerning the use of those piers and their need by the military. Obviously the results of that were not made public, but we do understand that their recommendation favored the release of the piers by the military.

Senator BUTLER. I am also interested in a fifth point that you made in connection with the operators in domestic trading having a priority on the purchase of turned-in subsidized freighters. That may mean putting the *America* into service on your run if she is retired on the Atlantic run, rather than letting her lay in mothballs or something of the kind.

Mr. SEVIER. That would be an example. Of course, the ones we had in mind were freight vessels, primarily.

Senator BUTLER. I would say that it seemed to me to make a lot of sense to employ these vessels rather than lay them up, and if they can be profitably employed by the domestic operators, it would seem to me that the domestic operator, in the best interest of the national interest, should have that priority to use those vessels.

They are all turned in by the vessels owners in foreign trade, aren't they?

Mr. SEVIER. Yes. The subsidized lines in their replacement programs turn the ships in with an allowance from the Government.

Senator BUTLER. Has this been taken up with the Maritime Administration?

Mr. SEVIER. Yes, sir; it has, and it is my recollection—I am not sure that I have my facts absolutely correct—that of the 2 or 3 C-3-type freighters that have been turned in, there are some 18 or 20 applicants for those vessels. We are among them.

These vessels are more suitable for our purposes than some of the vessels we are now operating. Specifically it would be our hope that we could turn in some of our less desirable vessels on these more desirable vessels and be given a priority because of the essentiality of the service we are rendering, rather than some tramp service that might not be good.

Senator BUTLER. In conclusion, may I say that the sixth point that you have made I think would meet tremendous resistance in the Congress. From my experience here I would think that you would meet formidable opposition even in this committee to extending a direct

subsidy to your domestic trade. I think that maybe the solution to this problem would lie in some other direction.

Mr. SEVIER. I think, Senator, that I suspected that that might be the case.

Senator BUTLER. I speak only for myself. From my experience on this committee, I would say that that would meet with some resistance.

I say that anything that we can do in maintaining this essential trade with our sister State, we will certainly do. Your presentation and the suggestions that you have made will be most carefully studied. We certainly appreciate your coming here and giving us this information.

Mr. SEVIER. Thank you, sir.

Senator BUTLER. It is a very beautiful and very well documented statement.

Mr. SEVIER. Thank you, sir.

Senator BARTLETT. Thank you, Senator Butler.

It has been suggested that Senator Fong might have a sympathetic interest in these problems. I suspect that is the case.

Do you have any questions, Senator Fong?

Senator FONG. Yes, Mr. Chairman.

First I want to say that we of Hawaii are very grateful to you and to Senator Butler and Senator Cotton for your patience in listening to the testimony which has been presented to this committee. The people of Hawaii certainly appreciate your patience and your interest in the matter.

I would like to thank Mr. Sevier for his very comprehensive statement. It covered the situation very, very well. The six principal points that he has presented to this committee give us a very fine idea of the magnitude and complexity of the problem.

I would like to thank Mr. Sevier and his company for the 80 years of very useful service of the Matson Navigation Co. to the people of Hawaii and to the United States in general.

Coming to the point of subsidy, did you mention, Mr. Sevier, that the two passenger ships that you have are not under subsidy now?

Mr. SEVIER. They are not. They are completely without subsidy or Government aid of any kind.

Senator FONG. You said, I think, in your statement that these are the only two ships that are not under subsidy.

Mr. SEVIER. The only two remaining ships in the American merchant marine that are not subsidized—passenger liners, yes.

Senator FONG. Would you please elaborate on that problem a little bit, on subsidies for other ships, as compared to no subsidy for these two ships?

Mr. SEVIER. We made a uick calculation. Admittedly it has no validity because there is no precise formula. But we do operate two subsidized passenger ships under a subsidiary company, the Oceanic Steamship Co., which owns and operates the *Mariposa* and *Monterey* by way of the South Pacific to Hawaii.

We took the established rates, the subsidy rates, as applied to those ships, and just for our own purposes we applied them to the *Lurline* and *Matsonia* operation. And for the year 1960, had we received subsidy to the same extent; that is, the same percentage of wages and subsistence that the Oceanic ships received, the Federal Government would have paid us \$6 million in subsidy.

Of course, the ships just about broke even so that would have been \$6 million which would represent profit had those rates applied.

The only assistance we have had from the Federal Government on those ships has, as I mentioned, been the right to carry and earn the revenues derived from carrying dependents of military personnel being transferred to and from the mainland. When that was abruptly discontinued that put a substantial crimp in our resources, and does imperil the vessels.

I would say that the continued operation of those two ships is very much in the balance.

Senator FONG. I understood you to say that if you had secured a subsidy equivalent to the subsidy given to the other ships, you would be receiving \$6 million?

Mr. SEVIER. \$6 million in Government aid for those two ships for the year 1960, had we received the same rates of subsidy as the Oceanic ships received.

Senator FONG. Just for 1 year?

Mr. SEVIER. One year.

Senator FONG. All these years you have not received any subsidy at all, for the past 80 years that you have been operating?

Mr. SEVIER. Not ships in the Hawaiian trade, no, sir.

Ships in the foreign trade that we operate, the Oceanic ships, do receive the subsidy. They have subsidy contracts with the Government and we receive subsidy payments annually for the operation of the Oceanic freighters and passenger vessels.

Senator FONG. Would you like to comment a little bit on the modernization of your ships in relation to replacing them?

Mr. SEVIER. In relation to replacing them?

Senator FONG. Yes.

Mr. SEVIER. We acquired war-built ships, which were general purpose vessels, by and large, and we adapted them to our trade at the time of their acquisition, or following their acquisition. With changes in the method of moving cargoes, bulk cargoes, unitized cargoes and container cargoes of various kinds, we found that the length of the life of a ship could be substantially extended by a modernization program. We have done that in the case of conversions for container cargo, automobile carriage, and for bulk sugar carriage.

There are further modernization plans that we have. We haven't proceeded with them largely because of the cost and the inability to earn on the overall freight service.

We think that an additional container ship could be supported by the trade. We think a package-lumber ship could be devised out of an existing freighter that would be a useful facility. But as I say, it is difficult to get the capital to do that when you can't earn on the money you already have invested in the service.

Senator FONG. You have a very difficult time attracting capital to your company?

Mr. SEVIER. As I mentioned, it is probably one of the poorest financial risks that I can think of. I think we would have a very difficult time finding a buyer for any stock issue that we would attempt to put on the market.

Senator FONG. Has the company made a very definite decision on the Northwest Line to Hawaii? I think there was a time when you

were contemplating cutting out one of your ships, or cutting down the service from the Northwest to Hawaii?

Mr. SEVIER. It goes beyond that. We gave very serious consideration to abandoning the service entirely. We lost a good deal of money in the service in 1959 and 1960. In fact we have never made any money up there. But in looking at it on the aggregate we felt that it was the type of thing that we should include in our service; there was a demand for goods from the Pacific Northwest. Matson had served that area since the beginning of the century. We therefore continued it. But we found that the inroads of foreign competition in the Canadian newsprint trade and foreign automobiles was such that we could no longer afford to call at British Columbia ports.

We found we had barge competition for the carriage of lumber out of some of the ports where most of the lumber originated. They were shallow draft and we couldn't get into those ports. We have had to contract and discontinue a specialized lumber service.

We still will operate, at least for the time being, a service from Seattle, Tacoma, and Portland.

The frequency of the service between those ports and Honolulu will be an improvement over our past service. Our service to the out ports will be less satisfactory.

We will continue to carry approximately 20 million feet of lumber on those ships as contrasted with some 45 or 50 million feet.

We carried about 50 million feet last year, and in 1961 or in any full year, our present operation would be about 20 million feet.

Senator FONG. You apprised me sometime ago that you were contemplating a request for another rate increase. You stated this morning that you are now asking for a 10-percent increase?

Mr. SEVIER. Yes, sir.

Senator FONG. Can you give us some idea of what you are basing that on?

Mr. SEVIER. We are basing it on two factors: one, a portion of it, roughly half of it, will be applied toward costs that have been experienced since our last increase went into effect. In other words, since September 1959. The costs we have realized arose out of collective bargaining agreements, the money we have paid and are paying to labor, money we have paid for fuel oil and other supplies and for shipyard labor costs; in other words, operating costs in the trade that have been experienced to date.

The remaining part of our 10 percent would at least be a contribution toward a profit in the trade; something to make up the loss in 1960, to avoid a substantial loss which we are confronted with in 1961, and possibly and hopefully provide something for profit.

Our forecasted loss in our freighter operation for 1961 at the present time is \$2 million. The loss for the year 1961. We obviously can't go on on that basis.

Senator FONG. You say your loss in 1961 is \$2 million?

Mr. SEVIER. Our forecasted loss in January was \$2,600,000. We have since had this Northwest service adjustment, and other adjustments we have made. We have brought that forecasted loss down to slightly over \$2 million. And that is where it stands today.

Senator FONG. That is, if you do not receive this 10-percent increase that you are asking for?

Mr. SEVIER. That assumes two things, Senator: it assumes that we get no further increase in rates, and it assumes we have no further cost increases in 1961. I have my fingers crossed on that one.

Senator FONG. Does it assume also that the increase that you have asked for, 12½ percent, will be sustained?

Mr. SEVIER. We don't know. That is up for decision by the Board, and we haven't any idea not only what the decision would be but when it will be rendered.

Senator FONG. My question to you is this: Your anticipated loss of \$2-million-some-odd is based on the fact that you will take into consideration the fact that your request for an increase will be granted?

Mr. SEVIER. The 12½-percent increase?

Senator FONG. Yes.

Mr. SEVIER. Yes, sir. We are assuming that we will not have to rebate or refund any of the 12½ percent that was granted to us in September of 1959, subject to a hearing.

Senator FONG. And the State of Hawaii has filed an objection to that, is that correct?

Mr. SEVIER. They were rather vigorous in their protest; yes, sir.

Senator FONG. And now you are saying to this committee that even with that increase of 12½ percent, you anticipate a loss of approximately \$2 million and more?

Mr. SEVIER. That is correct. And furthermore, even with that 12½ percent which we enjoyed throughout 1960, we lost \$35,000 on \$71 million revenue, with the 12½ percent.

Senator FONG. And now you have an increase of 10 percent which you are speaking of. Do you anticipate you will come out even in 1961?

Mr. SEVIER. We anticipate that we will have a modest profit but not in excess of anything that was authorized by the Board in docket 808.

Senator FONG. What would that amount to as far as your capitalization is concerned? What percentage?

Mr. SEVIER. In the neighborhood of 7½ percent.

Senator FONG. When do you expect to file this request for an increase?

Mr. SEVIER. We have our accountants here now, and attorneys. We will meet with the Board probably on Wednesday. We have already had preliminary discussions with the regulatory section. And as soon as our figures are finalized and verified—we have submitted the figures that we have prepared to date to the Board and to the State—we would expect to file this week sometime.

Senator FONG. Is there any possible way of deferring it for a while until this hearing has been concluded?

Mr. SEVIER. If you will give us a special appropriation so that we can stay in business.

Senator FONG. That I can't promise you.

I have no further questions.

Senator BUTLER. Mr. Chairman, I have one further question.

Mr. Sevier, on the second point that you made under your general heading of No. 6, I think it is, suggestions for Federal assistance, the second point is that you be given the right to make agreements with other carriers the same as the railroads now do, and have a shipment go on a joint rate from the origin to destination. I can see how

that would simplify the handling of claims and it would certainly fix single carriage responsibility. But how would that result in an increase in your revenue?

Mr. SEVIER. It doesn't, necessarily. We feel that it is of more benefit to the shipper, the consignee, than it would be to the carrier. At the present time we can't offer that service to the trade, which we believe they are entitled to have. We can't offer it because neither the ICC nor the Federal Maritime Board will take jurisdiction. I think in Alaska you have a somewhat different situation. I am not too familiar with that. But I know in Hawaii we can't make a through arrangement of the kind that is contemplated by the joint board bill.

Senator BUTLER. Who would object to that arrangement being made? Would anybody be hurt by that?

Mr. SEVIER. I believe you held hearings, some committee of Congress held hearings last year on that.

Senator BARTLETT. Hearings were held before this committee. The Senate did pass a joint board bill. No action was taken in the House of Representatives.

Senator BUTLER. I can't see objection to that type of relief if it is going to help you.

Mr. SEVIER. I think it would help Hawaii a great deal.

Senator BUTLER. I will join with the Senator from Hawaii and we will see if we can't push it through again and get after the House.

Mr. SEVIER. It would be good legislation, and both ICC and the Federal Maritime Board favor it, I believe. I think the railroads probably, and the trucklines may have some objections.

Senator BUTLER. It would seem to me that that would be good legislation, and that it would simplify the shipper's shipping procedures.

Mr. SEVIER. It would. Today it is a very awkward arrangement.

Senator BUTLER. I have no further questions, Mr. Chairman.

Senator BARTLETT. I think I might say in reference to the joint board that, for information purposes, the truckers generally approved it, and that the ICC had some substantial doubts which have now been, if not removed, diminished, so that prospects for some future affirmative action are much better than they were in the last Congress.

Mr. SEVIER. I see.

Senator BARTLETT. Mr. Sevier, in the concluding sentence of your statement you said:

We are confident that with the joint efforts of the Federal and State Governments, labor, management, and users of transportation service, workable solutions can be developed.

For my own part, after two full hearings and this third hearing underway now, I would want to strike the word "confident" and replace it with "hopeful."

Mr. SEVIER. I think that is probably more realistic.

Would you feel that today, if I may say so, Mr. Chairman, we have not had at all times that joint effort that is referred to there. If we would get in and move in the same direction, I think there would be a better chance.

Senator BARTLETT. I think this is the first time, as far as I am aware at least, that this joint effort has been attempted without creating a forum in which recriminations instead of constructive suggestions are put to the forefront.

You quoted, on pages 3 and 4 of your statement, Dr. Shoemaker; and on page 4 the quotation was in these words:

I would say that there is, in my view, no question but what there will be a substantial advance in this economy.

Mr. Sevier, I don't ask you to speak for Dr. Shoemaker, but I am wondering what might occur to cause continued substantial advances in the economy of Hawaii?

Mr. SEVIER. Neither can I speak for him, Senator. I have talked to Dr. Shoemaker many times. We used the quote in here to merely emphasize the fact that people who have studied the problem intimately in Hawaii—and I am sure Dr. Shoemaker would be in that category—feel that the economy is sound and will continue to grow.

I believe that that is based in substantial measure on hopes that the tourist industry will continue. As you know, Hawaii has a delightful climate. I could put on a nice sales talk here, if you would be interested. It is a 12-month recreation area. It does have an appeal to the traveler. It is a way of conserving the gold outflow, since it is all in our own economy. I think there is a good deal of hope that that will take up the slack that might result from some decline in the sugar and pineapple revenues or other types of revenues. There have been new industries attracted there in recent months. The Standard Oil Co. has completed a \$60 million project for an oil refinery. Two cement plants have been constructed, one with mainland capital, one partly mainland and partly island capital.

There have been other small industries starting up there, and I think there is some reason, some ground for hope that the economy will continue to prosper.

Senator BARTLETT. I wasn't seeking to dispute his conclusion, but merely to verify it from you. You agree that tourist expansion offers the best foreseeable opportunity to cause the economy to increase and to enlarge.

Mr. SEVIER. I do, sir. I do feel that the economy has several legs to it, as you know, supported by agricultural commodities, agricultural production, by the military, the military spending, the Government installations there, and by the services and tourists. I think the latter is probably the most reliable of those supports.

Senator BARTLETT. As expressed on page 8 of your statement, "the level of rates for Hawaii's essential freight services have not had a serious, adverse effect on the economy." That was the quotation from your statement.

Mr. SEVIER. Yes, sir.

Senator BARTLETT. Do you believe that further rate increases might possibly have that adverse effect?

Mr. SEVIER. Yes, Mr. Chairman, I am confident that there will come a time, if rates keep going up and spiralling, and all other costs go up proportionately, or even to a lesser extent, there will come a time when they will become extremely burdensome. They do have an effect. It would be foolish to say they have no effect, because you can't transport goods 2,400 statute miles without incurring some costs, and that has to be borne along with other costs.

So it does have an effect. We don't think it has the damaging effect that some believe they have. Some of our exhibits are quite clear. Using information supplied by the State on the difference in costs

between the mainland and Hawaii, we have attempted to show, in exhibit 4, that the freight has been a small part of that.

Senator BARTLETT. It is my indistinct recollection that the rate increases for Hawaii since the end of the war have been on the order of 89 percent, or was that in error?

Mr. SEVIER. Our rates have gone up on the average, since 1946, 150 percent. I believe the State used a figure of 172. But that was more on general merchandise. But on the average it has been 150 percent.

Senator BARTLETT. 150 percent?

Mr. SEVIER. Yes.

Senator BARTLETT. Let me ask you this: Have the numbers and degrees of those rate increases been on an accelerating basis? By that I mean this: Have the greater number and have the greater percentage amounts been applied in the last, say 8 years?

Mr. SEVIER. I may have something on that.

Senator BARTLETT. I ask that because generally it seems that this has been the case, that these rate increase requests have come with greater frequency in the last few years.

Mr. SEVIER. I have here a record that we prepared in anticipation of some questioning on that.

On March 10, 1947, we had a 20-percent rate increase.

September 1, 1948, we had a 10-percent increase.

February 1, 1951, a 10-percent increase.

January 14, 1952, a 7½-percent increase.

March 1, 1953, an 8½-percent increase.

March 19, 1955, a 6-percent increase.

February 1957, 9 percent.

July 1957, 13.42 percent.

I am lost there. I don't know which that should be. I think the Board allowed some of the rate increase to go into effect, and then held a hearing and granted the balance of it, that is my recollection.

January 1958, 9 percent.

January 1959, 12½ percent.

Senator BARTLETT. That would seem to reveal, then, that before 1953, rates increased a bit less than 50 percent between the end of the war and that period, and a little over 100 percent since then. So this tends to prove, does it not, that the problem is becoming aggravated and inflationary pressures are to be noted more by Matson in the last 8 years than in the previous 7.

Mr. SEVIER. I haven't chartered this out or plotted it out, but it would seem that the curve is fairly steady, Mr. Chairman. Our costs have gone up that same way. I believe it is safe to say that the standard of living in Hawaii has increased, and the per capita income has likewise gone up. This Consumers Price Index that I mentioned earlier on the cost of living in Hawaii, only the city of Cincinnati had a lower increase in the Consumers Price Index than Honolulu.

Senator BARTLETT. Would you not agree with me that although it may well be true, as you stated on page 8, that freight costs do not constitute a large part of the retail prices, nevertheless when a rate increase is made, this tends to have a pyramiding effect on the cost of living. It isn't only the added cost of carrying the freight; it is that others, down to the person who sells to the ultimate consumer, are likely to and may be forced to add to their prices. Is that a fair statement?

Mr. SEVIER. I think that is a fair statement, Mr. Chairman. I couldn't quarrel with that. I think any increased cost that is passed on to the consumer does pick up a little bit of something all along the line. If the status quo could be maintained it would be a much better situation.

The last thing we want to do, I might say, is to raise our freight rates, because it doesn't bring us any happiness. They don't put a lei around our neck in Hawaii when we announce that we are going to raise freight rates. It is a very unpleasant experience so far as we are concerned. But we have to cover our freight costs with freight revenues. We have no alternative to that.

Senator BARTLETT. I think the committee quite understands your situation.

Another reason why you wouldn't want to raise rates unless you felt obliged to is because this would subject you to competitive pressures that otherwise might not be imposed.

Mr. SEVIER. That is correct.

Senator BARTLETT. You quoted Dr. Hicks, who implied in his statement as to the cost of living in Hawaii that the absence of need for winter clothing and heating homes and such might counterbalance the higher cost of imported consumption goods and residential land. But it is a fact, is it not, that the Bureau of Labor Statistics of the U.S. Labor Department revealed the cost of living in Hawaii to be substantially higher than in any city on the mainland?

Mr. SEVIER. I have done no research on that, Mr. Chairman, at all. I realize that the Federal Government does pay a cost-of-living allowance to Federal employees there, but whether that is based on BLS statistics, I don't know. If that is a fact I will accept it as such.

Senator BARTLETT. That is the case; yes.

How about private industry? Does private industry have to pay its employees in Hawaii, notably in Honolulu, a cost-of-living allowance greater, for example, than might be paid in San Francisco? Do you know?

Mr. SEVIER. No. Our personnel, we in our office in Honolulu have the same salary administration program for the employees there as we do in San Francisco. The starting salary for monthly employees, I believe, is the same. We make no cost-of-living allowance. We do recognize when a person is transferred there that he has some problems and we try to recognize that and help him in those problems of transition, but not in the basic wage. People doing comparable work in one place get the same salary as in the other.

Senator BARTLETT. I don't know whether any other companies do this in Hawaii, either, but I do know that several, maybe all of them, do in Alaska—Standard Oil, Pan American Airways—and I will seek elsewhere information on that point as to whether there is a cost of living paid to private employees in Hawaii.

Mr. SEVIER. If I could just check?

Senator BARTLETT. Surely.

Mr. SEVIER. I was just checking with Mr. Stanley Powell, executive vice president, who might be more familiar with that. He confirmed what I said was correct.

Senator BARTLETT. If you don't have it readily available, we can get it elsewhere if we need it.

On page 14 of your statement you referred to the modernization methods that Matson has employed. It was stated here last week, and there is no dissent from anyone on the committee, Mr. Sevier, that these carriers engaged in so-called offshore trades have led the entire American merchant marine in this field, containerizing and the like, and all of you, in my judgment, are to be complimented for your forward-looking attitudes and actions in that area.

However, it has occurred to me that there is so much you can do in respect to modernization, and using new methods, such as containers, and no more. There will be a period when you will just have to use what you have. And then again there will be, will there not, an adverse effect on the consumer in Hawaii if general costs continue to rise and you cannot make savings such as from 13 percent to above 31 percent? There is a point of no return on that; is there not?

Mr. SEVIER. Well, yes. I presume we will reach a point where we will have modernized everything that is suitable for that. Then we will have to look into new design. We have, as I mentioned, a very well-staffed, competently staffed research department which, among other things, works with shippers and consignees in suggesting ways that they might change their packaging or shipping methods, movement of cargoes that lend themselves to bulk carriage and that type of thing. We do a good deal of research on that for the benefit of our customer.

We feel that the ocean transportation part of serving an island area of this magnitude is only a small part of the total movement of that cargo from factory to consumer. We therefore are interesting ourselves in more than just the part that we perform.

That is why we suggested some of these joint rates. We suggested legislation that clears up the point of jurisdiction and responsibility in the port areas. We believe that there is money to be saved in various areas that really aren't our particular business. We are trying to point those things out in an effort to reduce the landed cost of merchandise in the State of Hawaii.

Senator BARTLETT. You surely are to be congratulated for having instituted this research department. I think that is wonderful. But there will come a time, of course, when they can make only refinements upon the methods to which you have referred, and we can't hope for the dramatic results which have been apparent in the last few years.

Mr. Sevier, how many troops can the *Lurline* and *Matsonia* carry? Or how many did they carry during the war?

Mr. SEVIER. During the war they carried in the Atlantic trade—we had two in the Atlantic trade and two in the Pacific—we had four ships of comparable size—they carried roughly 6,000 troops each.

Senator BARTLETT. What happened in September 1960 when you had counted upon a million dollars worth of Federal Government business in transporting dependents and that was withdrawn? How did they send those people over?

Mr. SEVIER. By air, by military air transport, largely, and also MSTs surface transport.

Senator BARTLETT. You said that you don't know how you are going to maintain those liners in the Hawaiian service because of the mounting costs and obsolescence. If you are not able to make any arrangement for modernizing them, how long will they last?

Mr. SEVIER. Of course, the cost of maintaining them increases as the vessels get older—the tax life of the *Lurline* will be complete in another 2 years. She can probably operate without major expenditure for probably the balance of this decade. The *Matsonia* will be somewhat longer, but that ship has been more recently renovated and a great deal more money spent on it in 1957.

Senator BARTLETT. If you went out in the money market and sought capital for the construction of new passenger liners, would you (a) in your opinion be able to secure it, and (b) if you didn't build those ships would you be able to keep the rates low enough so that people would travel on those ships?

Mr. SEVIER. I am afraid not, Senator. I say that with a good deal of regret, but I just do not believe that we would be able to get financing under title 11 or any other type of financing because I don't believe we would prove the economic feasibility of such construction. It would cost approximately \$40 million to replace either of those ships. And even if we had construction subsidy of—55 percent, is it now, Senator Butler?

Senator BUTLER. On a temporary basis.

Mr. SEVIER. Even if we had 55 percent, I doubt we could justify the investment.

Senator BARTLETT. You would have to charge the passenger much more than you do now if he were to go on a brandnew ship?

Mr. SEVIER. Probably not, no; I would think not. I think we might be able to, in a new ship design, eliminate certain things, certain stations that now have to be manned. We could eliminate those, perhaps reduce the crew, which would perhaps reduce the cost somewhat. We have less manning, for instance, on the *Matsonia* than we have on the *Lurline*.

Senator BUTLER. But your only hope of securing financing of those vessels would be through insurance?

Mr. SEVIER. That is right.

Senator BUTLER. You are not entitled to differential subsidy?

Mr. SEVIER. Oh, no; no. That is pie in the sky. I realize we don't have a construction differential subsidy available to us, but I said if we did even then it wouldn't be economically feasible and certainly would not be on a domestic operation.

Senator BARTLETT. Senator Fong?

Senator FONG. Mr. Sevier, you alluded to possible Federal assistance for the Hawaiian shipping. And you mentioned the Federal program of modernization for Hawaiian ports, including the possible transfer of military piers 39 and 40 in Honolulu, and also that the Vessel Exchange Act be amended so that a priority would be given on the purchase of turned-in freighters, and assistance in defraying costs of purchase and modernization. You have not stated anything about subsidy; is that right?

Mr. SEVIER. About what?

Senator FONG. About subsidy.

Mr. SEVIER. My only reference to subsidy is that we haven't a position on it. We realize that the existing laws would have to be substantially modified and changed to make subsidy possible, to make it available to us. We would have to see what those changes meant and what they involved.

Our recommendations would be to go along with what other witnesses have said, that this thing should be studied carefully, and then legislation drafted perhaps, and if it were drafted we would then be perfectly willing to testify on that legislation. At the present time we don't know what subsidy would mean.

Senator FONG. Mr. Sevier, you are apprised of the action taken by the Hawaiian Legislature?

Mr. SEVIER. Yes, sir.

Senator FONG. That a subsidy be given to the Matson Navigation Co. so that costs of shipping would be cut down?

Mr. SEVIER. I did not see the bill, but I am aware of the legislation.

Senator FONG. The present cabotage laws, present maritime laws, prejudice Hawaiian residents to this extent: that freight must be shipped on U.S.-flag vessels and may not be shipped by any other vessels; is that correct?

Mr. SEVIER. Cannot be shipped by any other vessels between two American ports; that is correct.

Senator FONG. So that the freight which comes to Hawaii from the west coast or from any American port must be shipped by a U.S.-flag ship.

Mr. SEVIER. That is correct, under existing laws.

Senator FONG. A ship going to Japan—say, flying the Panamanian flag—cannot take cargo to Hawaii.

Mr. SEVIER. That is correct.

Senator FONG. Could you venture a guess, if these ships were allowed to take freight to Hawaii—that is, the Panamanian-flag ships, the Japanese-flag ships, and any flag ship that was operating between the west coast, Hawaii, and the Orient—would there be a saving in cost to the Hawaiian residents?

Mr. SEVIER. There certainly should be, because their operating costs are less than half of the American-flag costs. Their construction costs are less than half of the American-flag costs. And they certainly should charge less freight rate. Our freight rates are based on our costs. If their freight rates are based on their costs, it certainly would be cheaper.

Senator FONG. Without arriving at a percentage, would you say that the people of Hawaii are in fact subsidizing the American merchant marine to that extent?

Mr. SEVIER. Well, I do say here that because of the cabotage laws, and because of the fact that we must employ American citizens, we must buy our ships and equipment from American manufacturers, that that indicates that the subject is a matter of national concern. That is why I commented that I think this committee should be congratulated for undertaking a review of the subject.

However, Senator, I think the record is amply borne out that even though it is subject to some debate and controversy in various places and at various times, it is borne out that that reliance on foreign-flag shipping to carry America's commerce either in foreign trade or domestic trade is rather an insecure way of protecting the customer.

I believe that if the domestic operator is crowded out of the Hawaiian trade and it were left to the foreigners, and they had the opportunity to charge what they wanted, that their rates would be at least as high as ours and probably higher.

Senator FONG. I brought this matter up not that I am against the cabotage laws; I am just as much for the cabotage laws as you are. I feel that we should have a strong merchant marine. But I brought it up just to show that the Hawaiian residents are subsidizing a part of the American merchant marine to that extent. That being so, it would not be fair to the Hawaiian population to bear all the costs of the transportation, would it?

Mr. SEVIER. It would seem that there is some justification in the State's position for the Federal Government to interest itself in the problem. And I think that Senator Bartlett's committee is to be commended for making such a thorough examination of it.

However, I think these things are all subject to rather sudden change. Freight rates, where freight service is being rendered by disinterested parties. That is certainly what the foreign-flag operator would be, or even a subsidized operator under the American flag in foreign trade. His principal objective is his destination.

We are a destination carrier. Our service is to Hawaii, with turn-around service. We turn around and go back again. So we have a vital interest in it. And I think that more attention, therefore, would be given to it.

I agree with you that if we can get some relief, it is a fine thing. But you raised the question of foreign rates. I teletyped our office on Saturday and asked for some information which came in this morning. It is rather interesting. I will agree that I wouldn't want to swear to this or vouch for it, because it is subject to many variables. All trades aren't the same, volume has a factor to it, and so on. But we checked on rates.

I believe the question may have arisen last Monday or Tuesday, here, on freight rates of subsidized lines. In the Caribbean area we took some distances. New York to Cartagena, a distance of 1,800 nautical miles. I have no idea of the Cartagena imports or exports, or the volume, or anything about it. But the distance is 1,800 miles, which is 300 less nautical miles than our service. The n.o.s. merchandise rate is \$70 a ton, weight or measurement.

New York to Trinidad, 2,000 nautical miles: the merchandise n.o.s. rate there is \$56.80, weight or measurement.

These are subsidized lines, American-flag subsidized carriers. Our rate for 2,090 miles is \$25.76.

We have another conference rate, New Orleans to Kingston, Jamaica, a distance less than ours. That is \$72, weight or measurement. That is the subsidized carrier or foreign-flag carrier. It is the same rate.

As I say, those aren't exactly comparable with the Hawaiian situation, but they are indicative of the fact that freight rates vary. Our rates have been fair and reasonable, we believe, even though they have been going up.

Senator FONG. To the extent that the Hawaiian population is paying more for this freight rate than it would be paying if foreign vessels were allowed to operate between the two ports, would you say that it would be fair that the National Government should bear a portion of that expense, although you have not stated whether it should be subsidy or otherwise? You are saying that some relief should be given in that respect?

Mr. SEVIER. I am sure Senator Bartlett's questioning led to the point that sooner or later these rates will become burdensome. I think when that time comes—if it is here now and it can be demonstrated that it is here now—perhaps this is the time for Government aid. I believe the subject should be discussed and studied further.

I don't believe we are in a position to say that we should have help. We don't believe that the impact of our rates at the present time is that serious. They are serious; of course, any of it is. None of us like costs. I don't like the cost of anything. But we know we have to live with them. We believe some of the suggestions that we have made here, in these five or six points at least, would enable us to hold the line on costs, at least to assist us in holding the line. I don't believe we can expect a reduction in freight rates, although that would be the day that I hope to live to see, when I can come in and say that we are going to reduce them. Don't count on that, Senator.

Senator FONG. With the present rates that you have, there is a mounting protest in Hawaii due to the fact that these rates are pretty high, isn't that correct, as evidenced by the opposition filed by the Attorney General?

Mr. SEVIER. Senator, I am not being facetious. I don't know whether this is political or whether it comes from the consumer, or just where it comes from, but I will admit that there has been opposition.

Senator FONG. You know further, that with your request for another 10 percent, that there will be further opposition?

Mr. SEVIER. I suspect it. I am going down next Friday. I will probably hear all about it.

Senator FONG. And you wish this committee naturally to study the problem, and if relief can be given in the matter of subsidy, it is for the committee to decide.

Mr. SEVIER. I believe that is correct.

Senator FONG. Thank you.

Senator BARTLETT. I have a good many more questions here, Mr. Sevier. I am not going to put them to you, nor will the staff members ask the questions they have prepared, because we have kept you on the stand for almost 2 hours now. With your permission, we should like an opportunity to submit questions, perhaps in writing, to you, and you can reply at your convenience.

I will only say, in concluding, that the problem is, in my opinion, as related by Senator Fong, a national one. And it is national from two standpoints: The continuing development of the economies of Puerto Rico, Hawaii, and Guam, and Alaska, and national defense needs. Senator Butler said he thought there would be grave difficulties in persuading the Congress to adopt a subsidy program and I have no doubt that that is the case. This would be revolutionary but we may have to adopt some revolutionary tactics. The suggestions that you made to the committee will be carefully considered, as they ought to be, because they are constructive in their nature.

I do want to say, however, that no matter how desirable a Federal program of port modernization for Hawaiian ports might be—and I don't doubt at all that it is desirable—it will perhaps be almost as difficult to go into a new area such as that as it would be to approach the broader problem to which Senator Fong and I have made previous reference.

Thank you very much, Mr. Sevier.

Mr. SEVIER. Thank you, sir.

I would be very happy to furnish any material or any information that the committee wants and would welcome any questions that you have to submit in writing.

Senator BUTLER. Thank you, Mr. Sevier.

Senator BARTLETT. Now we turn north. The next witness is Mr. D. E. Skinner, president of the Alaska Steamship Co., a company that has some interest also in this problem.

We are glad to have you here, Mr. Skinner.

STATEMENT OF D. E. SKINNER, PRESIDENT OF ALASKA STEAMSHIP CO.

Mr. SKINNER. Thank you, Senator.

Mr. Chairman and members of the committee: I am D. E. Skinner, president of the Alaska Steamship Co. I should like to say in preface to my following remarks that having heard the testimony which Mr. Sevier gave on behalf of Matson Navigation Co., we would subscribe to all of the recommendations that Matson made in connection with the Hawaiian trade. We would subscribe in principle to those recommendations as they apply to the Alaska trade.

We appreciate this opportunity to meet cooperatively with your committee to try to work out some long-range solutions of the shipping problems of the domestic noncontiguous areas. We are pleased to note that the nature of the testimony in these hearings with one exception has been constructive rather than destructive and it is in the former spirit that we offer our comments.

We agree with the State of Alaska in favoring the establishment of certificates of convenience and necessity for both common and contract water carriers in the noncontiguous trades in much the same way Congress has recognized their need in other domestic areas. In the 65 years that we have served all of Alaska, over 130 carriers have come and gone from that trade and for good reasons. The great distances and small tonnage available present a unique problem to any carrier. Probably nowhere else in the world does a private common carrier operate in a trade that provides him with less than 1 ton of cargo for every mile traveled. In addition there are the inherent hazards of the operation, such as one-way haul, seasonality, and the number of small ports. This pattern of maritime carriers coming and going in the Alaska trade over the years has worked a real hardship on all concerned. Each one of them has skimmed some of the cream off the trade and many of them have assumed little or no responsibility. Meanwhile, this surviving common carrier has been left to provide the reliable service that the Alaskan economy requires.

As a responsible common carrier serving Alaska it has long been our determination to provide complete service. To implement this goal we have spent substantial sums of money seeking the most complete service that the people of the area could afford. Not all of our efforts have been successful but they all were part of our determination to provide comprehensive, frequent, and regular service at a reasonable rate.

We have continuously sought to devise improved methods of cargo handling in order to reduce costs. One of the key factors in this search for economy has been to pioneer for all the transportation industry the use and application of containers on board ships. Our actual experience with vans began in 1953 and since that time we have invested approximately \$3 million in ship improvements and company-owned containers, and in addition at least another \$3 million worth of equipment to implement this program.

Confirming our judgment on the future of "contained cargo shipments" we then sought to develop a complete containership which could accommodate both rail freight cars and vans. Notwithstanding the fact that we had the affirmative support of MARAD and the Department of Defense we were forced to abandon the project because the cost together with the tonnage forecast would have necessitated a rate beyond the ability of the Alaskan shippers to pay.

Being forced to abandon the roll-on, roll-off ship we continued to accommodate and expand the container program to our existing fleet. In 1957, for example, we carried 1,129 24-foot vans to Alaska. By 1960 this figure has increased to 8,445. This does not include a many times larger movement of smaller-sized containers ranging from 4 to 12 feet in length. This has been of great importance to the Alaska consumer because the van program has reduced both the frequency and amount of rate increases. Constant improvement of efficiency in cargo handling is necessary if we are to survive in a labor market whose cost in the last 14 years has increased 137 percent. You can appreciate the effect of this large increase on our trade where 73 percent of our operating expense dollar is paid for direct labor. In view of these substantial wage increases, I believe the carriers should be complimented rather than criticized for limiting general tariff increases to 56 percent over this period of time. The last 3 years of our passenger operation, 1952-54, were conducted at a loss of \$1½ million. Appreciating the value of tourism to the Alaska economy we made futile efforts to increase the volume of traffic as well as to get off-season patronage or use for these vessels. Since that time there has been no American passenger service to and from Alaska.

In 1958 we purchased lighterage equipment in the Nome area for \$500,000. This investment was made in spite of a depressed local economy and no indication of any improvement in sight. The principal objective of the purchase was to assure the people of that area continued complete water transportation service even though the volume of traffic did not give any promise of a return on this investment.

We submit that 45 percent of our trade is devoted to unprofitable voyages, but no responsible authority in either the Government of Alaska or Washington, D.C., has suggested we abandon these services, or even indicated a method by which these routes could become profitable. It is, of course, true that such service is of benefit to the State of Alaska as well as to the Defense Department of the United States.

The greatest need in Alaskan water transportation is stabilization. The laws and regulations should apply alike to all. We strongly recommend to your committee that the Federal Maritime Board should be given sufficient effective personnel to actively police and enforce existing statutes. We need adequate enforcement and more

intelligent regulation and inspection of both contract and common carriers in this Alaska trade which has numerous totally or partially unregulated and uninspected carriers.

The Alaska trade is not only plagued by the unregulated financially irresponsible operator, but also by Government competition. For many years the Bureau of Indian Affairs has conducted an operation in Alaskan waters to service the native schools and hospitals. We ask this committee to study the operation to determine whether or not we could provide this service more economically for the Government.

Similarly the State of Alaska is currently considering authorizing the expenditure of about \$23 million for the operation of a ferry system. We do not oppose this but we feel we must point out to this committee the impact that such an operation might have on the Alaska maritime situation. To the extent that these ferries haul cargo they will not create new tonnage, they will only further subdivide that which already is too small.

All Federal agencies require certain minimum standards for contracting with builders or suppliers. We think that this committee should recommend that such a program be extended to the common carriers who are required to conform with all Federal laws and regulation. Thus if a Government project is to be built in Alaska, various statutes having to do with wages, working conditions, et cetera, are a necessary part of contracting with the Government. We ask that the Government show the same consideration by following the same procedure in their contract award so that an integral part of any contract be the shipment of materials and supplies on carriers who are serving Alaska in compliance with all Federal laws and regulations.

We seek more expeditious rate hearings and determination of simpler, more definite, and uniform regulatory rules. The use of the operating ratio theory is a possible solution but in any event it is important that we have fixed formulas to determine "capital necessarily employed" and a "fair rate of return." We are pleased to hear the Chairman of the Federal Maritime Board report that he feels he has answered the criticism of Dean Landis on what he termed the "inordinate delays in the disposition of adjudicatory proceedings before substantially all of our regulatory agencies." The Federal Maritime Board Annual Report for 1960 shows 795 proceedings pending at the start of the year, and 901 on file at the end of the year. Every trade represented in these hearings has had to contend with long-drawn-out hearings, several of which have been in process over a year at this moment. We would be opposed to any legislation that might cause additional unnecessary delays.

We feel that the Federal Maritime Board can further stabilize our operations by stating and defining more clearly the criteria for suspension of applications for a general rate increase. Similarly there have been altogether too many rate investigations that have repetitiously covered the same subject matter at great loss of time and money to the State, Federal Government, and the carriers. To correct this we advocate a clearer and firmer statement of reasons or grounds for initiating and dismissing investigations, without infringement on the right of any parties to file formal complaints.

We endorse the position of Chairman Stakem seconded by Senators Bartlett, Fong, and Long as well as the State of Alaska that repeal

of the cabotage laws is undesirable. At the same time, we wish to call to the attention of this committee that these cabotage laws do not protect our noncontiguous trades equally. Alaska faces a present threat of foreign-flag competition not true of any other of these areas because of the third proviso of section 27 of the Merchant Marine Act of 1920.

We maintain that Alaskan maritime transportation rates do not have as much impact on the prices or economy of Alaska as is often contended. The water transportation charges of all carriers were increased on January 10, 1960. The University of Alaska Agriculture Extension Service, in cooperation with the U.S. Department of Agriculture, publishes a quarterly report on Alaska's food prices. I have appended to my statement an attachment (No. I) showing the market basket prices in various cities in Alaska and Seattle during December 1959 and March 1960 and the freight revenue which would accrue to Alaska Steamship Co. if it transported the 40 food items which comprise the market basket. Obviously since the water transportation charges increased on January 10, 1960, and since the market basket price or cost to the housewife in the cities shown was increased in some instances and decreased in others, the transportation charge which must be a component of the final price or cost is certainly far from a controlling or even dominant factor. For further comparisons I have attached exhibit No. II.

We agree and heartily endorse the suggestion of the Federal Maritime Board for a precise study of the relationship of the ocean carrier's charges to the ultimate consumers' costs. We feel this would bring out many unregulated items and show that ocean transportation costs are not as significant a factor as often claimed. In our opinion the problem is not that transportation costs are too high, but rather that transportation is necessary at all. I have attached a list of five food items (No. III) mentioned by the State of Hawaii to show the great disparity between price differentials and transportation costs. We join with the Federal Maritime Board and the Matson Navigation Co. in recommending the passage of regulations establishing a joint board. This would then allow water carriers to offer through rates and joint rates with carrier subject to the jurisdiction of the ICC and CAB.

I have attached a list of the 62 ports (No. V) of call for the year 1960 to show the extent of our Alaskan operations.

I have also attached a comparison of freight rate increases from 1947 through 1960 (exhibit No. IV) in several trades to correct and complete figures introduced into these hearings in various contexts. In the case of Alaska this shows the general across-the-board increases and does not include many rate reductions made by our company during that period. These include reductions on groceries, household goods, and a dozen other items as well as reduced charges for container cargoes and our assumption of cargo insurance formerly paid by shippers.

If the foregoing suggestions are favorably acted upon by your committee and the Government agencies involved, we feel that the concepts of subsidies, either construction or operating, as presently constituted and administered do not adapt themselves to our trade at this time.

(Exhibits I through V follow.)

EXHIBIT I

§ "Market Basket" retail prices of listed 40 food items in Alaska cities and Seattle from "Quarterly Report on Alaska's Food Prices" in December, 1959, and in March, 1960, published by University of Alaska Agriculture Extension Division.

* Freight revenue accruing to Alaska Steamship Company for transportation of the 40 "Market Basket Items" ship's tackle receipt and delivery.

Seattle	Dec	\$16.74
	Mar	\$16.64
Ketchikan	Dec	\$19.44
	Mar	\$19.48
Petersburg	Dec	\$20.42
	Mar	\$20.36
Juneau	Dec	\$20.74
	Mar	\$20.17
Seward	Dec	\$21.87
	Mar	\$22.07
Kodiak	Dec	\$21.97
	Mar	\$22.30
Anchorage	Dec	\$21.86
	Mar	\$21.16
Palmer	Dec	\$22.10
	Mar	\$21.56
Fairbanks	Dec	\$24.68
	Mar	\$24.80
Nome	Dec	\$28.15
	Mar	\$28.37

EXHIBIT II

Tabulation of retail shelf prices effective Mar. 7, 1961, on so-called market basket food items from a grocery chain which has stores in both Anchorage, Alaska, and Seattle, Wash.

[Figures in parentheses indicate number of units]

Food item	Unit	Price, Anchorage	Price, Seattle
Flour.....	5 pounds.....	0.85	0.59
Rolled oats.....	42 ounces.....	.77	.59
Corn flakes.....	12 ounces.....	.33	.27
Bread.....	1½ pounds.....	.47	.34
Round steak.....	Pound.....	1.39	1.19
Chuck roast.....	do.....	.89	.69
Ground beef.....	do.....	.69	.55
Bacon, sliced.....	do.....	.89	.73
Luncheon meat.....	12 ounces.....	.75	.60
Frying chicken.....	Pound.....	.89	.55
Milk.....	Quart.....	.45	(2).49
Ice cream.....	do.....	.65	.43
Butter.....	Pound.....	.80	.73
Milk, evaporated.....	14½ ounces.....	(2).37	(3).47
Eggs, large AA.....	Dozen.....	.67	.55
Strawberries.....	10 ounces.....	.35	.25
Orange juice.....	6 ounces.....	.35	(2).49
Apples.....	Pound.....	.33	(2).45
Bananas.....	do.....	.37	.17
Oranges.....	do.....	.39	.21
Potatoes.....	do.....	.223	(5).39
Onions.....	do.....	.19	(3).29
Carrots.....	do.....	.25	(2).29
Lettuce.....	do.....	.39	.19
Cabbage.....	do.....	.29	.10
Tomatoes.....	do.....	.59	.29
Orange juice.....	46 ounces.....	.79	.57
Peaches.....	2½ can.....	.43	.33
Fruit cocktail.....	303 can.....	.33	.27
Peas.....	do.....	.29	(2).43
Tomato soup.....	11 ounces.....	.17	(4).45
Pork and beans.....	16 ounces.....	(2).45	(2).31
Jello.....	3-4 ounces.....	(3).35	(4).37
Baby food.....	4½-5 ounces.....	(6).73	(6).63
Coffee.....	Pound.....	.79	.75
Shortening.....	3 pounds.....	1.03	.87
Oleo.....	Pound.....	.31	.29
Salad dressing.....	Quart.....	.75	.59
Sugar.....	10 pounds.....	1.49	1.13

EXHIBIT III

Comparisons of 5 food items in 2 Alaska cities and U.S. averages¹

	U.S. average	Ketchikan	Nome	Difference	Freight
Flour (1 pound).....	0.56	0.76	0.99	0.20	0.064
Bacon (sliced) (1 pound).....	.68	.76	.97	.08	.11
Butter (1 pound).....	.68	.78	.97	.08	.021
Potatoes (1 pound).....	.76	.78	1.05	.02	.038
.....	.76			.29	.02
.....	.07	.10		.03	.039
.....	.07		.13	.06	.012
Coffee (1 pound).....	.75	.75		XX	.022
.....	.75		.94	.19	.015
.....					.029

¹ The distance between Ketchikan and Seattle is 649 miles; between Nome and Seattle 2,290 miles. All freight quotations are tackle to tackle.

EXHIBIT V

ALASKA STEAMSHIP CO. PORTS OF CALL, YEAR 1960

Ports shown in parentheses served on regular scheduled basis. Other ports, indicated by asterisk (*), served as tonnage warrants.

*Metlakatla	*Orca (Cordova)	*Kenai
*Waterfall	*Port San Juan	*King Cove
*Ward's Cove	*Port Ashton (Valdez)	*Cold Bay
*George Inlet	(Seward)	*False Pass
*Excursion Inlet (Ketchikan)	(Whittier)	*Sand Point
*Tamgass Harbor (Wrangell)	(Kodiak)	*Squaw Harbor
(Petersburg)	(Womens Bay)	*Chignik
*Kake (Juneau)	*Ousinki	*Dutch Harbor
*Hood Bay	*Alitak	*Captains Bay (Nushagak)
*Chatham	*Jap Bay	(Naknek)
*Pelican	*Port Wakefield	(Port Moller)
*Hawk Inlet (Sitka)	*Shearwater Bay	(Goodnews Bay)
(Mount Edgecumbe)	*Uganik Bay	(Bethel)
(Haines)	*Port Williams	(Nome)
(Skagway)	*Larsen Bay	*Port Clarence (St. Michael)
*Letnikof Cove	*Port Bailey	(Unalakleet)
*Yakutat	*Snug Harbor (Seldovia)	(Teller)
	(Homer)	(Kotzebue)

Senator BARTLETT. Thank you, Mr. Skinner. Assuming that the suggestions that you have made are adopted, is it your opinion that they would go a long way in enabling you to withhold further freight rate increases?

Mr. SKINNER. I would say they would go a long way in helping us to minimize the effect of additional increases in our direct operating costs.

What effect that would have on the freight rate itself, I am obviously not prepared to say at this time.

Senator BARTLETT. You have suggested that in your opinion the freight rates to Alaska do not of themselves constitute the reason for the high costs to be found there, is that correct?

Mr. SKINNER. That is correct, sir.

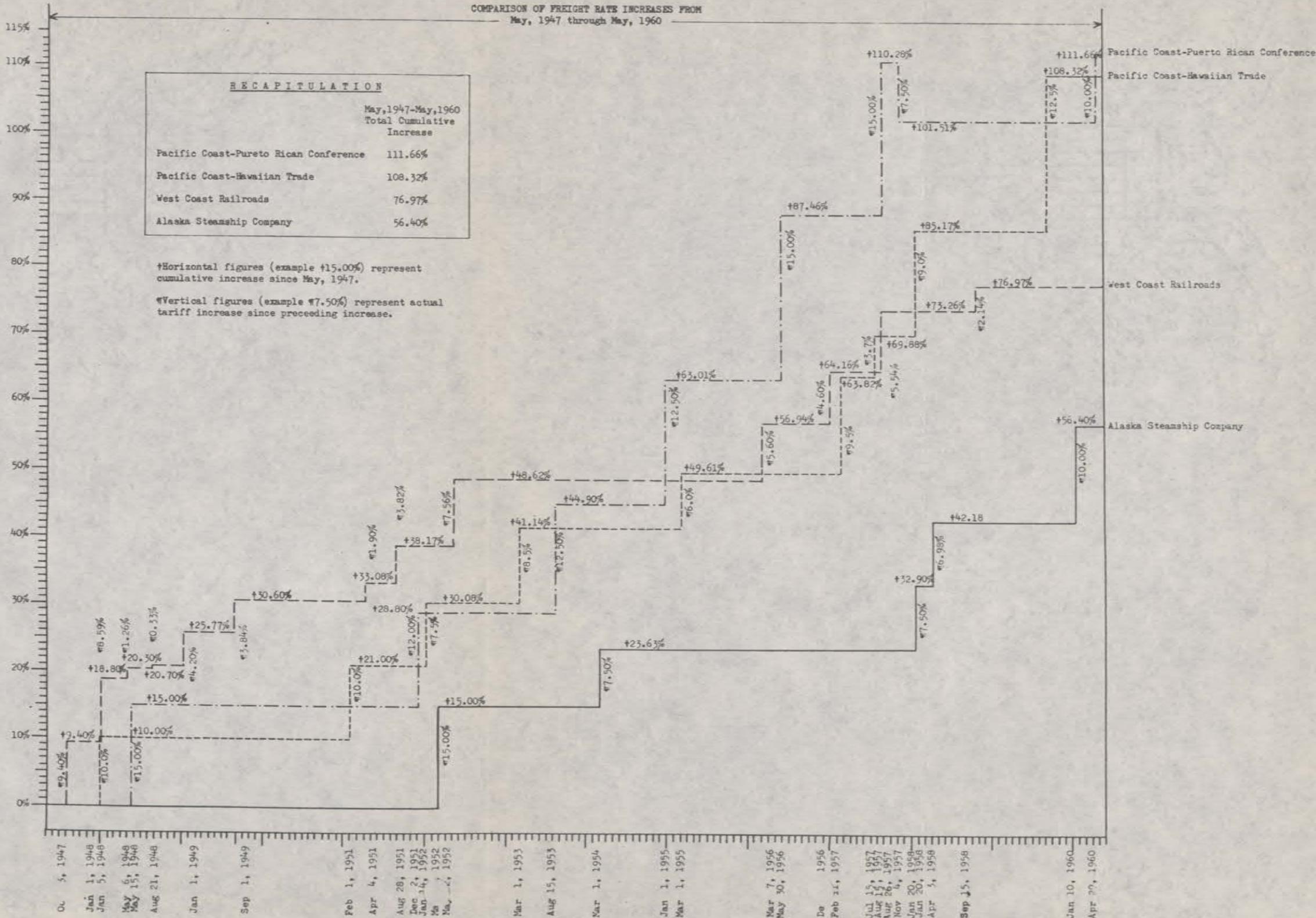
Senator BARTLETT. You and I know, and everyone else knows, that the cost of doing business, the costs of living in Alaska, are indeed very high. What factors do you believe are chiefly responsible for these facts, mindful that the cost of living in Fairbanks is on the order of 150 percent over and above that of Washington, D.C. My recollection is that not too long ago the Corps of Engineers assigned a construction cost for Alaska of about 2.4 times that which would prevail on the average in the smaller and earlier 48 States. What are these factors which taken together account for that?

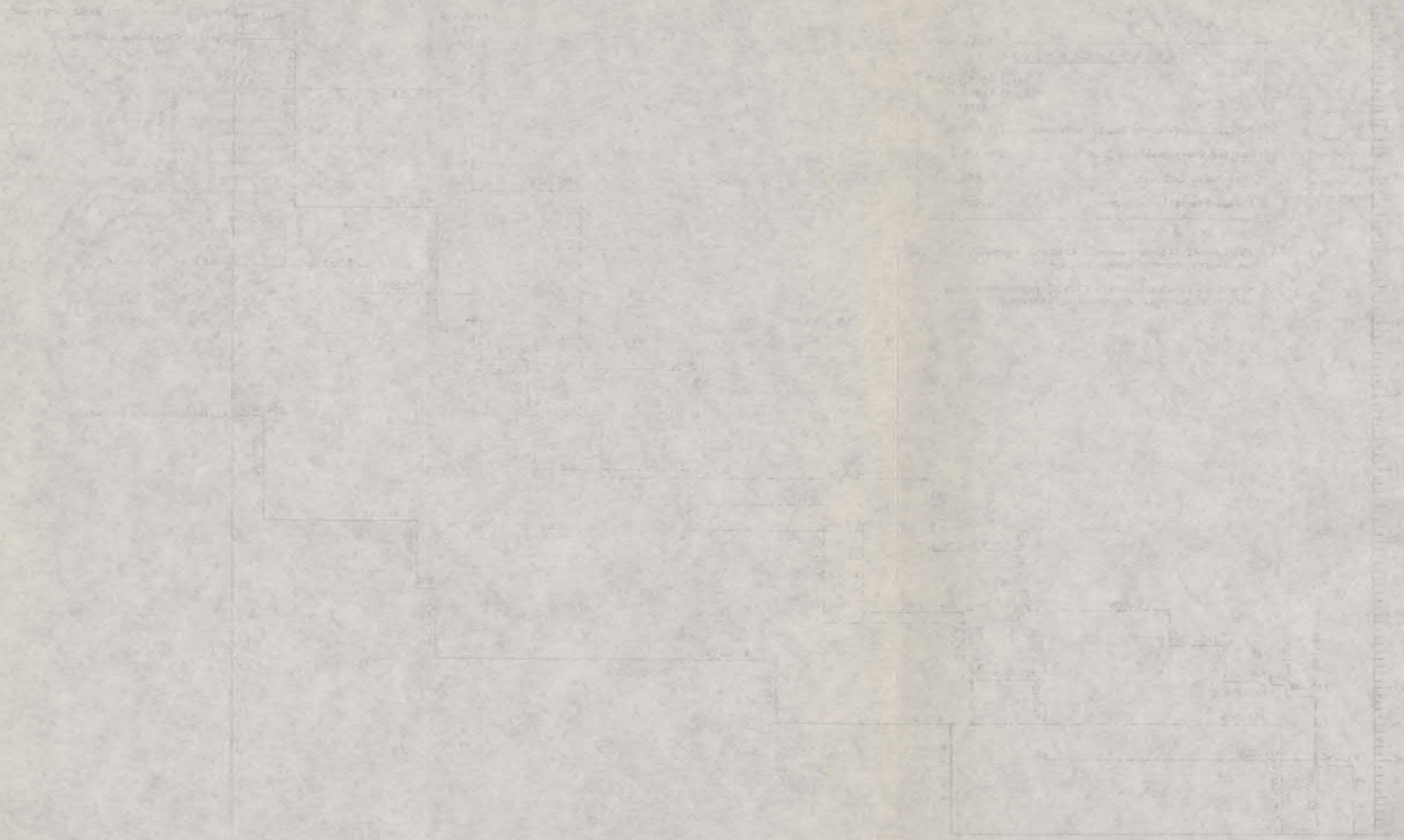
Mr. SKINNER. I think the answer to that would vary, depending on what area we were discussing. So long as you mentioned Fairbanks let us assume it is the railroad area, and I well know the economy up there is pretty well dependent upon the Defense Department. Even though it might be said that it is a blessing that the Federal Government has decided to include Alaska in its defense program, that has been a blessing to the people who have lived there and has been directly responsible for many people moving there from the United States, it nevertheless is a burden also.

I think the fact that the defense program fluctuates as it has over say the past 15 years has contributed certainly to the higher cost of

EXHIBIT IV

COMPARISON OF FREIGHT RATE INCREASES FROM
May, 1947 through May, 1960





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living there than maybe some other comparable area that had in addition to a defense program a normal economy based on local industry. I think a good example in that case would be the Hawaiian Islands, which Mr. Sevier has just explained. The fact that there is such a large territory to serve, and so few people in it means that it becomes impractical economically for people to build large warehouses in the area, making it possible then to ship in carloads of groceries, for instance. The demand is not large enough to justify this expense and, therefore, it requires a frequency of sailings from Seattle, the principal port of supply, to the many areas throughout Alaska. This obviously creates a burden to the water carrier. In order for him to satisfy the trade it becomes necessary to offer at least two sailings a week. In many cases the carrier cannot justify that in view of the fact that the tonnage to so many of the ports is as low as it is. When I say that, to be specific, I would say that over 50 percent of our arrivals in port are for the purpose of discharging less than 200 tons of cargo. I think for most water carriers this would be quite a burden.

Senator BARTLETT. Let us desert the rail belt for a moment and go to Juneau where I believe the Federal Government figures show the cost of living to be something of the order of 25 percent above Washington, D.C.

What factors in your estimation would cause the price to be so high in Juneau in consideration of the fact that on the sea it is only 900 miles north of Seattle?

Mr. SKINNER. In Juneau, as you know, that being the capital of the State, there is very little other industry in that city which contributes to its economy. The fact that the Federal Government, prior to statehood, determined that the people in Alaska were entitled to 25 percent higher salaries than people doing comparable work in the other 48 States, had a great effect, I think, on increasing the cost of doing business in Juneau, because the day the Government decided that those people were entitled to 25 percent more in salaries it automatically meant that other people doing business there also had to meet that salary scale or lose their employees.

This is just one of the reasons. I don't know how far you want me to go.

Senator BARTLETT. If you have any other reasons in mind, we would be glad to hear them.

Mr. SKINNER. I don't think Juneau is necessarily unique. I think that it is representative of the problems that the State has to face.

Senator BARTLETT. You are being subjected to competition at this time and you have been for quite awhile from barge operators, are you not?

Mr. SKINNER. Yes, sir, that is correct. We also are faced with competition in other forms as I testified in my statement.

Senator BARTLETT. You mentioned the operation of the Bureau of Indian Affairs ship, and suggested as I recall that an effort might be made to inquire as to whether this could be done cheaper through your services than is now the case.

Have you made proposals to the Bureau of Indian Affairs citing rates that you would charge?

Mr. SKINNER. We haven't been able to do that because until we knew what service they would wish us to perform it would not be

very easy to tell them how much we would charge. We do know that the Bureau's ship services the same area that we serve on a common carrier basis. We do know that since the need for that service was determined some years ago, the nature of that need has changed also.

You probably recall that that ship had passenger facilities in order to take the natives from and to the villages, and had dentist and doctor facilities on board in order to treat those same natives.

It is my understanding that since that time, with the excellent air service which is being provided, that that ship is no longer called upon to provide the transportation service, and that the medical needs of the natives are handled by taking them to the medical centers from those particular villages.

So I think that now the job of that ship is pretty much a transportation service, transportation of cargo. I see no reason why the common carrier operating in that trade couldn't do that at a great saving to the Government. All I suggested is that we be allowed to study it for that purpose.

Senator BARTLETT. I am going to ask Mr. Goding in that connection to prepare a letter to the Commissioner of Indian Affairs on that subject for my signature or that of Chairman Magnuson, so that we may look into this matter.

Mr. SKINNER. Thank you, Senator.

Senator BARTLETT. Mr. Skinner, you related to the impact of military construction throughout the railroad belt especially. As we know, that is in the process not of being leveled off but of dropping very precipitously. The actual construction dollars to be spent in this field during the coming season are probably not more than 25 percent of last year's, and there will be a further diminution in the following year if the Defense Department plans are not altered.

In light of this fact, if that is what it turns out to be, that military construction will not have the bearing on the Alaska economy that it has had since the end of the war, what is your vision for the Alaska of 50 years from now, if this isn't too abrupt a question? You can say anything that you want, however, because none of us will be around to challenge you if you turn out to be wrong.

Mr. SKINNER. This is one of the few times when I ever had the opportunity to answer a question when I myself won't be here either, in order to eat my words, probably.

Let's look at it from the light of what was Alaska before the war. I would say that we are quite prepared—we wouldn't look forward to it but I would say that we are quite prepared to serve an area such as Alaska, whose demands were no greater than they were prior to 1941. That isn't a very pleasant outlook, but the company I represent has been serving it since 1895, and I think as far as we are concerned we are dedicated to serving it no matter how small or large it gets.

But for me to make a prediction as to what the economy of Alaska would be 50 years from now I think would be unrealistic and would be presuming that I am much more intelligent on the subject than I know I am.

Senator BARTLETT. Mr. Sevier related the operating experiences of Matson during the last several years as to profit and loss. Would you care on behalf of your company, Mr. Skinner, to tell us whether you are losing money or making money?

Mr. SKINNER. I would say that fortunately we have, over the years since the war, certainly ended up in the black. But I could refer to testimony which was introduced in our freight rate hearing in 1958, where a representative from a nationally known bonding house testified that had we, instead of buying Alaska Steamship Co. stock from the Kennecott Copper Co. in 1944, had we taken that same amount of money and bought Government bonds, we would have had a considerably greater return on our investment than the one that we did make.

That is hardly any compensation for the blood, sweat, and tears that those of us who are in the water transportation business have had to put up with since that time.

If you asked me whether or not we would have made the same decision again, knowing what we know now, I think probably we would have, because of our sincere interest in Alaska. But certainly as an investment we are in no different position than the Hawaiian trade.

Senator BARTLETT. Mr. Skinner, we will ask you the same indulgence that Mr. Sevier granted, and that is permission to put questions to you in writing, if you so desire, at a later date.

Mr. SKINNER. We will be happy to accommodate you in any way.

Senator BARTLETT. Thank you, sir.

(See questions submitted by Mr. Clark, p. 321.)

Senator BARTLETT. We have a time problem. We always do. Before the committee goes into recess, we should like to hear from Mr. Ross, secretary-treasurer of the Pacific Far East Line. We understand that he desires to depart Washington as soon as possible.

STATEMENT OF LEO C. ROSS, SECRETARY-TREASURER, PACIFIC FAR EAST LINE, INC.

Mr. Ross. Mr. Chairman, I too would like to say that the Pacific Far East Line welcomes this opportunity to address this committee on this most important issue.

Senator BARTLETT. We are glad to have you do so, Mr. Ross.

Mr. Ross. Thank you.

My name is Leo C. Ross, and I am secretary-treasurer of Pacific Far East Line, Inc., with main offices in San Francisco, Calif.

To understand better the experience of Pacific Far East Line in maintaining a service to Guam over the past 14 years, a brief résumé of our overall operations, growth, and development appears to be in order.

Pacific Far East Line, Inc., a Delaware corporation, was formed in July 1946 to engage essentially in the trans-Pacific Ocean freight service. The company began operations with vessels chartered from the U.S. Government and in the first year of operation purchased five C-2 type vessels under terms and conditions set forth in the Ship Sales Act of 1946.

By the end of 1947, the company was operating a total of 32 vessels, 5 owned and 27 under bareboat charter, all engaged in the trans-Pacific service, including a monthly service to Guam. In 1951, the company purchased from the U.S. Government three AP-3 *Victory* type vessels and by the end of that year had in service 49 vessels—8 owned, 27 chartered, and 14 operated on behalf of the National Shipping Authority under a general agency agreement. Our service had

been expended to the Indian Ocean area enroute to the Persian Gulf and, via the Panama Canal, to ports in the Mediterranean, and the service to Guam was increased to two monthly sailings.

Effective January 1, 1953, Pacific Far East Line was awarded an operating-differential subsidy contract on Trade Route 29. The terms of the agreement provided in part for not less than 36 sailings nor more than 40 sailings per annum, employing five C-2 type vessels and three AP-3 type vessels. The company committed itself to replace the three AP-3 vessels with three *Mariner* type vessels and, in addition, agreed to the ultimate replacement of the five C-2 vessels with more modern tonnage satisfactory to the U.S. Government. Trade route 29 embraces service from California to Japan, Korea, Okinawa, Formosa, Philippine Islands, Hong Kong, Indochina, and Thailand.

Continued operation of services to other than Trade Route 29 areas was dependent upon obtaining approval from the Federal Maritime Board, which resulted in reducing our fleet by the end of 1953 to 22 vessels, 2 of which were operated under general agency agreement with the National Shipping Authority. We continued however, to maintain, with the approval of the Federal Maritime Board, a twice-monthly unsubsidized service to Guam.

In 1955, we took delivery of three *Mariner* type vessels contracted for in 1953 in substitution for the *Victory* type vessels and, in addition, purchased a fourth *Mariner* to augment our subsidized service, and the number of subsidized sailings was increased to a minimum of 47 and a maximum of 57 sailings annually.

Pacific Far East Line became the first operator to purchase and place in service the *Mariner* class cargo ship, which basic design has become the accepted standard for most operators engaged in foreign commerce.

In 1956, three additional *Mariners* were purchased from the U.S. Government, thus leaving us with but two C-2 type vessels to be replaced by modern tonnage to complete our replacement obligations under subsidy. The last two *Mariners* were contracted for in 1959 and are presently under construction with anticipated delivery early in 1962. Delivery of these last two vessels will complete our replacement obligations under our subsidy contract. Pacific Far East Line thus became the first company to complete its replacement obligations under the Merchant Marine Act of 1936. During this entire period and to date, in addition to meeting the substantial financial obligations involved with the acquisition of new tonnage, the company continued to maintain and expand as needed its service to Guam to meet not only the commercial requirements but the military as well.

Through the payment of operating differential subsidy funds and construction differential paid to domestic shipyards, we have been able to fulfill our obligations to the U.S. Government in building up a fast modern fleet of cargo vessels for our subsidized service in competition with foreign-flag vessels.

Pacific Far East Line is one of the few American-flag operators with an operating differential subsidy that has every year without exception refunded to the U.S. Government in the form of recapture a part of operating subsidy accrued to the line. The financial return to the company resulting from maintaining continuous service to Guam, without financial assistance however, has been so marginal over the years that it has been impossible to modernize the fleet in

this service. In fact, during the past 3 years, Pacific Far East Line has suffered substantial losses in this trade.

The present tonnage in this service consists of three AP-3 *Victory* type vessels and three C-2 vessels with an average age of 17 years from date of construction, all owned by Pacific Far East Line or its subsidiary company. These vessels must ultimately be replaced and, with continuing losses, it would be impossible to meet the obligations that would be imposed if we were to contract for new tonnage.

So long as the strategic location of Guam remains important to the national interest, as is evidenced by the continued movement of military cargoes to that area and commercial cargoes which in turn supports the military and defense needs of the area, we would desire to continue to serve Guam, providing a fair return on the capital so employed could be realized.

However, since we are a publicly owned company and we have an obligation to our shareholders, we cannot justify the continued absorption of heavy losses by maintaining this service. It has been the policy of the company, in recognition of the economic limitations of Guam, to defer rate increases until all other means of meeting ever-increasing costs had been exhausted. This is evident when one reviews the history of the rate increases in this area during the period January 25, 1951 to December 31, 1959, in relation to increased per diem vessel costs for the like period. During this period, there have been three rate increases aggregating 39 percent. Operating expense of vessels of the type employed in this service had, during this same period, risen from an average of \$1,633 per day to \$2,763 per day, or 66 percent.

In view of the foregoing, justification for the most recent application for a commercial rate increase is, we feel, apparent. Operating results for the year 1961 predicated on income produced by the latest published tariff continues to reflect a loss in this service. One of the major problems in serving this area is that it is a one-way service, that is to say, the outbound tonnage movement, both military and commercial, must be in such volume and move at such a rate as to create revenues sufficient to meet the round voyage costs and overhead applied to this operation. Return cargo from Guam has been limited primarily to military household goods and military retrograde cargo. Commercial cargo has, for the most part, been limited to occasional shipments of scrap, trocus shells, and empty containers.

Schedule 1 to exhibit III gives the comparison of outbound revenue to inbound revenue for the year 1959, which year is representative of our annual experience. Inbound commercial cargo constitutes less than 2 percent of total voyage revenue.

In order to justify the continued service to Guam, this company has in the past attempted to augment the inbound revenue by calls beyond Guam to Japan and the Philippines. There are, however, limitations in cargo liftings from these areas since we must avoid competition with subsidized vessels servicing these same areas.

Although no part of our service to Guam, including calls to foreign ports beyond Guam, permits of subsidy payments, in instances where the revenue derived in foreign areas on Trade Route 29 amounts to 50 percent or more of the total voyage revenue, the net financial results of such voyages must be taken into account for purposes of determining the amount of recapture, if any, that may be due the Gov-

ernment. Recapture is an amount equal to 50 percent of profits realized after statutory return on capital employed.

It is now quite apparent that the volume of available tonnage moving interport from most Far East ports to Guam is not compensatory with the added vessel time in calling at such ports. However, since Guam has in an effort to bolster their own economy and to find markets for their limited production engaged in modest trade with Japan, and since Pacific Far East Line is the only ocean carrier providing service for such movement, we contemplate continuing this service between Guam and Japan for the time being.

A proforma (exhibit I), based on a year's operations utilizing 5 vessels serving west coast to Guam and, in addition Japan, has been prepared to show the anticipated financial results of this service. Whereas our calculations indicate a substantial reduction in losses presently being incurred, the net result of this curtailed service still remains in a loss position. In addition, this revised service by limiting calls beyond Guam-to-Japan leaves us with one surplus vessel for which we must find other employment or place in idle status, adding further to our costs.

We have also made a study of the net effect if our service were further reduced to limit calls to the mid-Pacific islands and turning at Guam. This is submitted as exhibit II and indicates approximately the same financial results as is evidenced by exhibit I.

When this committee has the opportunity to review these exhibits, it will be noted that the overhead allocated to this service is quite substantial. Since this company operates its transpacific service under an operating differential subsidy contract, the basis for allocating overhead between subsidized operations and unsubsidized operations is prescribed by the Maritime Administration. If we can prevail upon the Administration to amend their allocation of overhead, it will help materially in justifying the possible continuance of this service.

If the volume of military and commercial tonnage outbound remains at the level experienced during the years 1959 and 1960—and we have been informally advised that there appears to be no lessening in the military cargo for 1961—there is need for a minimum of 4 vessels of the C-2 and/or *Victory* class in this service, maintaining a frequency of calls at Guam not less than every 12 days.

We are required by the Maritime Administration to submit quarterly operating statements on the results of our unsubsidized operations, and the continuance of this service is subject to the approval of the Federal Maritime Board. Since the losses sustained in this service during the past 2 years exceed \$1 million a year, such losses obviously cannot continue. It is therefore quite apparent that a solution to this problem must be found with reasonable dispatch and, in our opinion, the answer is not to be found by continued upward revision of ocean freight rates to the point where in time it will affect the overall economy of Guam.

The present commercial freight rates applicable to Guam are in excess of the rates to foreign ports in the Far East. The Far East rates are established by the Pacific Westbound Conference which is dominated by foreign-flag lines. Under the two-third voting rule in the conference, even if all American-flag lines voted in a block, they would still be outnumbered by the foreign-flag vote. This situation

permits foreign-flag lines, whose operating costs are less than American, to maintain a rate level which would not necessarily be in all cases compensatory to the American-flag operator.

With respect to the operation of American-flag vessels in the Far East trade, all operators are either presently subsidized or have made application for subsidy contracts pursuant to public hearings conducted by the Federal Maritime Board. It therefore seems only proper that the aid for service to Guam should come from the Government the same as is the case in the Far East instead of coming from the residents of Guam. Freight rates to Guam are based solely on the American-flag operator. Therefore, rates must be compensatory to American-flag operators with their higher operating costs. The net result is that the residents of Guam are, in effect, bearing the burden. This situation certainly appears to be an unreasonable and unrealistic position; nevertheless, if it were not the case, American-flag vessels could not profitably operate to Guam.

By its geographic location and at the same time its apparent strategic importance to the national interests of the United States and the desire on the part of the Navy to maintain the security for defense of this area, the problems confronting Guam are unique. Guam must be served solely by American-flag operators as no foreign lines are permitted to make calls. Vessel operations conducted at Guam are subject to limitations imposed by the Navy.

For example, vessels cannot arrive or depart or make an intraport shift between sunset and sunrise. All harbor floating equipment and services incident thereto, such as tugboats, launch hire, pilotage, floating cranes and barges, are controlled by the Navy, all with the apparent intent to maintain the defense security of the island. Whereas Guam is considered in the domestic trade, it lies over 5,000 miles west of continental United States, the most distant outpost on our defense perimeter containing major defense installations. The nearest land mass beyond Guam is Japan, approximately 1,300 miles northwest and, secondly, the Philippines, approximately 1,500 miles due west. Because of this relative isolated location, it is difficult to integrate service to Guam with any other area affording ample commercial tonnage for sustained operations.

Pacific Far East Line is the only commercial operator maintaining regular service to Guam except for one other commercial operator calling at Guam on an average of 14 times a year. Pacific Far East Line alone maintains service between Guam and Japan.

The foregoing constitutes in brief the service that Pacific Far East Line has endeavored to maintain to this strategically important area, the steps we have taken to improve the economic conditions to permit of the continuance of such a service, and the conclusions reluctantly reached that without some form of financial assistance from the Government the maintaining of service to this area by Pacific Far East Line is seriously questioned.

In support of our position and statements made today, we would like to submit for your study and evaluation the following exhibits and schedules:

Exhibit I: Pro forma of the projected annual operating results utilizing five vessels in the Guam service, including calls between Guam and Japan.

Exhibit II: Pro forma of the projected annual operating results utilizing four vessels in the Guam service, eliminating calls beyond Guam.

Exhibit III: Operating revenue and expense statement—unsubsidized service—domestic leg (Guam) for the year 1959.

Schedule 1 to exhibit III: Vessel operating statement—year 1959 and analysis of terminated voyage revenue and expense.

Exhibit IV: Operating revenue and expense statement—unsubsidized service—domestic leg (Guam)—first 6 months 1960.

Schedule 1 to exhibit IV: Vessel operating statement—first 6 months 1960 and analysis of terminated voyage revenue and expense.

Exhibit V: Analysis of annual tonnage to Guam for the years 1956 through 1959 and first half 1960 based on voyage terminations.

Exhibit VI: Characteristics of vessels employed in the Guam service.

Exhibit VII: Analysis of increased vessel operating cost per day 1957 to 1960.

I would like to add, Mr. Chairman, that we would like the privilege of supplementing our testimony and these exhibits at some future date, depending on other testimony given before this committee.

Senator BARTLETT. That permission is granted, Mr. Ross. Yours has been an excellent statement.

Mr. Ross. Thank you.

Senator BARTLETT. We appreciate your giving it.

Specifically, I should like to inform you that the record is to be kept open for 6 weeks from the date of the last hearing. We would be, I know, especially interested in having any concrete suggestions from you as to what form the financial assistance from the Federal Government might take, because, as you have stated, it must be given if this service is to be maintained. If you fail to offer those specific suggestions, we shall understand, because it is already apparent that this isn't simple at all.

Mr. Ross. No, sir, it isn't.

Senator BARTLETT. In any case, you have aided us by stating the extent and deepening gravity of the situation. I can well imagine that the most attentive auditor of your testimony was Mr. Goding on my right, as President Kennedy has announced his intention of appointing Mr. Goding as High Commissioner to the Trust Territory. He will be living at Guam and will have the keenest interest in the continuation of satisfactory maritime service to that entire area.

Mr. Ross. Very good, sir.

Senator BARTLETT. I should like, in the interest of saving time, Mr. Ross, to ask you if we might put to you questions in writing for your answers in the same form?

Mr. Ross. Certainly, sir. I would be very happy to respond.

Again, my thanks to you and your committee for permitting us these moments.

Senator BARTLETT. We are especially glad to hear from you because we didn't hear enough about Guam previously.

(Exhibits to Mr. Ross's statement follow:)

PACIFIC FAR EAST LINE, INC.

EXHIBIT I.—Guam service—5-vessel fleet

Three sailings a month (every 10 days) as follows:

<i>Itinerary</i>	<i>Average turnaround in days</i>
1. West coast to Guam and return direct to west coast.....	40
2. West coast to Kwajalein, Guam, Japan and return to west coast.....	50
3. West coast to Honolulu, Wake, Guam, Japan, Guam and return to west coast (includes Portland call every 60 days).....	60

NOTE.—Los Angeles call to be made every 20 days (or as required).

Estimated revenue:

	<i>Projected full year</i>
Commercial freight outward.....	\$4, 533, 825
Commercial freight intermediate:	
Scrap.....	108, 000
General.....	611, 931
	719, 931
Commercial freight inward.....	876, 015
Bulk revenue outward:	
Seed.....	162, 000
Bulk asphalt.....	13, 872
Cement.....	288, 000
	463, 872
Household goods vans:	
Outward.....	161, 637
Intermediate.....	9, 897
Inward.....	326, 901
	498, 435
Mail outward:	
Civilian.....	100, 386
Military.....	40, 986
	141, 372
Military revenue outward:	
Space.....	2, 579, 232
Exempt.....	250, 209
	2, 829, 441
Military revenue intermediate.....	121, 014
Military revenue inward.....	477, 618
Passengers:	
Outward.....	19, 200
Intermediate.....	1, 600
Inward.....	16, 000
	36, 801
Other voyage revenue (H/L & Hdlg. \$35,991.54, Wake Hdlg. \$16,092.41).....	156, 252
Total estimated revenue.....	10, 854, 576
Estimated operating expenses:	
Vessel operating expenses.....	5, 285, 796
Agency fees and commissions.....	290, 655
Port charges.....	341, 826
Stevedoring.....	1, 494, 783
Other cargo expense.....	1, 585, 374
other voyage expense.....	90, 000
	9, 088, 434
Total estimated operating expenses.....	9, 088, 434
Direct profit.....	1, 766, 142
Depreciation and interest.....	429, 963
	1, 336, 179
Overhead allocation.....	1, 414, 881
Net loss before taxes.....	(78, 702)

EXHIBIT II.—Guam service—4-vessel fleet

Sailings every 12 days (voyages averaging 48 days) as follows:

Itinerary

1. West coast to Guam and return direct to west coast.
2. West coast to Kwajalein, Guam, and return direct to west coast.
3. West coast to Honolulu, Wake, Guam, and return direct to west coast.

NOTE 1.—Sailing from Portland every 60 days.

NOTE 2.—Sailing from Los Angeles every 24 days.

	<i>Projected full year</i>
Estimated revenue:	
Commercial freight outward.....	\$4,319,178
Commercial freight intermediate.....	13,905
Commercial freight inward.....	109,116
Bulk revenue outward:	
Asphalt.....	\$13,872
Cement.....	273,600
	<hr/> 287,472
Household goods vans:	
Outward.....	149,067
Inward.....	255,975
	<hr/> 405,042
Mail outward:	
Civilian.....	95,367
Military.....	38,937
	<hr/> 134,304
Military revenue outward:	
Space.....	2,424,279
Exempt.....	237,699
	<hr/> 2,661,978
Military revenue intermediate.....	11,937
Military revenue inward.....	353,358
Passengers:	
Outward.....	\$5,250
Inward.....	2,625
	<hr/> 7,875
Other voyage revenue (Hdlg & H/L \$34,139, Wake Hdlg \$15,287.....)	<hr/> 148,278
Total estimated revenue.....	<hr/> <hr/> 8,452,443
Estimated operating expenses:	
Vessel operating expenses.....	4,078,518
Agency fees and commissions.....	184,854
Port charges.....	289,716
Stevedoring.....	1,133,523
Other cargo expense.....	1,270,263
Other voyage expense.....	75,000
Total estimated operating expense.....	<hr/> 7,031,874
Direct profit.....	1,420,569
Depreciation and interest.....	323,355
Total.....	<hr/> 1,097,214
Overhead allocation.....	<hr/> 1,176,252
Net loss before taxes.....	<hr/> <hr/> (79,038)

EXHIBIT III.—Water line operating revenue and expense statement unsubsidized service, domestic leg for the period Jan. 1, 1959, through Dec. 31, 1959

	Total	Commercial cargo	Military cargo
Terminated voyage results:			
Number of terminations.....	24		
Revenue.....	\$7,798,228.41	\$5,015,313.74	\$2,782,914.67
Expense.....	7,521,705.36	5,225,331.05	2,296,374.31
Gross profit or (loss) from vessel operations.....	276,523.05	(210,017.31)	486,540.36
Other shipping operations:			
Income.....	30,013.33	30,013.33	
Expense.....	131,543.50	131,543.50	
	101,530.17	101,530.17	
Gross profit or (loss) from shipping operations before overhead and depreciation.....	174,992.88	(311,547.48)	486,540.36
Overhead:			
Administrative and general expense.....	1,071,626.76	612,970.51	458,656.25
Less: Agency fees, commissions and brokerage.....	136,278.86	77,951.51	58,327.35
	935,347.90	535,019.00	400,328.90
Advertising.....	35,803.62	35,803.62	
Taxes, other than Federal.....	9,124.96	5,219.48	3,905.48
	980,276.48	576,042.10	404,234.38
Gross profit or (loss) from shipping operations before depreciation.....	(805,283.60)	(887,589.58)	82,305.98
Depreciation:			
Amortization, leasehold.....	3,326.04	1,902.49	1,423.55
Floating equipment, vessels.....	138,283.44	70,109.70	68,173.74
Other floating equipment.....	6,913.54	3,954.54	2,959.00
Other shipping property and equipment.....	54,085.25	30,936.76	23,148.49
	202,608.27	106,903.49	95,704.78
Gross profit or (loss) before shipping operations.....	(1,007,891.87)	(994,493.07)	(13,398.80)
Other deductions from income: Doubtful notes and accounts receivable.....	85,184.81	85,184.81	
Net profit or (loss) before mortgage interest and Federal income tax.....	(1,093,076.68)	(1,079,677.88)	(13,398.80)

DOMESTIC OFFSHORE SHIPPING

SCHEDULE I.—Vessel operating statement for the period Jan. 1, 1959, through Dec. 31, 1960, unsubsidized service, domestic leg

	Outbound	Intermediate	Inbound	Total
Freight payable tons of cargo carried.....	212,122	15,564	37,883	265,569
(600) Operating revenue, terminated voyages:				
Commercial cargo.....	\$3,573,240.18	\$268,626.88	\$72,522.48	\$3,914,389.54
Military household goods.....	98,670.14	3,543.00	419,252.17	521,465.31
Military cargo.....	2,076,931.87	170,656.64	502,718.00	2,750,306.51
Bulk cargo.....	295,480.61	11,538.60		307,019.21
Passenger.....	11,725.00	400.00	14,681.25	26,806.25
Commercial and military mail.....	106,090.93		11,069.92	117,160.85
Other voyage revenue.....	140,800.97	18,162.23	2,117.54	161,080.74
Total operating revenue.....	6,302,939.70	472,927.35	1,022,361.36	7,798,228.41
(700) Operating expense, terminated voyages:				
Vessel expense:				
01 Wages.....				1,560,487.00
08 Payroll taxes.....				59,649.39
09 Contributions.....				100,543.38
10 Subsistence, domestic.....				134,472.10
14 Subsistence, foreign.....				6,587.44
15 Stores, supplies, and equipment, domestic.....				163,444.67
24 Stores, supplies, and equipment, foreign.....				5,229.04
25 Maintenance expense.....				70,893.37
35 Fuel oil.....				539,390.09
40 Repairs, domestic.....				185,467.15
49 Repairs, foreign.....				15,998.17
55 Insurance, hull and machinery.....				257,996.28
57 Insurance, P. & I.....				226,169.31
59 Insurance, other.....				5,259.23
60 Charter hire.....				851,225.88
64 Other vessel expense.....				56,709.52
Total vessel expense.....				4,239,522.02
Port expense:				
65 Agency fees and commissions.....				191,868.52
70 Wharfage and dockage.....				32,168.17
79 Port charges.....				190,115.64
Total.....				414,152.33
Cargo expense:				
80 Stevedoring.....				1,309,720.33
89 Other cargo expense.....				1,494,571.27
Total.....				2,804,291.60
Brokerage:				
90 Freight.....				17,799.80
92 Passenger.....				285.94
Total.....				18,085.74
Other voyage expense:				
99 Other voyage expense.....				45,623.67
Total voyage expense.....				3,282,183.34
Total vessel operating expense.....				7,521,705.36
Direct profit from vessel operations.....				276,523.05

EXHIBIT IV.—*Waterline operating revenue and expense statement, unsubsidized service, domestic leg, for the period Jan. 1, 1960, through June 30, 1960*

	Total	Commercial cargo	Military cargo
Terminated voyage results:			
Number of terminations.....	12		
Revenue.....	\$3,904,711.51	\$2,540,991.92	\$1,363,719.59
Expense.....	3,835,059.91	2,710,856.23	1,124,203.68
Gross profit or (loss) from vessel operations.....	60,651.60	(169,864.31)	239,515.91
Other shipping operations:			
Income.....	2,657.13	2,657.13	
Expense.....	62,179.43	62,179.43	
Gross profit or (loss) from shipping operations before overhead and depreciation.....	59,522.30	59,522.30	
Gross profit or (loss) from shipping operations before overhead and depreciation.....	10,129.30	(229,386.61)	239,515.91
Overhead:			
Administrative and general expense.....	486,481.88	285,078.38	201,403.50
Less: Agency fees, commissions and brokerage.....	34,564.81	20,254.98	14,309.83
Advertising.....	451,917.07	264,823.40	187,093.67
Taxes, other than Federal.....	11,973.61	11,973.61	
	4,310.50	2,525.95	1,784.55
Gross profit or (loss) from shipping operations before depreciation.....	468,201.18	279,322.96	188,878.22
Gross profit or (loss) from shipping operations before depreciation.....	(458,071.88)	(508,709.57)	50,637.69
Depreciation:			
Amortization, leasehold.....	1,222.42	716.34	506.08
Floating equipment, vessels.....	90,310.55	51,115.77	39,194.78
Other floating equipment.....	3,890.20	2,279.66	1,610.54
Other shipping property and equipment.....	23,279.51	13,641.79	9,637.72
	118,702.68	67,753.56	50,949.12
Net profit or (loss) before mortgage interest and Federal income tax.....	(576,774.56)	(576,463.13)	(311.43)

SCHEDULE I.—Vessel operating statement for the period Jan. 1, 1960, through June 30, 1960, unsubsidized service, domestic leg

	Outbound	Intermediate	Inbound	Total
Freight payable tons of cargo carried.....	107, 590	5, 618	23, 210	136, 418
(600) Operating revenue, terminated voyages:				
Commercial cargo.....	\$1, 849, 293. 28	\$100, 601. 20	\$68, 494. 81	\$2, 018, 389. 29
Military household goods.....	40, 948. 75	891. 00	188, 587. 45	230, 427. 20
Military cargo.....	943, 791. 72	38, 431. 91	358, 950. 26	1, 341, 173. 89
Bulk cargo.....	173, 675. 50	0	0	173, 675. 50
Passenger.....	3, 850. 00	0	4, 975. 00	8, 825. 00
Commercial and military mail.....	46, 156. 69	0	5, 298. 26	51, 454. 95
Other voyage revenue.....	71, 525. 51	8, 206. 46	1, 033. 71	80, 765. 68
Total operating revenue.....	3, 129, 241. 45	148, 130. 57	627, 339. 49	3, 904, 711. 51
(700) Operating expense, terminated voyages:				
Vessel expense:				
01 Wages.....				888, 455. 09
08 Payroll taxes.....				48, 789. 43
09 Contributions.....				51, 870. 60
10 Subsistence, domestic.....				79, 660. 45
14 Subsistence, foreign.....				2, 291. 13
15 Stores, supplies and equipment, domestic.....				82, 175. 77
24 Maintenance expense, foreign.....				187. 25
25 Maintenance expense.....				34, 586. 42
35 Fuel oil.....				258, 076. 95
40 Repairs, domestic.....				114, 620. 95
49 Repairs, foreign.....				11, 719. 25
55 Insurance, hull and machinery.....				114, 001. 93
57 Insurance, P. & I.....				126, 614. 58
59 Insurance, other.....				3, 130. 31
60 Charter hire.....				298, 788. 25
64 Other vessel expense.....				28, 424. 84
Total vessel expense.....				2, 174, 293. 20
Port expense:				
65 Agency fees and commissions.....				163, 822. 93
70 Wharfage and dockage.....				15, 302. 62
79 Port charges.....				101, 391. 35
				220, 516. 90
Cargo expense:				
80 Stevedoring.....				665, 198. 81
89 Other cargo expense.....				740, 342. 14
				1, 405, 540. 95
Brokerage:				
90 Freight.....				9, 064. 67
93 Passenger.....				183. 75
				9, 248. 42
Other voyage expense:				
99 Other voyage expense.....				25, 460. 44
99 Total voyage expense.....				1, 660, 766. 71
Total vessel operating expense.....				3, 835, 059. 91
Direct profit from vessel operations.....				69, 651. 60

EXHIBIT V.—Unsubsidized service, domestic leg, annual tonnage to Guam (based on voyage terminations)

	Commercial general		Military household goods		Military cargo		Commercial bulk		Commercial and military mail		Total	
	2,000 pounds	Revenue tons	2,000 pounds	Revenue tons	2,000 pounds	Revenue tons	2,000 pounds	Revenue tons	2,000 pounds	Revenue tons	2,000 pounds	Revenue tons
1956.....	57,848	82,290	.....	.....	84,866	132,983	1,590	1,590	770	770	145,074	217,633
1957.....	54,945	76,431	154	140	47,855	85,699	30,325	27,173	705	705	138,084	200,145
1958.....	53,110	74,051	244	244	41,966	85,013	2,794	2,779	838	838	138,693	192,492
1959.....	68,818	96,500	387	387	44,005	83,318	35,794	32,203	888	888	149,853	222,798
1960 (½ year).....	33,521	49,300	154	154	16,581	40,298	22,260	19,968	365	365	73,131	110,085

EXHIBIT VI.—Vessel characteristics—Unsubsidized service

Vessel	Date of construction	Gross tonnage	Deadweight	Bale cubic capacity	Grain cubic capacity	Speed	Reefer capacity	Dry cargo capacity	Liquid capacity
Alaska Bear.....	July 1944.....	7,604	10,702	455,047	526,797	16.0	(1)	455,047	(2)
Canada Bear.....	March 1945.....	7,601	10,753	453,210	523,740	16.0	(1)	453,210	(2)
Guam Bear.....	June 1944.....	8,197	10,937	524,406	561,853	14.8	(1)	524,406	(2)
Hawaii Bear.....	February 1945.....	7,628	10,658	455,047	526,797	17.0	(1)	455,047	(2)
India Bear.....	September 1944.....	8,197	11,149	524,585	562,052	15.0	(1)	524,585	(2)
Pacific Bear.....	February 1944.....	8,157	11,268	530,529	570,992	14.5	(1)	530,529	(2)

1 No reefer capacity.

2 No liquid capacity.

EXHIBIT VII.—Increased costs in vessel operations

COMPARISON OF VESSEL OPERATING COSTS

	1957 per diem	1960 per diem	Percent increase or (decrease)	Percent increase or (decrease) to total increase
Wages:				
Straight time.....	\$743	\$877	18.03	38.95
Overtime.....	277	335	20.94	16.86
Fringe.....	158	263	66.46	30.53
Subsistence.....	112	114	1.79	.58
Stores and supplies.....	84	124	47.62	11.63
Repairs and maintenance.....	161	223	38.51	18.02
Fuel oil (per sea-day) ¹	856	707	(17.41)	(43.31)
Insurance.....	265	314	18.49	14.24
Vessel expense.....	26	69	265.38	12.50
Subtotal.....	2,682	3,026	12.83	100.00
Port expense.....	289	414	43.25	.....
Total.....	2,971	3,440	15.79	.....
Per diem per port-day.....	143	119	(16.78)	.....

¹ Average cost per port-day not included.

COMPARISON OF LONGSHORE WAGE-HOUR RATES, PACIFIC WEST COAST PORTS

	Subsequent to June 15, 1957			Subsequent to June 13, 1960			Percent increase
	Straight time rates	Fringe	Total	Straight time rates	Fringe	Total	
Longshoremen.....	\$2.53	\$0.49	\$3.02	\$2.82	\$0.62½	\$3.44½	14.07
Winch-lift truck operator.....	2.68	.49	3.17	2.97	.62½	3.59½	13.41
Gang boss.....	2.73	.49	3.22	3.02	.62½	3.64½	13.20
Walking boss.....	3.29	.49	3.78	3.86	.56	4.42	16.93
Clerk.....	2.68	.49	3.17	3.03½	.62½	3.66	15.46
Clerk supervisor.....	2.95	.49	3.44	3.44	.62½	3.96½	15.26
Supercargo.....	3.21½	.49	3.70½	3.72	.62½	4.34½	17.27
Carpenter.....	2.68	.16½	2.84½	3.00	.28	3.28	15.29
Carpenter foremen.....	3.18	.18½	3.36½	3.50	.29	3.79	12.63

Senator BARTLETT. It is the conclusion of the committee to hear one more witness, Mr. Lykes.

Mr. MARK SCHLEFER (counsel for Mr. Lykes). He was under the impression that he would be heard this afternoon, and will not be back until then.

Senator BARTLETT. It was stated that Mr. Ross would be the last witness. However, we cannot continue this afternoon because of the situation on the floor of the Senate.

At this time the committee will stand in recess until 10 o'clock tomorrow.

(Whereupon, at 12:50 p.m., the subcommittee was adjourned, to reconvene at 10 a.m., Tuesday, March 14, 1961.)

DOMESTIC OFFSHORE SHIPPING

TUESDAY, MARCH 14, 1961

U.S. SENATE,
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
SUBCOMMITTEE ON MERCHANT MARINE AND FISHERIES,
Washington, D.C.

The subcommittee was called to order, pursuant to adjournment, at 10:15 a.m. in room 5110, New Senate Office Building, Hon. Clair Engle, presiding.

Senator ENGLE. The Subcommittee on Merchant Marine and Fisheries will be in order. We will proceed this morning until a quarter past 11, or approximately that time, when the chairman of the full committee will arrive for the purpose of considering some nominations.

Our hearings continue this morning on the domestic offshore shipping. Our first witness is Vice Adm. Frank M. McCarthy, president of the Bull Lines.

Admiral, we will be very glad to hear you at this time.

You may go right ahead. Do you have a prepared statement?

STATEMENT OF ADM. F. M. McCARTHY, PRESIDENT OF A. H. BULL STEAMSHIP CO.

Mr. McCARTHY. I have, Mr. Chairman.

I am F. M. McCarthy, president of the A. H. Bull Steamship Co., the principal carrier in the Puerto Rico trade. Bull's association with transportation to and from Puerto Rico has been over a 60-year period. It has likewise been our chief interest. During that period we have been part of the transition from sail to steam. We acted as banker, warehouseman, developer, and promoter of trade between the mainland and Puerto Rico. We have aided in the development of the island in the past, and have every intention of continuing to do so in the future.

Serving Puerto Rico as we have for more than a half century, let us assure you that there is no intention of harming the economy of Puerto Rico. Such a policy would be extremely harmful to us. Our basic general cargo services are exclusively Puerto Rican. We have no other trade—therefore the best interests of our company dictate a continued policy of cooperation and development. Significantly enough, while this has always been our policy for better than a half century, the first time that any freight rate adjustment needed to meet changing conditions, was challenged, was in docket 807.

I might correct myself there, Mr. Chairman. Due to an inadvertent oversight, there was a previous freight rate case challenged, docket 500, which was before World War II.

The steamship industry contributes more than \$9 million annually to the island's economy in the form of direct wages to terminal employees on the island. This does not include administrative and office personnel, nor does it include expenditures in Puerto Rico for any other services.

If I may digress a moment, sir, from my prepared statement, I would like to point out that this as well does not include wages paid to crews on ships. On the Bull Line, natives of Puerto Rico comprise about 70 percent of our crews. We operate six C-2 ships in the trade in Puerto Rico, and during 1960 the wages paid to crews amounted to \$2,098,462. This also was a benefit to the economy of Puerto Rico, and I am quite certain that to some of the same degree, other lines serving Puerto Rico likewise have a considerable number of native Puerto Ricans in their crew.

Wages in the industry are among the highest on the island. I have prepared for the committee in this respect a tabulation of the hourly wage pattern for a number of years. They will be found in the two statements attached to the written statement.

The same data was prepared for stateside labor. I might add that when the dock labor in Puerto Rico handles certain unitized freight, the wages are automatically increased to the same scale paid in North Atlantic ports.

Our losses in the trade have reached staggering proportions. The problem confronting all of the lines is how they can continue to absorb such losses.

It has been contended here that the solution to this problem is operating and construction subsidies. We are not a subsidized carrier in any trade; however, we are not taking a position one way or the other with respect to the subsidy proposals advanced by the Commonwealth. If the Congress should, in its judgment, see fit to change existing laws with respect to subsidies, we can readily adapt ourselves to the changes, but we are not at all satisfied that subsidies will produce what everyone seems to expect.

Traditionally, and within the framework of the Merchant Marine Act, 1936, subsidies are designed to establish a parity with low-cost foreign-flag competition. It is important, therefore, to examine the possible effect of such competition in the protected trades, as well as the effect of subsidy on the present carriers in these trades.

There is no doubt that the cost of construction and operation of American ships is more expensive than foreign-flag vessels, but that in itself is no guarantee that foreign-flag lines will provide service at less than prevailing rates, nor will they devote their resources. In times of war or better business elsewhere, they are likely to serve the most profitable routes. The existing coastwise law, in addition to accomplishing its intended purpose, also has had the effect of promoting intense competition among the American-flag lines who operate thereunder.

Much of the Caribbean area, exclusive of Puerto Rico, is served by foreign-flag lines. We have prepared an exhibit for this hearing of the rates on some 60 or 70 commodities, which represent a generous cross section of traffic to the entire area.

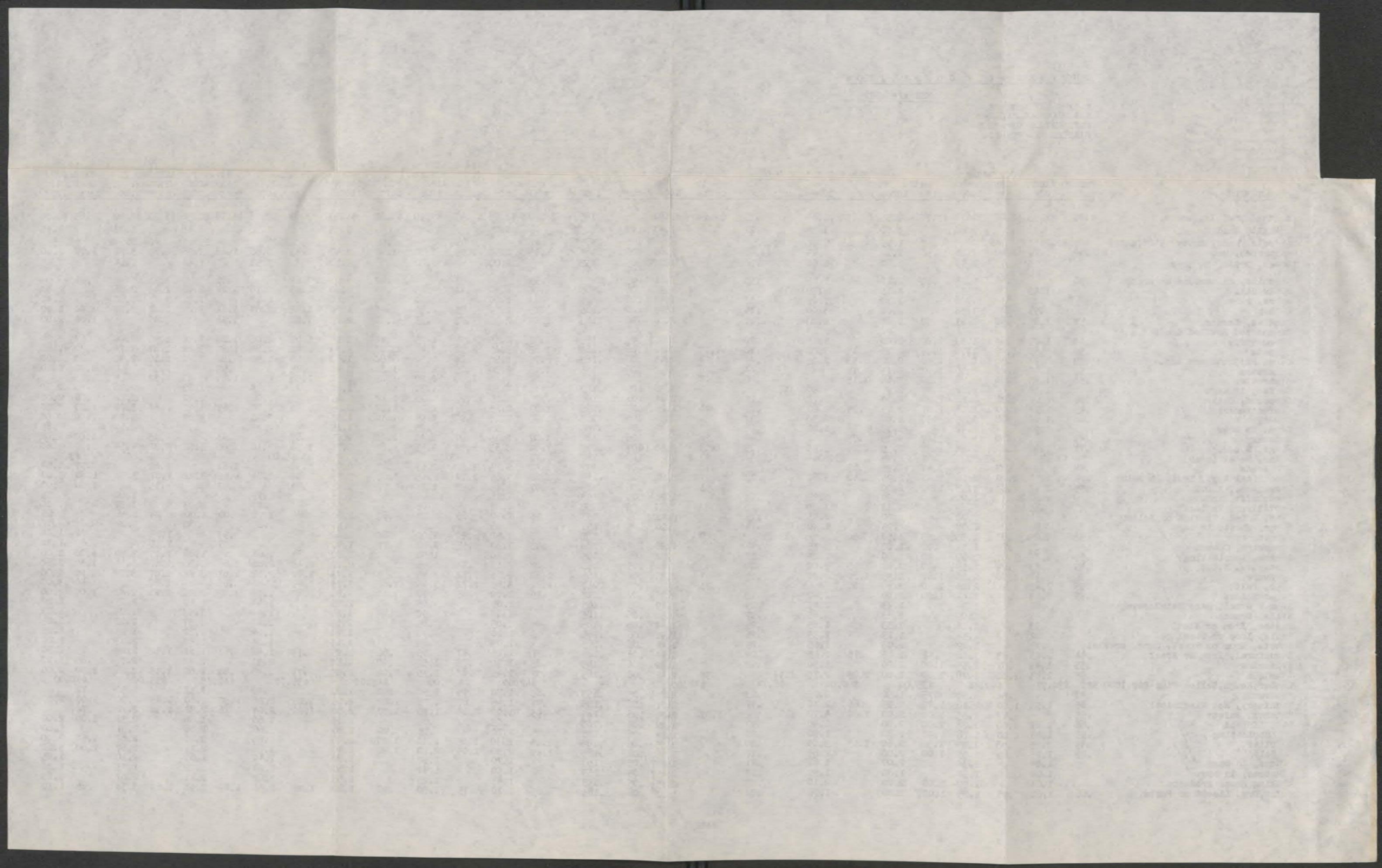
(Exhibits follow:)

OUTWARD RATE COMPARISON

FOR: TARIFF AUTHORITIES
 ADDITIONAL CHARGES
 EXPLANATION OF ABERRATION AND FORMULA

SEE APPENDIX:
 A
 B
 C

COMMODITIES	1		2		3		4		5		6		7		8		9		10		11		12				
	PUERTO RICO cuft 100#	DOMINICAN REPUBLIC cuft 100#	HAITI cuft 100#	HAVANA, CUBA R. H. & D. cuft 100#	SANTIAGO, CUBA R. & H. cuft 100#	ARUBA CURACOA cuft 100#	LA GUAIRA PTO. CABELLO MARACAIBO cuft 100#	PUERTO SUCRE cuft 100#	TRINIDAD B. W. I. cuft 100#	B. W. I. BARBADOS cuft 100#	LEeward IS. WINDWARD IS. cuft 100#	JAMAICA B. W. I. cuft 100#															
Agricultural Implements	\$.65	\$1.53	\$1.00	\$1.78	\$.77	\$1.55	\$.65	\$2.65	.35	\$.64	\$3.01	.06	.185	\$.77	\$1.55	\$.45	\$.90	\$.82	\$1.65	\$1.03	\$2.06	\$1.18	\$2.36	\$1.31	\$2.62	\$.85	\$1.70
Asphalt, Road		.78		.80		1.00		1.35	.22		1.47	.06	.185		1.05		.85		1.15		1.36		1.48		1.82		1.15
Barrels, Wood, Empty 13'6" (EACH)	\$2.04		\$3.30		.57	1.15	\$3.30		\$.62	.32		.06	.185	.47		\$3.50		.52		\$3.00		\$4.25		\$4.80		\$3.25	
Batteries, Wet	.69	1.70	1.20	2.16	.56	1.12	2.45		.41		2.66	.06	.185	1.15	2.30	1.05	2.10	.52	2.40	1.43	2.86	1.68	3.36	1.87	3.74	1.00	2.00
Beans, Dried, in bags		.95		1.40		1.80		1.60	.16		1.207	.05	.153		1.00		.80		1.10		1.31		1.42		1.64		1.45
Biscuits, in cartons or crates	.36		.66	1.17	.60	1.20		3.75	.33		3.81	.05	.153	.55		.47		.62		.62		.66		.91		.55	
BOARD WALL		1.25		1.78		2.15		1.75	.11		1.93	.06	.185	.75	1.50	.42	.85	.80	1.60	1.08	2.16	1.24	2.48	1.43	2.86		2.40
Brick, Fire		.80		1.08		1.50		1.25	.23		1.43	.06	.185		1.00		.80		1.10		1.24		1.32		1.82		1.40
Burlap		.94	.87	1.55		2.00		3.00	.19		1.59	.06	.185	.85	1.70	.75	1.50	.90	1.80	1.42	2.84	1.61	3.22	1.87	3.74	1.00	2.00
Candles, Common	.52	1.29	.68	1.21	.90	1.80		2.20	.21		2.26	.06	.185	1.07	2.15	.97	1.95	1.12	2.25	1.08	2.84	1.61	3.22	1.87	3.74	1.00	2.00
Canned and Bottled Goods (Foodstuffs)	.49	1.25	.89	1.59	1.00(3)	2.00		1.85	.20		1.807	.05	.153	1.07	2.15	.97	1.95	1.12	2.25	1.03	2.06	1.26	2.52	1.50	3.00	.67	1.34
Carpets	.59	1.55	1.00	1.78	1.07	2.15	1.15	3.00	.18	1.07	2.71	.06	.185	1.82	3.65	1.72	3.45	1.87	3.75	1.42	2.84	1.61	3.22	1.87	3.74	1.30	2.60
Cars, Railroad and Acc.	.39	.94	.76	1.35	1.00	2.00	.53	2.05	.29		2.06	.06	.185	.75	1.50	.65	1.30	.80	1.60	.78	1.56	.86	1.72	1.16	2.32	.80	1.60
Chinaware	.55	1.43	1.20	2.16	1.07	2.15	.75		.44		1.76	.06	.185	1.15	2.30	1.05	2.10	1.20	2.40		.83		.93		1.15	1.30	2.60
Cigarettes	.58	1.43	1.00	1.78	1.30	2.60	1.15		.26	1.07		.06	.185	.62		1.10	2.20	1.25	2.50	1.58	1.86		2.32		2.32	1.15	
Coffee, in bags		1.14		1.78		2.95		3.50	.13		3.36	.05	.153		1.50		1.30		1.60		1.49		1.63		2.18		2.60
Compound, Boiler	.66	1.61	1.20	2.16	1.00	2.00		2.70	.17		2.67	.06	.185	1.07	2.15	.97	1.95	1.12	2.25		2.06		2.42		3.12	1.00	2.00
Confectionery	.45	1.14	1.00	1.78	1.07	2.15	.95	2.20	.17	.94	2.26	.05	.153	1.07	2.15	.97	1.95	1.12	2.25	1.42	2.84	1.61	3.22	1.87	3.74	1.00	2.00
Condage	.66	1.61	.87	1.55	.90	1.80		2.50	.17		2.54	.06	.185	1.07	2.15	.97	1.95	1.12	2.25		3.91		4.67		5.20	1.00	2.00
Corn, in bags		.90		1.41		1.13		1.40	.18		1.42	.05	.153		1.15		.95		1.25		.75		.90		1.60		.85
Crockery	.49		1.00	1.78	1.07	2.15	.75		.44			.06	.185	1.07	2.15	.97	1.95	1.12	2.25	.83		.93		1.15		1.00	2.00
Drugs, N.O.S.	.77	1.92	1.20	2.16	1.47	2.95	1.20	3.45	.13	1.21	3.50	.07	.217	1.82	3.65	1.72	3.45	1.87	3.75	1.58	3.16	1.86	3.72	2.32	4.64	1.80	3.60
Drums, Metal (each)		\$1.43		\$3.30		.57	1.15	\$3.30	\$.62		\$3.21	.06	.185	.47		\$3.50		.52		\$3.00		\$4.25		\$4.80		\$3.25	
Dry Goods	.54		.87	1.55	1.47	2.95	.65		.19		.78	.07	.217	1.42	2.85	1.32	2.65	1.47	2.95	1.38	2.84	1.61	3.22	1.81	3.74	.97	1.94
Electrical App., Equip. & Matls.	.69	1.70	1.20	2.16	1.47	2.95	1.40	3.60	.22	1.27	3.21	.06	.185	1.82	3.65	1.72	3.45	1.87	3.75	1.42	2.84	1.61	3.22	1.87	3.74	1.80	3.60
Enamelware, N.O.S.	.55	1.43	.87	1.55	1.00	2.00	.47		.51			.06	.185	.67	1.15	.57	1.35	.72	1.45	.83		.93		1.15		1.00	2.00
Feedstuffs, in bags		.80		1.00*		1.50		1.25	.17		1.26	.05	.153		1.15		.95		1.25		.75		.90		1.60		.75
Fertilizer, in bags		.65		.84		1.15		1.30	.15		1.33	.05	.153		.85		.65		.95		.74		.95		1.37		1.10
Fish, Dried, Pickled or Salted		.84		1.02		1.00		2.45	.15		2.48	.05	.153	.75	1.50	.65	1.30	.80	1.60	.89	1.78	1.00	2.00	1.24	2.48	1.65	
Flour, Wheat, in bags		.85		1.08		.95		1.30	.14		.902	.05	.153		1.05		.85		1.15		.85		.87		1.02		.87
Furniture	.53	1.29	.87	1.55	.75	1.50	.50		.13	.60		.06	.185	.75	1.50	.50	1.00	.80	1.60	.83		.93		1.15		.72	1.44
Glassware, Common	.49	1.25	.79	1.41	.90	1.80		1.75	.44		1.36	.062	.186	.65	1.30	.55	1.10	.70	1.40	.83		.93		1.15		.65	1.30
Grease, Lubricating	.55	1.43	.87	1.55	.90	1.80		1.25	.17		1.32	.06	.185		1.70		1.50		1.80	.83	1.66	.93	1.86	1.15	2.30	1.00	2.00
Groceries, N.O.S.	.49	1.25	.89	1.59	1.00	2.00	1.15	3.00	.20		1.80	.05	.153	1.07	2.15	.97	1.95	1.12	2.25	1.43	2.86	1.68	3.36	1.87	3.74	1.30	2.60
Hardware	.59	1.48	1.20	2.16	1.47	2.95	1.80	4.70	.17	1.07	2.71	.06	.185	1.82	3.65	1.72	3.45	1.87	3.75	1.42	2.84	1.61	3.22	1.87	3.74	1.00	2.00
Hats, Felt	.55	1.43	1.20	2.16	1.30	2.60	.60		.16	.71		.07	.217	1.82	3.65	1.72	3.45	1.87	3.75	1.43	2.84	1.61	3.22	1.87	3.74	1.50	3.00
Insecticides	.55	1.43	.79	1.41	1.00	2.00		2.40	.13		2.36	.07	.217	.55	1.10	.45	.90	.60	1.20	.87	1.74	1.03	2.06	1.21	2.42	1.00	2.00
Iron & Steel, Bars Reinforcing		.82		1.34		1.33		1.45	.29		1.19	.06	.185		1.05		.85		1.15		1.44		1.57		2.03		1.20
Nails, Common		.93		1.09		1.33		1.65	.17		1.52	.06	.185		1.10		.90		1.20		1.44		1.57		2.03		1.15
Plates, Iron or Steel		.93		1.36		1.33		1.65	.29		1.44	.06	.185		1.05		.85		1.15		1.44		1.57		2.03		1.25
Rails, Iron or Steel		.82		1.34		1.13		1.35	.26		1.51	.06	.185		1.10		.90		1.20		1.24		1.32		1.95		1.25
Sheets, Iron or Steel, Corr. or Plain		.93		1.09		1.08		1.65	.29		1.44	.06	.185		1.05		.85		1.15		1.24		1.32		1.95		1.20
Structural, Iron or Steel	.44	1.03	.83	1.46	.72	1.45	.75	1.45	.29		1.49	.06	.185	.57	1.15	.47	.95	.62	1.25	.74	1.48	.81	1.62	1.12	2.24	.65	1.30
Kalsomine	.55	1.43	.87	1.55	1.00	2.00		1.90	.22		1.82	.06	.185	.85	1.70	.75	1.50	.90	1.80		2.11		2.42		2.76	.85	1.70
Linoleum	.55	1.43	1.00	1.78	1.00	2.00	1.05	2.75	.11	.97	2.46	.06	.185	.97	1.95	.87	1.75	1.02	2.05	.74	1.48	.81	1.62	1.13	2.26	1.00	2.00
Lumber, Rough, Yellow Pine-Paw 1000 BFT	\$30.77		\$40.48		\$35.00		\$50.00		\$6.74		\$44.00		\$6.25		\$42.00		\$35.00		\$47.00		\$35.00		\$41.75		\$55.00		\$40.00
Macaroni	.48		.54	.98	.75	1.50		2.95	.23		2.87	.05	.153	.85	1.70	.75	1.50	.90	1.80		3.49		4.13		4.50	.72	
Machinery, Not Electrical	.65	1.53	1.20	2.16	1.47	2.95	.66	2.70	.47		2.61	.06	.185	.97	1.95	.87	1.75	1.02	2.05	1.13	2.26	1.30	2.60	1.45	2.90	1.00	2.00
Matches, Safety	.55																										



OUTWARD RATE COMPARISON

FOR:	SEE APPENDIX:
TARIFF AUTHORITIES	A
ADDITIONAL CHARGES	B
EXPLANATION OF ABBREVIATION AND FORMULA	C

COMMODITIES	1 PUERTO RICO		2 DOMINICAN REPUBLIC		3 HAITI		4 HAVANA, CUBA		5 SANTIAGO, CUBA		6 ARUBA		7 LA GUAIRA		8 PUERTO SUCRE		9 TRINIDAD		10 B. W. I.		11 LEEWARD IS.		12 JAMAICA																													
	cuft	100#	cuft	100#	cuft	100#	cuft	100#	cuft	100#	cuft	100#	cuft	100#	cuft	100#	cuft	100#	cuft	100#	cuft	100#	cuft	100#																												
Paper: Bags		\$.94		\$1.90		\$.70		\$1.40		\$1.45		\$.26		\$1.17		\$.06		\$.185		\$.65		\$1.30		\$.55		\$1.10		\$.70		\$1.40		\$1.41		\$2.17		\$2.67		\$.55		\$1.65												
Building		1.03		\$.87		1.55		.90		1.80		2.00		.17		1.17		.06		.185		.75		1.50		.65		1.30		.80		1.60		2.86		3.36		3.75														
Newsprint, in Rolls		.78		1.90		1.90		1.50		1.20		.22		1.32		.06		.185		1.00		.80		1.10		.66		1.66		1.86		1.86		2.31		2.31		1.55														
Printing		.94		1.90		.90		1.80		1.45		.22		1.34		.06		.185		1.65		1.25		1.75		2.26		2.61		2.61		3.27		3.27		1.55																
Wrapping		.84		1.90		.57		1.15		1.70		.22		1.43		.06		.185		1.40		1.20		1.50		1.66		1.82		1.82		4.55		4.55		1.20																
Potash, Chloride of		\$.77		1.92		1.20		2.16		1.00		2.00		\$1.20		3.45		.13		1.23		.05		.153		1.15		2.30		1.05		2.10		1.20		2.40		\$1.42		2.84		\$1.61		3.22		\$1.87		3.74		1.00		2.00
Muriate of, in bags		.65		1.00		1.47		2.95		1.30		.15		1.23		.05		.153		.85		.65		.95		1.10		1.42		2.84		1.61		3.22		1.87		3.74		1.10												
Sulphate of, in bags		.65		1.00		1.78		1.47		2.95		1.30		.15		1.23		.05		.153		1.15		2.30		1.05		2.10		1.20		2.40		1.42		2.84		1.61		3.22		1.87		3.74		1.10						
Sulphate of Mag., in bags		.65		1.00		1.78		1.47		2.95		1.30		.15		1.23		.05		.153		1.15		2.30		1.05		2.10		1.20		2.40		1.42		2.84		1.61		3.22		1.87		3.74		2.50		5.00				
Refrigerators, Mesh.		.55		1.43		1.00		1.78		1.07		2.15		3.80		.52		3.96		.62		.186		.47		.37		.52		.79		1.58		.91		1.82		1.63		3.26		.45		.90								
Rice, in bags		.95		1.03		.89		1.59		1.50		1.25		1.04		.05		.153		1.30		1.10		1.40		1.06		1.11		1.11		1.11		1.11		1.11		1.11		1.11		.95										
Salt, in bags		.55		1.20		2.16		1.07		2.15		1.10		\$.13		1.16		.07		.217		1.07		2.15		.97		1.95		1.12		2.75		1.43		1.86		1.68		1.87		1.30		2.60								
Shoes, Leather		1.25		2.04		2.00		2.60		1.50		.20		1.60		.06		.185		.55		1.10		.45		.90		.60		1.20		1.86		2.11		2.67		2.67		1.70												
Shoeks, Barrel or Box		1.03		1.78		1.00		2.00		.60		2.05		.13		.76		2.33		.06		.185		.97		1.95		.87		1.75		1.12		2.25		1.66		1.86		2.55		1.00		2.00								
Soap, ships and flakes		.80		1.29		1.15		2.05		.17		2.07		.06		.185		1.07		2.15		.97		1.95		1.12		2.25		1.19		1.26		1.73		1.73		1.20														
Soap, laundry		.67		1.08		1.12		1.85		.17		1.29		.06		.185		1.05		1.05		.75		1.15		1.31		1.42		1.42		1.42		1.42		1.78		1.78		.95												
Soda, Ash		1.03		1.20		.75		1.50		1.25		.14		1.27		.07		.217		1.50		1.30		1.60		2.16		2.48		2.91		2.91		2.91		1.65																
Soda, Silicate of		1.36		1.00		1.78		1.00		2.00		1.80		.22		1.87		.06		.185		1.07		2.15		.97		1.95		1.12		2.25		.64		1.28		.73		1.46		.95		1.90		.77		2.54				
Tile, Floor and Wall		3.09		6.08		1.00		2.00		2.65		.90		2.51		.45		5.20		5.00		5.00		5.30		5.04		5.04		5.04		5.62		9.10		9.10		5.50														
Tires and Tubes, Auto		.32		.42		.55		1.10		.44		\$19.27 EACH		.39		\$19.27 EACH		.68		1.36		.57		1.15		.73		1.46		.54		1.08		.69		1.38		.92		1.84		.55		1.10								
Vehicles, Auto		.38		.52		.55		1.10		.44		\$25.69 EACH		.39		\$19.27 EACH		.68		1.36		.57		1.15		.73		1.46		.54		1.08		.69		1.38		.92		1.84		.55		1.10								
Trucks																																																				
Passenger																																																				
Waste, Cotton, Nylon, Rayon, Wool		1.42		2.00		.65		1.30		2.00		.22		1.14		.06		.185		.60		.50		.65		2.14		3.70		3.90		3.90		3.90		3.90		2.00														
Wire, Brass and Copper		.69		1.70		1.20		2.16		1.30		2.60		2.30		.22		2.17		.06		.185		1.15		2.30		1.05		2.10		1.20		2.40		1.30		2.60		1.55		3.10		1.75		3.50		1.50		3.00		

- * Temporary Rate of 75¢ per 100 lbs. will expire April 2, 1961
- † Temporary Rate of 45¢ per cu. ft. or 88¢ per 100 lbs. will expire March 31, 1961
- ‡ Temporary Rate of 75¢ per cu. ft. or \$1.50 per 100 lbs. will expire April 2, 1961

APPENDIX A

APPENDIX B

APPENDIX C

OUTWARD RATE COMPARISON

TARIFF AUTHORITY

1. A.N. Bull Steamship Co., Outward Freight Tariff No.1 FMB - F No.1
2. United States Atlantic & Gulf - Santo Domingo Conference Outward Freight Tariff No. 16
3. United States Atlantic & Gulf - Haiti Conference Southbound Tariff No. 7
4. Havana Steamship Conference, Southbound Freight Tariff No.H-14
5. Santiago De Cuba Conference, Southbound Freight Tariff No. S-11
- 6, 7 & 8. United States Atlantic & Gulf - Venezuela & Netherlands Antilles Conference, Freight Tariff No. Ven.- 7
- 9,10 & 11. Leeward & Windward Islands & Guianas Conference, Southbound Freight Tariff No. 8
12. U.S. Atlantic & Gulf Ports - Jamaica (B.W.I.) Steamship Conference, Southbound Freight Tariff No. J-6

OUTWARD RATE COMPARISON

ADDITIONAL CHARGES

No additional charges, such as landing, wharfage, arrimo (handling) lighterage, or other port charges, even though they are provided for in the Rules and Regulations of the Tariffs, are reflected in Rate Comparison, except for Havana and Santiago, Cuba Reception and Handling Charges.

- R.H. & D.
- R. & H.
- Cuft.
- 100#
- B F T
- N.O.S.

OUTWARD RATE COMPARISON

EXPLANATION OF ABBREVIATIONS

- Reception, Handling and Delivery (Havana, Cuba)
- Reception and Handling (Santiago, Cuba)
- Cubic Foot
- One Hundred Pounds
- Board Feet
- Not Otherwise Specified

FORMULA

- Commodities: Representative Selection of Cargoes Moving to all Areas Analyzed
- Rates: Contract Rates were used in Areas observing the Contract, Non-Contract (Tariff Rate) System
- Lowest Rate was used in categories where escalated rate structure based on measurement, value or any other restricted factor was used
- Conversion: When converting rates based on a weight or measurement ton basis (2000 lbs./40 cuft), to a cubic foot or 100 pounds, all fractions were dropped

To go off my statement, Mr. Chairman, for a moment, because of the limited time involved prior to these hearings I have not been able to have this statement reproduced. However, here is the original and one copy. Should the committee desire additional copies, we will be glad to have them prepared for you.

Senator ENGLE. This material, since it is not susceptible of being placed in the record, will be made a part of the file in this matter, but not a part of the record, and that is the San Juan Star of Thursday, March 9, 1961, and the other items.

Mr. McCARTHY. Thank you, sir.

An examination of this will reveal that despite the fact that the area is serviced by foreign-flag or U.S. subsidized carriers, Puerto Rico enjoys a competitive or a lower level of rates, except to Venezuela where a major rate disturbance has developed. If those rates are any criteria of foreign-flag services or subsidized services, obviously they would not be beneficial to Puerto Rico.

At this point, Mr. Chairman, I would also like to make some comment on the effect of the rates. For example, if there was any freight disturbance or attempt to disturb the economy of Puerto Rico, probably the first place that it would affect would be in the matter of foodstuffs and the general commodities that are consumed by the people. I have only one copy of it here, which I will give to you, of a series of advertisements in the Puerto Rican press, specifically the San Juan Star, dated March 9, 1961, which is the closest one to these hearings that I could obtain.

I would like to call attention to the fact that in this advertisement on foodstuffs here is smoked ham, 45 cents, and there are some variations of this, half a shank, butt half, or the center steak; top quality fresh pork shoulders, 39 cents; all up and down the line; picnic hams, 37 cents. There are likewise some sales advertised of consumer goods in the nature of dresses, bath towels, women's wear, et cetera.

It would seem to us that this would belie the contention that the lines serving Puerto Rico are attempting—perhaps this is not the word—to strangulate the Puerto Rican economy.

Now, sir, if you would have a look at the exhibit of freight rates to the entire Caribbean, and for example look at groceries in the foodstuffs area, which is a rather wide commodity description embracing a great many items, the rate to Puerto Rico is either 49 cents a cubic foot or \$1.25 a hundred, depending upon which is the greater. To the Dominican Republic the rate on the same commodity is 89 cents a cubic foot or \$1.59 a hundred. And if you go clean across to the 12 ports of the Caribbean which we have selected, you will find that Puerto Rico enjoys a lower rate.

May I also call attention to the rate on canned and bottled goods, foodstuffs, which embraces the next largest group of commodities under other than groceries, not otherwise specified.

The rate is 49 cents a cubic foot or \$1.25 a hundred pounds to Puerto Rico; the Dominican Republic is 89 cents. And if we follow that clear across to the 12 ports we will see somewhat of a similar comparison.

Few, if any, of these areas enjoy the type of frequency of service enjoyed by Puerto Rico. The trade from the North Atlantic demands frequent sailings. Bull at present maintains a weekly sailing from Philadelphia and Baltimore and a twice weekly service from

New York. At the present time on all lines there are two weekly sailings from Baltimore, one weekly sailing from Philadelphia, and five weekly sailings and one bimonthly sailing from New York. I doubt whether there is any other area that enjoys such service.

Not only would foreign ships fail to meet the real problem, but subsidy of the present carriers without repeal of the coastwise laws raises some problems.

First, there is the problem of computing operating subsidy in the absence of foreign-flag competition. If that question were satisfactorily resolved, then some analysis of the distribution of costs would be essential to any evaluation of the effect of a subsidy. For example, our cargo-handling costs—not subject to operating subsidy and identical whether or not foreign ships are used—absorb from 62 to 65 percent of our revenue dollar. Overhead, which also would not be affected by subsidy or foreign operation, consumes about 10 percent of the revenue dollar. There are other substantial items, such as fuel costs, port expense, et cetera, which are the same whether under subsidy or foreign-flag operation.

Again, sir, if I may depart from my prepared statement, I would like to point out that, while it would appear that the cost of handling cargo in the Puerto Rican trade is high, the fact of the matter is that it is high and there are reasons for it over and above what a steamship line is normally called upon to perform. For example, the Puerto Rican trade is not individually a volume trade. What I mean by that is that the majority of consignees in the Puerto Rican trade are not large volume receivers. The large volume receiver is in the minority.

It is not unusual for our line to have 5,000 bills of lading per week on shipments moving to Puerto Rico. A large percentage of them are minimum bills of lading. In other words, one or two packages where the cube or the weight of those packages does not come up to the minimum and a minimum is assessed.

On the larger volume consignees, who are admittedly in the minority, they will bring into Puerto Rico, for example, 10,000 sacks of feedstuffs, animal feedstuffs. There may perhaps be 10 different types of feed in that bill of lading. We are required to first make an assortment of each and every type of feed that is in there. Then it is the custom in the trade for that receiver to advertise that the cost of feed is 35 cents or 50 cents a bag less if you, as a consumer, will go to the dock and pick it up. His salesman sell this material and they issue delivery orders on us to their individual consignees, so that people come down—consignees come down, the buyer in this case, and he will have a delivery order for 2 sacks of broiler mash, or any of the other number of different types that are in there. We have to act as a warehouseman; we have to keep an accounting of that, and then, after that shipment has been fully delivered or "liquidated," as they term it, we are obliged to render him an accounting of just exactly what merchandise we delivered and against what delivery orders the delivery was made.

Obviously in the handling of cargo in that fashion you will run up against a tremendous amount of slackage because perhaps you may have made 50 or a hundred deliveries out of that total shipment. This is likewise true and just as prevalent with packinghouse products.

Importers will bring in four, five, or six thousand cases of lard. The lard comes packed in tin cans, two to a case, sometimes just a can. We have to deliver those in the same fashion. So that those are just a few of the things which make the Puerto Rican trade expensive insofar as handling costs are concerned.

Now, sir, if I may go back to my prepared statement.

With respect to insurance, crew wages, vessel construction costs, reflected in depreciation, and other subsidizable cost factors, any subsidy that has the effect of absorbing part of those costs obviously will be beneficial.

In order to aid the Congress in this investigation, we have made a study of our 1960 operation, on the assumption that both construction and operating subsidies were applicable to Puerto Rico with the same number of ships, and under present freight rates in the trade the study showed that such an operation would still not produce a profit. In our case, we estimate it would produce a loss of \$439,106 annually, before any return on the capital invested. Additionally, the history of exceptionally poor showings of the carriers in the Puerto Rico trade makes it extremely doubtful that anyone would risk the capital necessary to build new ships.

All of the carriers in the Puerto Rico trade have been fully conscious of the need to retain freight rates at the lowest possible level consistent with service demands, and they have introduced technological advances as much as possible.

Since cargo-handling costs consume the largest percentage of the revenue dollar, Bull has engaged in a long-range program of containerization in order to reduce handling cost to a minimum. Because of the sensitive labor situation this has had to be introduced on a gradual basis to avoid sharp dislocations and labor disturbances. We learned our lesson in a long, costly strike which paralyzed the island for about 2 months, when the producers of sugar decided suddenly to move raw sugar in bulk instead of in bags, displacing stevedores with the bulk-loading facilities.

At that point, Mr. Chairman, I would also like to comment on the peculiarities of the labor situation in Puerto Rico. In the entire port of New York, for example, the longshore force consists of approximately 25,000 people. In Puerto Rico there are in excess of 10,000 persons entered on the rolls in the longshore industry. Not all of those people earn what might even be termed a decent living because they do not get enough work. In the course of a year, on a tabulation that was just completed for other purposes, the number of persons who worked a minimum of 200 hours, and not exceeding 900 hours in one year, the total was approximately 5,200.

Puerto Rico being unfortunately plagued with the matter of unemployment, in dealing with the sensitivity of this labor and moving abruptly into automation, it is very easy to understand that Fomento, for example, will spend an extraordinary amount of effort, and they feel successful, which they have every reason to feel, when they are able to promote a plant to come to Puerto Rico to employ anywhere from 10 to 15 people in some cases, perhaps 50 people. But you realize how many plants would have to be established in Puerto Rico if, because of the introduction of automation or technological improvement, whatever we want to call it, just realize how many plants

it would take to displace the 10,000 people that are presently employed on the waterfront.

We realize that that is a problem. We are working now with the unions in view of a new contract coming up, to try to find some solution, to get the casual worker out of the steamship industry. But we realize that after we get them out of our industry, what are they going to do if there isn't any other work available?

To go back to my prepared statement again: Gradual containerization was started by us in 1946, when commercial services were restored following World War II. In 1954 Bull introduced a larger van unit two and one-half times larger than the 1946 version. A short time later refrigerated units were introduced. In all, some 600 8-foot units and in excess of 400 15-foot units were placed in service by 1956 along with the 17-foot refrigerator unit.

Labor problems in the United States delayed introduction of still larger units. Finally, in late 1959, labor and the New York Shipping Association agreed to arbitrate "automation." Until those issues were resolved, Bull was unable to put in service larger units of the 35-foot variety, and was even prohibited from adding any more units of the sizes then in service. With the labor issue being firmly resolved by an arbitration award of November 16, 1960, further progression of automation was possible.

In December 1959, when the Statehood Line and the New York Shipping Association agreed to arbitrate the issue, the freeze, so called, on the introduction of any further automation, was resolved. We then introduced into the Puerto Rico trade 166 35-foot units, and we have plans for the introduction of still more.

At the same time a word of caution must be injected lest we expect automation to provide all the answers. It is the considered opinion in the industry that the capital expenditures required when added to the demand of labor to share in the fruits of increased productivity may produce results far short of anticipation.

I reviewed generally the transcript of last week's hearings, and I would like to comment on portions of the testimony which in our opinion is either erroneous or incomplete.

1. The Commonwealth has complained of high freight rates to Puerto Rico. I have shown above, in my exhibit which I discussed earlier, that rates to foreign areas in the Caribbean are generally higher than to Puerto Rico. It is also noteworthy that rate increases to other noncontiguous areas since the war have exceeded ours—in some cases by as much as 80 percent. The general rate increases have been as follows:

May 10, 1948, 10 to 12½ percent.

In a statement introduced in the record by the Commonwealth there is a freight rate increase shown as being effective in 1946. Actually, what that 1946 publication was is a gathering together of various surcharges, various charges that had been made when the War Shipping Administration was operating the services rather than the steamship lines. The net result was that when commercial services were restored it was necessary to bring out a composite tariff: tariff No. 3 came out in May 1946. It superseded tariff No. 1, which was published in January 1939.

In the early portion of my statement I connected the relationship of docket 807 and docket 500. It was tariff No. 2, as I recall, that was involved in docket 500, and it did not go into effect.

The next increase was on November 12, 1951, at which time the freight charges were adjusted on the basis of 10 cents per hundredweight on outward cargo, and only $3\frac{1}{2}$ cents a hundredweight or 2 cents a cubic foot on inward cargo. That increase amounted to approximately 15 percent overall.

At that point I think it might be significant to refer to the tables of wages which are attached to my statement, wherein you will note that in 1948 as a general proportion your wage rates in Puerto Rico and your wage rates in New York were comparatively low. You had tremendous increases in the period of those 3 years and since that time as well.

It is also necessary for us to call attention to the measure of the rate which was established on the northbound commodities. Those were the sensitive items; those were the so-called promotional rates established for the purpose of generating this industry in Puerto Rico as far as the steamship lines could do it. There is some further comment later on in my prepared statement. I don't want to take up too much of your time except to stress the point that here again we demonstrated that the carriers were fully cognizant of what was needed for Puerto Rico. Perhaps those rates could have been increased far more. If they were, there was no question it would have affected factories which were established in Puerto Rico.

There was no further freight rate increase until 1957, the carriers having absorbed all of the increased costs during that period—that was approximately 6 years—and were finally economically compelled on January 10, 1957, to file increases amounting to 15 percent or 6 cents per cubic foot, or 12 cents per hundredweight. Finally in 1958, the carriers were compelled to make a general further increase of 12 percent. The total cumulated increases in this trade since World War II is slightly less than 65 percent.

2. The Commonwealth expressed the view that freight rates have endangered its economy. To the contrary, the Bull Line has aided the establishment of industry in Puerto Rico, through the publication of rates designed to encourage the industrialization of the island. Many of those rates were noncompensatory years ago. Today those noncompensatory rates are at ruinous levels; others that were barely compensatory fall far short of covering even handling costs today. For example, while refined sugar is not a promotional rate, none the less it is a rate that is very important to the economy of the island. The rate today produces the carriers' revenues of approximately \$13 per gross ton. The actual cost of handling refined sugar exceeds the revenue because here again the methods and the demands of making delivery of refined sugar are expensive. Shippers in Puerto Rico will forward to their brokers in the North Atlantic area shipments of anywhere from 10 to 50 thousand bags of sugar. Steamship lines are required to make delivery of that sugar in lots anywhere from 100 to 500 bags. The average delivery is about 500 bags because that approximates a truckload.

To go back to my statement: Indeed, the promotional rates on inward industrial commodities were so low that not all the carriers

were interested in the carriage of inbound cargo to North Atlantic ports. Even today other carriers either offer no service or are reluctant to provide full service northbound to the North Atlantic ports. Bull, however, has continued to provide the northbound service despite the inadequate rate level.

3. The Commonwealth has stated the "lower shipping costs have already been a factor in shifting most of Puerto Rico's extensive lumber purchases from the United States to Canada." The fact is that the lumber rates of the principal Canadian carrier to Puerto Rico are 10 percent higher than those from U.S. ports.

I would like to briefly recite the history of the Bull Line in handling lumber. For a good many years Bull Line maintained a service from South Atlantic ports that originated large quantities of lumber destined to Puerto Rico. We maintained this service just as long as it was possible for us to do so. The level of rates was somewhat lower than it is today, but even on an increased level of rates we could not profitably sustain the service, and we were forced to abandon it.

4. It has also been stated that freight rates may have contributed to the heavy inroads made by European cars and trucks and some other manufactured goods. We do not share that view. But import taxes levied by the Commonwealth itself have an important restrictive role in the movement of autos to Puerto Rico. The Commonwealth assesses an extremely high graduated excise tax on cars.

A car valued at more than \$2,300 is assessed \$660 plus 80 percent of the excess over \$2,300. The ocean freight rates on automobiles are from \$140 to \$180 depending on size—less than half the Commonwealth's excise tax. The tax has sharply reduced the movement of high-priced American cars.

Here again, if I may leave my prepared statement: While the rates on automobiles were adjusted upward in the last freight rate adjustment, they were immediately dropped back to their former level and today are on substantially the same level as they have been for a long number of years. Additionally, the type of car that moved to Puerto Rico years ago in quite some volume—Cadillacs, Buicks, Pontiacs, Oldsmobiles; in other words, the higher priced cars—today not too many of them move. I can't recall our line moving a Cadillac to Puerto Rico in about 2 years. I do recall one about 2 years ago, but that was for a special purpose.

In prior years that type of auto moved in considerable quantities—in other words, the larger car that I was just speaking of—and the small European car has largely taken its place.

As for other European imports, it would be logical that they should increase. The Commonwealth is promoting such imports as well as the establishment of European industry in Puerto Rico. A week or so ago I read an article in the Puerto Rican press to the effect that Fomento—"Operaton Bootstrap"—was considering moving their European office from its present location to a more strategic one. The article further went on to state that activity in this European field would be increased, and in any event the ability of European goods to compete in U.S. markets is very well known to all of us. The essential base is lower wages as compared with our standards.

Here it might be appropriate to comment that for a long number of years one of the basic volume moving commodities to Puerto Rico was iron and steel articles. Today very little iron and steel moves to Puerto Rico from the United States. It all moves from abroad.

5. It has been indicated by Commonwealth witnesses that a dire need for passenger services exists. I would like to point out that our experience operating a deluxe passenger liner service lead to near disaster. After some 2 years operating the SS *Puerto Rico* we were forced to withdraw and had to dispose of the ship for approximately one-half million dollars, a fraction of its initial cost. We found the passenger demand existed for a few short months in the winter season. Invariably at other times the crew outnumbered passengers—sometimes 3 to 1.

I realize the Commonwealth has grave problems confronting them. We have a similar one: we are caught between progress in Puerto Rico, which means increasing costs, and an inability to recover those costs from the rates. We will be faced in September of this year with negotiating a new longshore labor contract in Puerto Rico. At the present time, we are negotiating a new contract with the Seamen's Union. The constant increases in costs without corresponding increases in revenue are bound to result in deterioration of the kind of service Puerto Rico needs and demands.

We have noted that carriers in the other domestic trades have specific suggestions to improve their trades and services. These are suggestions peculiar and applicable to those trades.

Conditions in each of those trades are not the same. What is good for Alaska or for Guam or for Hawaii may not fit the uniqueness of Puerto Rico's aspirations and economy.

The brief period afforded us in preparing for these hearings has been insufficient to enable us to make the kind of study which would lead to a responsible recommendation. In the recent enacted vessel exchange legislation, which our company and Alcoa played a major part in formulating, we think we have found at least an interim solution.

I might add here that there is another area in which the lines serving Puerto Rico could be aided considerably, and that is if the Commonwealth would undertake to clear up the differences between local laws and Federal laws.

Steamship lines operating in the Puerto Rico trade have paid out millions of dollars in overtime suits, first trying to observe the local law in Puerto Rico, then later discovering through suits that were started by attorneys getting together a number of longshoremen, and other suits that raised serious question as to what was supervisory personnel. We went on the basis of the local law, which was to the effect, substantially, that any person who had the authority to hire and fire came under the category of an executive. That is a peculiar way to interpret it, but in a case which acted as precedent, the so-called major domo in the sugar industry, who did have the authority to hire and fire cane workers, was classed as an executive. On that precedent we went along. We found that we were in error.

To repeat, millions of dollars have been paid out by the steamship lines. There is a conflict there which could be cleared up, and we would most certainly welcome any suggestions or aid that could be given to the lines in that respect.

To go back to my statement again: We pledge our complete cooperation to this committee and to Maritime on any investigation they deem fit to make with respect to the Puerto Rican trade.

Despite the heat that has generated over freight rates, I would like to take this opportunity to assure the Commonwealth that Bull has no desire whatsoever to disturb the economy by unwarranted rate demands. I feel safe in saying this is the attitude of all the lines.

Mr. Chairman, that completes my direct statement. I am very grateful for the opportunity of appearing before this committee.

(Appendixes to statement follow:)

Stevedore hourly wage schedule

PUERTO RICO

Effective	Basic hourly	Funds	Total	Percent increase
Jan. 1, 1947	\$0.90		\$0.90	
Jan. 1, 1948	1.00		1.00	11.1
Jan. 1, 1949	1.05		1.05	5.0
Jan. 1, 1950	1.05	\$0.13	1.18	12.4
Jan. 1, 1951	1.13	.13	1.26	6.8
Jan. 1, 1952	1.23	.15	1.38	9.5
Jan. 1, 1953	(¹)	(¹)	(¹)	(¹)
Jan. 1, 1954	1.33	.15	1.48	7.2
Jan. 1, 1955	1.43	.15	1.58	6.8
Jan. 1, 1956	1.53	.18	1.71	8.2
Jan. 1, 1957	1.63	.18	1.81	5.8
Jan. 1, 1958	1.71	.18	1.89	4.4
Oct. 1, 1958	1.81	.33	2.14	13.2
Oct. 1, 1959	1.91	.33	2.24	4.7
Oct. 1, 1960	2.01	.33	2.34	4.5
Total percent increase, 1947-60				160.0

¹ No increase.

NORTH ATLANTIC PORTS—NEW YORK

Aug. 21, 1947	\$1.75	\$0.025	\$1.775	
Aug. 21, 1948	1.88	.095	1.975	11.3
Oct. 1, 1950	2.00	.1625	2.1625	9.5
Oct. 1, 1951	2.10	.1875	2.2875	5.8
Oct. 1, 1952	2.27	.1975	2.4675	7.9
Oct. 1, 1953	2.35	.2225	2.5725	4.3
Oct. 7, 1954	2.42	.2925	2.7125	5.4
Oct. 1, 1955	2.48	.2925	2.7725	2.2
Oct. 1, 1956	2.66	.42375	3.08375	11.2
Oct. 1, 1957	2.73	.42375	3.15375	2.3
Oct. 1, 1958	2.80	.46	3.26	3.4
Oct. 1, 1959	2.92	.653	3.573	9.6
Oct. 1, 1960	2.97	.66725	3.63725	1.8
Oct. 1, 1961	3.02	.66725	3.68725	1.4
Total percent increase 1947-60				107.73

Senator ENGLE. Admiral McCarthy, this is a very fine statement. Mr. Grinstein has some statements which he would like to submit to you for your answers for the record. Would that be all right?

Mr. McCARTHY. Yes, indeed, sir.

Senator ENGLE. I will ask only one question: I am always intrigued when somebody doesn't want a subsidy. I understand that Alaska, Hawaii, and Puerto Rico, as governments, came in and asked for a subsidy. I understand that yesterday several shipping lines came in and, as does Bull, were opposed to subsidy. Unhappily, I couldn't be here. I was before the Committee on Education and Labor trying to continue the subsidy my people get for federally impacted school

areas in California. That took the greater part of the morning, and I am not sure I rescued it.

But most people do like to get ahold of a subsidy. Why don't you want a subsidy? You say it isn't necessary. Do you have any other reasons?

Mr. McCARTHY. Mr. Chairman, let's look at it this way: I don't know that I speak for all of the lines. I am only speaking for myself.

First of all, being rather conscientious about the whole thing, I don't think that it is correct to accept something for nothing unless it is going to do you some good. We have taken a situation, a theoretical situation. I covered it somewhat in my testimony. We assumed that tomorrow morning we are going to be a subsidized line. We are not only going to have a construction subsidy, but we are going to have an operating subsidy as well.

Then you have to ask yourself: all right, what are you faced with? To replace a vessel similar to the type that we are operating today would roughly cost about \$11 million. I use that figure because Moore-McCormack have just developed delivery of a number of vessels built under subsidy of approximately two of the ships that we have in that trade. So Uncle Sam is going to, first of all, donate \$5 million on every ship—\$5 million to \$5,500,000, roughly, 50 to 52 percent subsidy—on every ship that goes into the trade. What is going to be gotten out of that?

Then the next question that you have is, all right, that is the construction end of it.

Then you go to the operating subsidy. A good deal of the wages are going to be picked up. Some of the insurance will be subsidized. But when you add it all up, you come up on present freight rates with a deficit of \$139,000. It hadn't cured the situation, and the contribution that has been made by the taxpayers is a very considerable amount of money.

That is our reasoning and our logic to our approach.

Senator ENGLE. I suspect that any shipping line could figure out why it needed a subsidy. You said that you don't need one because trade requirements don't justify it. But you philosophically are opposed to the subsidy principle and the Government in this business, is that right?

Mr. McCARTHY. No, sir, we are not opposed to subsidy, sir. My comment was that since the subsidy will not produce anything—in other words the subsidy wouldn't help the situation—therefore why ask the Federal Government to contribute that much money for a zero accomplishment?

In our trades we think, as I stated, that the recently-enacted ship exchange bill is a much more desirable situation. For example, if we go back to the matter of—

Senator ENGLE. I like that bill. I was the author of it.

Mr. McCARTHY. Yes, sir, I recall that.

For example, if we go back now to the construction subsidy, and you have \$5 million of money invested in each and every ship, Bull operates six C-2 ships in that trade. That means an investment of \$30 million. We can accomplish the same purpose much better by trading in older vessels, under suitable vessels, and, for example, a C-4 ship which we have now pending before the Board, we are attempting to acquire two C-4 vessels by the trade-in of a Liberty ship.

The swap as you know, Senator, will be practically ship for ship, and that is the way it works out.

For \$1,200,000 in conversion costs we will have produced a ship that is just as good a ship as the one on which \$11 million could have been spent in other directions.

In other words, there is more relief in your ship exchange bill than there is in the subsidy bill for this particular trade.

The conditions in the other trades are not the same. In other words, you have the case of Guam, where they travel tremendous distances with no return cargo.

You have Hawaii, where the Matson Line has a vessel roughly every day and a half. You have two-way trade there.

You have the third case of Alaska, with rather hazardous navigating conditions and other operational difficulties, including weather, and there is no substantial movement.

In Puerto Rico you have a fairly good movement in each direction. The southbound movement exceeds the northbound considerably. So there is a need for everyone of them. Perhaps for Guam a subsidy is the answer.

Mr. Sevier stated it is not the answer for Matson. I am not quite positive of the position of Alaska subsidy lines.

Senator ENGLE. They were against it.

Mr. McCARTHY. They were against it as well.

As I say, in Puerto Rico, and perhaps this same line of thinking was Matson's as well, you can accomplish more in other ways with less expenditure of money because the Puerto Rican trade simply cannot afford to have a \$5 million ship in that trade. It won't support it. It just will not support it.

Today, for example, the feeling is that the freight rates are too high. I doubt that there is a vessel in the Puerto Rican trade today, at least of the break bulk carriers, that is on the books for much over \$500,000.

Senator ENGLE. Have you read the statements submitted to this subcommittee by the Representative of the Puerto Rican government?

Mr. McCARTHY. I have, sir.

Senator ENGLE. You do not agree with it?

Mr. McCARTHY. I do not agree with some parts of it. And the parts with which I disagree I have covered in this statement. Roughly there were five of them.

To go back to it, I don't know whether they were the result of misinformation or what, but we wanted to get the record straight in that respect.

As to the general desires of Puerto Rico, we have no quarrel. We want to cooperate with them.

Senator ENGLE. As I understand it, their witness stated that the excess burden of rates for Puerto Rico was in excess of \$10 million annually. That is, if foreign ships could participate in that trade the rates would be \$10 million less. As I listen to your statement—

Mr. McCARTHY. No, sir.

Senator ENGLE. You do not believe that to be true, and your exhibit has the purpose of proving that foreign trade ships to ports of equivalent distance actually charge rates that are higher than exists in Puerto Rico.

Mr. McCARTHY. Yes, sir, that is the purpose of this exhibit, to demonstrate that out of the 12 ports or countries or areas listed, that Puerto Rico enjoys a lower basis of rates than any of those points, with few exceptions, and practically all of the other points except Puerto Rico are served either by foreign-flag lines or, in some cases, subsidized American lines.

My contention is that the level of rates to Puerto Rico today is the lowest in the entire Caribbean.

Senator ENGLE. What about the density of traffic to Puerto Rico? Are we talking about eggs and oranges?

Mr. McCARTHY. I didn't hear that.

Senator ENGLE. What about the density of traffic with reference to these rates. In this exhibit that you have presented to the subcommittee you compare rates, but you don't compare volume.

Mr. McCARTHY. That is quite true, sir. I have made no attempt to compare volume because while I am aware of what the volume of traffic is to Puerto Rico, I must confess complete ignorance of the volume of traffic moving to any of these other points.

My exhibit was not intended to show anything but what the rates to these various points are today.

Senator ENGLE. It seems to me that that would have a very heavy bearing on the rates. That is, if you get heavy volume you can reduce rates, can't you?

Mr. McCARTHY. Not in all respects, sir.

In the Puerto Rican trade, for example, the more volume you have, it has not had the effect of reducing your cost because, as I outlined earlier, the demands of the Puerto Rico trade are such that you perform an awful lot of work for the consignee, for the shipper, in acting as warehouseman and delivery. And the more volume you had of that kind of traffic, the more your expense will be.

Senator ENGLE. Would you make more money with an 80-percent load than you would with a 100-percent load?

Mr. McCARTHY. It all depends, sir, on what the commodity is.

For example, if you were talking bulk, obviously a 100-percent load would produce more than an 80-percent load.

Volume has a very great effect up to a point. For example, if a vessel were sailing with insufficient cargo to pay her expenses, just simply because of a lack of volume, that is one thing.

If there is ample volume available, and there is ample volume available in the Puerto Rican trade—I have no figures with me at this moment, but as I recall all of that was gone into very elaborately in docket 807, and in that docket there are the utilization tables of all the lines in the trade. The volume is in the Puerto Rican trade, let's not deny that.

Senator ENGLE. If a subsidy is granted, who gets the subsidy?

Mr. McCARTHY. Who gets it?

Senator ENGLE. Yes.

Mr. McCARTHY. That, sir, I don't know.

Senator ENGLE. Presumably it would be reflected in reduced rates, would it not? In other words if the Federal Government gave the subsidy which is requested, it wouldn't do Puerto Rico any good unless they got lower rates, would it?

Mr. McCARTHY. Well, sir, as I pointed out in my statement, if we were to become a subsidized line tomorrow morning, and we carried identically the same volume and identically the same volume as we carried in 1960, we would be out of pocket \$439,000. That is a far cry from being out of pocket almost \$2 million on our 1960 operation.

Senator ENGLE. You just wouldn't go broke as fast.

Mr. McCARTHY. That is exactly the point, Mr. Chairman. In other words two things have to happen in the Puerto Rican trade, in either direction: the rates have to come up even though you were to subsidize the trade to make it break even.

Senator ENGLE. When you arrived at that \$435,000 figure, were you presupposing the subsidy contemplated by this bill, or the subsidies elsewhere in existence?

I will withdraw the question because we don't have a specific proposal. But did you base it upon the maritime operations at the present time?

Mr. McCARTHY. That is correct, sir.

Senator ENGLE. What it boils down to is that instead of losing \$2 million you would lose \$435,000, but you couldn't effect a rate increase because you would still be in the red?

Mr. McCARTHY. That is right.

Senator ENGLE. How long can you go on losing \$2 million?

Mr. McCARTHY. We have asked ourselves that question over and over again. As a matter of fact it is reaching the doubtful point right now.

This has been going on for years, Mr. Chairman. I don't think any of the lines in Puerto Rico have made money in the trade for several years. They didn't make any money in 1960; there was no money made in 1959; there was a slight profit made in 1958 which amounted to \$200,000. In 1957 our losses were \$997,000.

Senator ENGLE. I will have to confess that I am still puzzled. You are going \$2 million in the red annually; you are not in favor of a subsidy; the government of Puerto Rico has advocated a subsidy and claims that the rate structure or the tariff for bringing goods in costs them \$10 million more than it should, annually.

I notice in your statement you say that you are not prepared now, because of the pressures in preparing this statement, which is an excellent statement, to make any responsible recommendations.

Mr. McCARTHY. That is right, sir.

Senator ENGLE. You are going to have to do something pretty soon, aren't you?

Mr. McCARTHY. Yes, we are. No question in the world about it. We are going to have to do something pretty soon. Perhaps I didn't make myself sufficiently clear. I said that we are not opposed to a subsidy. What we feel is that your vessel exchange legislation will accomplish the purpose better.

For example, if we were called on tomorrow morning to go out and to replace our fleet, and to produce \$30 million as our part of a \$60 million-odd vessel replacement program, we don't have the money, and we couldn't get it.

Now, the freight rates to Puerto Rico will be reflected in the amount of capital that is invested there. Maritime has found, as I recall, that we would be entitled to roughly a 7½-percent return on our capital.

Seven and a half percent of \$5 million per ship is an awfully, awfully lot more than 7½ percent of \$1,200,000 in a converted vessel.

Senator ENGLE. Why don't you use that ship conversion bill?

Mr. McCARTHY. We are using it. We have an application in right now for two C-4 vessels. We have nominated the two Liberty ships to be exchanged. We have selected the two C-4's that we want. We also have an application in for title II insurance on them. That is in motion right now.

We hope, if all goes well, that within roughly 6 months time we will have two of those ships in the Puerto Rican trade. When we get them settled down then we hope to go to two more for our other trades.

Senator ENGLE. And this is the alternative that you have in mind—

Mr. McCARTHY. That is right.

Senator ENGLE. To the subsidy program?

Mr. McCARTHY. Right.

Senator ENGLE. And which you think over the long haul will erase your \$2 million annual deficit and put you back in business?

Mr. McCARTHY. In the black.

Senator ENGLE. That is correct.

Mr. McCARTHY. That is correct, absolutely correct.

Senator ENGLE. Now the light has dawned.

Mr. McCARTHY. I am sorry I didn't make myself clear.

Senator ENGLE. I appreciate your very fine statement, Admiral.

Mr. McCARTHY. Thank you, sir.

Senator ENGLE. The next witness is Mr. J. M. Lykes, Jr., senior vice president of the Lykes Bros. Steamship Co.

Mr. Lykes, we will be very glad to hear your statement.

**STATEMENT OF J. M. LYKES, JR., SENIOR VICE PRESIDENT,
LYKES BROS. STEAMSHIP CO.**

Mr. LYKES. Thank you, Mr. Chairman. I appreciate the opportunity of appearing before this committee.

My name is J. M. Lykes, Jr., I am senior vice president of the Lykes Bros. Steamship Co. I have been associated with Lykes' operations since 1930, and our Caribbean services, which include our service to Puerto Rico, are under my particular charge.

I am appearing before this committee in view of Lykes' long interest in Puerto Rico, and while I do not feel it necessary to go into all the facets of its operation, I believe the facts related below might be of assistance to the committee in resolving the matter at hand. From its testimony, undoubtedly the Commonwealth feels that it has its problems; we know we have one—namely a cost/revenue squeeze. We think this investigation therefore is most timely. We were particularly impressed by the testimony given by Mr. Stakem, and much will be gained by a careful analysis of the alternatives put forward by him. While we have no specific suggestions or recommendations at this time, we do, as stated, have real interest and would be prepared to testify later when the committee has particular legislation before it.

Lykes commenced its operation of service to the Latin American area in 1907. This service was broadened to include Puerto Rico in

1920, and after 1928—except for wartime interruptions beyond our control—Lykes furnished regular weekly service from west gulf ports to the principal Puerto Rico ports, until very recently. Due to the heavy losses in the Puerto Rican trade suffered by the company in recent years, we were compelled to reduce service to Puerto Rico to a fortnightly basis in July 1960.

Lykes' losses in the Puerto Rico phase of its operation for the years 1957 through 1960 were substantial. As the committee is well aware, the details of our operating results are on file with the Federal Maritime Board.

The cost squeeze which has been referred to stems, of course, from the continuing increase in cost factors without corresponding increase in our revenues. The following is a résumé of major elements of Lykes' cost increases 1951 to 1960.

Longshore wages including fringe benefits 1951 compared with 1960 were:

	1951	1960	Percent Increase
West gulf.....	\$1.97	\$3.39	72
Total per hour cost to employer (fringe benefits included), Puerto Rico.....	1.26	2.34	94

Cargo handling costs consisting principally of longshore wages absorbs between 45 and 50 percent of Lykes' revenue dollar.

Vessel operating costs, 1951, as against 1960 for our C-1B and C-2 type vessels were:

Vessel operating costs per diem (excluding depreciation, overhead, and fuel):

1951.....	\$1,008
1960.....	\$1,805
Percent increase.....	80

The 1960 figure is approximate, in that all of our accounts were not completed to get an actual figure. This vessel operating cost absorbed, in addition to cargo handling costs mentioned, approximately 45 percent of Lykes' revenue dollar. As noted, they exclude fuel and overhead which are constantly increasing cost factors, as well as depreciation which in itself is equally important.

The committee has before it the historical record of general rate increases in the Puerto Rico trade. Lykes, as a member of the Puerto Rico Conference, has had the same experience in this respect as the other carriers. We do believe it would be helpful in the light of Lykes' particular cost increases, which we have just outlined, to place in the record the rate increases corresponding to the same period; namely 1951 to 1960. On November 12, 1951, there was a general increase of 10 cents per hundredweight, or 5 cents per cubic foot, which percentage-wise approximates 15 percent at the most. From this base the cumulative rate increases up until the present time were 28.8 percent. In the light of major elements of cost increases ranging from 72 to 94 percent, shown above, it is evident that revenues have failed to keep pace with sharply rising cost factors.

In conclusion, we repeat that Lykes has a long-range and deep interest in the Puerto Rican trade. We shall follow the proceedings

closely and feel confident that at a very early date the Federal Maritime Board together with your staff will formulate proposed legislation. At that time we shall look forward to testifying concerning the specific proposals therein suggested.

Thank you, Mr. Chairman.

Senator ENGLE. Mr. Lykes, I observe from your statement that you are going broke on this trade, too.

Mr. LYKES. It has been very costly, sir.

Senator ENGLE. That is the understatement of the day.

Do you agree with Admiral McCarthy that this ship exchange bill could provide the route to get back in the black?

Mr. LYKES. I am not familiar with the bill, Mr. Chairman. As I understand it, it is a vessel exchange and it would permit us to continue without building new vessels for a time, which as I understand it, would prolong the question of new construction, which is most costly.

Senator ENGLE. We very much appreciate your statement, Mr. Lykes.

Thank you very much.

Mr. LYKES. Thank you, sir.

Senator ENGLE. This subcommittee will stand in recess for a hearing by the full committee on some nominations.

At this point we would like to insert in the record the statement of Mr. G. C. Halstead, vice president and director of Alcoa Steamship Co.

STATEMENT OF G. C. HALSTEAD, VICE PRESIDENT AND DIRECTOR, ALCOA
STEAMSHIP CO., INC.

Mr. Chairman, my name is G. C. Halstead. I am vice president and director of Alcoa Steamship Co., Inc., whose principal office is at 17 Battery Place, New York City. Alcoa has operated U.S.-flag vessels without subsidy before, during, and since World War II, in both foreign and domestic trades. Our fleet consists of 10 C1-B vessels and three C2 vessels. Alcoa has a long history of serving the Caribbean area, having started its service in 1923.

We welcome the opportunity to participate in this study concerning the non-contiguous domestic trades. We are hopeful that a careful and a complete study of the problems confronting the carriers, as well as any confronting the shipping public, will result in a solution fair and equitable to all concerned.

Our comments are limited to the Puerto Rico trade. We do not offer any service to the other domestic offshore areas which are part of this overall study. Alcoa commenced its service to Puerto Rico from east gulf ports in 1951 and from North Atlantic ports in 1952.

In our gulf service we offer a regular weekly service from Mobile and New Orleans to San Juan, Ponce, and Mayaguez. Cargo offerings have warranted recent service from Gulfport, Pensacola, Panama City, and Baton Rouge. From the North Atlantic we maintain regular weekly service from Baltimore and New York to San Juan, Ponce, and Mayaguez. Again, cargo offerings have recently warranted service from Searsport, Portland, Philadelphia, Norfolk, Charleston Georgetown, Savannah Jacksonville, Miami, and Tampa.

As part of our gulf and North Atlantic services we offer the only regular, scheduled service to the Virgin Islands.

Common carrier services to and from Puerto Rico have recently been the subject of a comprehensive investigation in *Atlantic & Gulf-Puerto Rico General Increases in Rates and Charges*, Board docket 807. Alcoa has contributed a great deal of time, effort, and expense in connection with the preparation and submission of evidence in this docket. The record in docket 807 is readily available and should be carefully considered by this committee. This record shows that even with the latest increases in rates on January 9, 1957, and January 5, 1958, Alcoa is operating at a loss on its regularly scheduled southbound services

from continental U.S. ports to Puerto Rico. The actual operating results since the close of the record show that losses are continuing.

At the time of our entry into the Puerto Rico trade, route conditions were carefully studied by management. We accepted the fact that the trade was restricted to American-flag ships and that there was no subsidy in the trade. We knew the terminal facilities were adequate although, particularly in Puerto Rico, not the best or most modern. We, of course, accepted the fact that we would be subject to American-style labor conditions on our ships and on our piers. We knew there was free entry into and exit from this trade, and that the active competition, including competition from MSTs, would be present. We were aware that this trade was subject to regulation by the Federal Maritime Board and that there was considerable precedent in its decisions indicating that with normal service patterns rates would be approved which permitted the operating companies as a whole to earn a reasonable profit. These were the rules of the game.

Alcoa immediately upon entering into the trade commenced investing money in improvements in terminal facilities in Puerto Rico and in other ways attempted to reduce costs. We invested money in our own trade development program supplementary to Operation Bootstrap. The resulting increase in revenues proved insufficient to absorb the continually rising costs. It became obvious that rate adjustments must be made, and accordingly new rates were put into effect by the conference. Hearings before the Federal Maritime Board commenced in 1957 and after 4 years of litigation the proceedings are still not concluded.

The carriers and the shipping public are now in a state of uncertainty. Carriers' costs are increasing daily. They have already absorbed substantial increases in longshore and crew wages and now face fresh labor negotiations in the immediate future. Losses are mounting, and carriers' confidence in the trade is decreasing.

We subscribe to rate regulation by hearings before the proper authority. We do not subscribe to rate regulation by pressure tactics, irresponsible attacks in the public press, and the like. The political pressure by the government of Puerto Rico with little regard for the facts is unfair to the carriers, leads only to worsening relations between them and the Commonwealth, and will result in deteriorating steamship service. The carriers must, of economic necessity, defend themselves against such attacks and against the delaying tactics of the Commonwealth.

Much has been written and spoken concerning the unfair burden of steamship rates on the economy of Puerto Rico. This is an area for most careful consideration and we are hopeful that the committee will not make any recommendations until a comprehensive study of the effect of rate increases on the insular economy is completed.

The situation is paradoxical. The conventional barometers of economic health indicate that the economic development in Puerto Rico over the past 10 years has been amazing. From the data of the Bureau of Economic Statistics of the Puerto Rico Planning Board and Puerto Rico Water Resources Authority, selected business indicators for the 10 years ending 1959 indicate: Commonwealth net income increased 92.3 percent; net income from manufacturing is up 197.6 percent; disposable personal income increased 83.6 percent; imports increased 129.2 percent; exports increased 146.6 percent; bank deposits increased 102.4 percent; and electrical energy consumption, 283 percent. Even as recently as March 7, 1961, a notice of sale for the \$40 million Commonwealth of Puerto Rico bonds indicates like glowing statistics. During the past 10-year period steamship rates have been increased approximately 29 percent.

How can it be that such a healthy economic situation exists in the face of the claim of burdensome steamship rates? Why is it that the steamship companies are denied a profit when responsible Puerto Rican authorities were quoted only last week in the New York Times justifying 12 to 40 percent profit on investment for new Puerto Rican manufacturing industries? What, exactly, is the total disadvantage suffered by Puerto Rican industry which profits from substantial tax benefits, special depreciation privileges, absence of custom duties, low wages, etc.? This entire problem of the alleged burden on the economy caused by steamship rates required the most careful study.

If, after careful and detailed study, it is found that an undue burden in fact exists, then and only then should forms of subsidy be considered. But if there is no such burden, a reasonably compensatory rate structure should be permitted without subsidy.

We have carefully studied Mr. Stakem's testimony before this subcommittee on March 6, and we noted his comments concerning construction and operating subsidy payments, similar to those now existing in the foreign trades. This form of subsidy produces essentially the same effect on costs as if foreign ships were allowed to participate in the trade. The Commonwealth wants to effect substantial reductions in existing freight rates in the Puerto Rico trade. Our studies indicate that such reductions cannot be obtained through construction and operating subsidy plans.

We have analyzed the results of our North Atlantic service to Puerto Rico for the year 1960. This service has resulted in a loss. We have estimated the results of this same service using foreign-flag operating costs. There are no profits obtainable under this estimate. In fact, there is still a sizable loss. This may seem strange to persons not familiar with the details of the expenses in the trade. But most costs are identical for both foreign and American ships. Thus, cargo handling expenses, port expenses, fuel, and overhead comprise about 77 percent of all expenses. The remaining 23 percent of total expenses, comprising principally vessel expenses including depreciation, is the only part that can be reduced by substituting foreign-flag costs. If, in fact, the foreign-flag costs were half as expensive as the American-flag costs, total expenses would only be reduced approximately 11 percent.

Mr. Stakem's other proposals are certainly unique and appear to be such that competitive drive will be stifled, which effect is normally not desirable, and is certainly no solution to the continuous upward spiral of rates due to costs.

In our study of the testimony to date before this subcommittee we have found instances of statements or statistics which do not accurately reflect the facts. For example, there has not been a 100-percent increase in ocean rates to Puerto Rico since 1947-48. The cumulative increases were in the neighborhood of 65 percent. It is interesting to note that according to the Bureau of Labor Statistics, this compares with an increase in the Consumer Price Index for public transportation for the continental United States of 131 percent since 1947. There was also a statement that passenger accommodations are saved principally for the shipper. This is not true. We are not attempting to pick apart the Commonwealth's statement because we realize that the subcommittee will scrutinize all testimony and check all the facts.

Thank you for this opportunity to appear before the subcommittee. It is obvious that further hearings, for the presentation of detailed and technical information, will be required to resolve this difficult problem. Possibly the type of investigation contemplated by section 212(f) of the Merchant Marine Act, 1936, would be appropriate.

The Alcoa Steamship Co. will be most happy to take part in such hearings and to contribute such facts as are required.

Senator ENGLE. The subcommittee stands in recess.

(Whereupon, at 11:23 a.m., the subcommittee adjourned.)

(The following information was subsequently submitted for the record:)

INTERSTATE COMMERCE COMMISSION,
Washington, D.C., March 14, 1961.

HON. WARREN G. MAGNUSON,
Chairman, Committee on Interstate and Foreign Commerce,
U.S. Senate, Washington, D.C.

DEAR CHAIRMAN MAGNUSON: This is a reply to your letter of March 8, 1961, requesting information on changes in freight rates over the last 10 years.

We regret that no index is available showing the trend of rail, highway, and water freight rates combined. There is available, however, and it is shown on the attached table, an index based on a sample of rail carload terminations showing changes in average freight rates on carload traffic since 1950. Two statements are attached relative to this index, one explaining the method, and the other showing the indexes in detail for 1951 through 1958.

We have also provided on the attached table information on revenue per ton-mile for class I railroads and for certain class I motor carriers as well as revenue per ton for maritime carriers. These averages, of course, reflect the influence of many factors in addition to rate changes and therefore should be used accordingly.

Please advise if we can be of further assistance in this matter.

Sincerely,

EVERETT HUTCHINSON, Chairman.

Freight rate index and revenue per ton-mile for class I railroads, revenue per ton-mile for class I motor carriers, and average revenue per ton for maritime carriers, 1950-59

Calendar year	Class I railroads		Class I motor carriers engaged in intercity service reporting revenue ton-miles ¹		Maritime carriers engaged in coastwise and intercoastal service ⁶	
	Index of average freight rates ¹	Revenue per ton-mile (cents) ²	Number of carriers ⁴	Revenue per ton-mile (cents) ⁴	Number of carriers ⁷	Average revenue per ton (dollars) ⁸
1960.....	(⁹)	¹⁰ 1.403	(⁹)	(⁹)	(⁹)	(⁹)
1959.....	118	1.445	885	6.234	26	\$19.73
1958.....	121	1.463	861	6.157	27	20.43
1957.....	118	1.445	828	6.124	30	19.02
1956.....	112	1.384	2,039	5.899	32	17.84
1955.....	108	1.370	2,036	5.730	32	18.65
1954.....	109	1.420	1,969	5.744	32	19.51
1953.....	111	1.478	1,894	5.670	29	18.79
1952.....	109	1.430	1,748	5.532	29	18.81
1951.....	102	1.336	1,638	5.102	28	18.07
1950.....	100	1.329	1,517	4.959	34	17.23

¹ Source: Indexes of average freight rates on railroad carload traffic, 1951-58, statement RI-1, September 1960. Figures for 1959 from tabulation not yet released (1950=100 for this index) (data based on the 1-percent rail carload sample).

² Source: "Transport Statistics in the United States," pt. I, table 44, 1950-59. Statement M220 for the 1st 11 months in 1960.

³ Source: "Transport Statistics in the United States," pt. 7, table 29 (1954-59); "Statistics of Class I Motor Carriers," table 29, 1950-53, statements 5228, 5351, 5423, and 5515.

⁴ From 1950 through 1956 class I motor carriers were defined as those having average gross revenues of \$200,000, or over annually from motor carrier property operations. Beginning with 1957 this amount was increased to \$1,000,000 or more.

⁵ Derived by dividing freight revenue from intercity service by the number of ton-miles of intercity service.

⁶ Source: "Transport Statistics in the United States," pt. 5 for 1954-59, and statements 521, 5439, 5442, and 552.

⁷ Number of carriers varies because of mergers, consolidations, new business, going out of business.

⁸ Derived by dividing freight revenue for coastwise and intercoastal service by number of tons carried in that service.

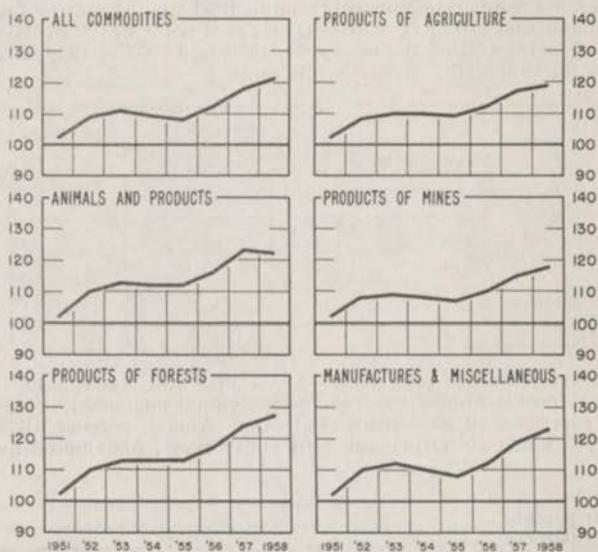
⁹ Not available.

¹⁰ For 1st 11 months of 1960.

 INTERSTATE COMMERCE COMMISSION, Bureau of Transport Economics and Statistics

indexes of average Freight Rates on Railroad Carload Traffic 1951 - 1958

1950 = 100


 Statement RI-1
 1951 - 1958

 September 1960
 Washington, D. C.

 This release, issued as information, has not been adopted by the Interstate Commerce Commission.

FOREWORD

This statement is the ninth in a series of annual indexes of average freight rates on railroad carload traffic. It includes information previously published for the years 1951-57 and adds results for the year 1958.

INDEX OF AVERAGE FREIGHT RATES, 1951-58

Table 1. Indexes of average freight rates for commodity groups and selected commodity classes

Table 1 shows indexes for average freight rates for commodity groups and selected commodity classes for the calendar years 1951 through 1958 with 1950 equal to 100.

The index for all commodities combined rose to 121 in 1958, the highest level reached thus far, continuing the upward trend begun in 1956. This rise reflects the general increases in rates authorized in February and August 1957, by *Ex parte 206* and the selective increases authorized in the interim and final decision in *Ex parte 212*.¹ It was estimated that the increases proposed in *Ex parte 212* would raise the overall rate level about 2.3 percent.

Trends in the indexes of average freight rates, 1951-58, for the major commodity groups are similar. The indexes rise through 1953, decline moderately through 1955, then resume the upward trend in 1956, and attain the highest level in 1958. Animals and products, however, decline 1 point to 122 in 1958.

The range of increase from the base year, 1950, and 1957 to 1958 varies considerably among the commodity groups as follows:

Commodity group	Percent change	
	1958 over 1957	1958 over 1950
Products of agriculture.....	1.7	19
Animals and products.....	- .8	22
Products of mines.....	2.6	18
Products of forests.....	2.4	27
Manufactures and miscellaneous.....	3.4	23
Forwarder traffic.....	4.8	30

The percentage increases between 1950 and 1958 and between 1957 and 1958 also vary considerably among the various individual commodity classes shown in table 1. Increases in 1958 over 1950 range from 3 percent (633 cement: natural and portland) to 45 percent (101 sugarbeets), distributed as follows:

	Classes
10 percent or less.....	5
11 through 20 percent.....	18
21 through 30 percent.....	19
31 through 40 percent.....	15
41 percent and above.....	3

¹ *Ex parte 206*, 299 I.C.C. 557, Feb. 4, 1957; 300 I.C.C. 633, Aug. 6, 1957; *Ex parte 212*, 302 I.C.C. 665, Feb. 11, 1958; 304 I.C.C. 289, Sept. 9, 1958.

Most of the individual commodity classes show index changes of from 2 to 5 percent increase in 1958 over 1957; six individual commodity classes show decreases. Commodity classes showing the largest and least or no percentage increase, and those showing decreases in 1958 from 1957 are:

LARGEST

Commodity class	Percent increase	
	1958 over 1957	1958 over 1950
309 Iron ore.....	10.4	38
401 Logs, butts and bolts.....	10.4	38
573 Iron, pig.....	8.8	36
577 Iron and steel, bar, rod, and slab.....	8.5	28
789 Scrap iron and scrap steel.....	8.2	32

LEAST

501 Gasoline.....	0	6
763 Food products, not otherwise specified, in cans and packages, not frozen.....	0	10
759 Sugar.....	0	19
003 Corn.....	0	24
773 Feed, animal and poultry, not otherwise specified.....	0	28
409 Pulpwood.....	.8	19
659 Printing paper, not otherwise specified.....	.8	22
403 Posts, poles, and piling, wooden.....	.8	27
669 Paperboard, fibreboard, and pulpboard.....	.9	11
329 Stone and rock, broken, ground, and crushed.....	.9	18
671 Wallboard.....	.9	18

DECREASES

Commodity class	Percent change	
	1958 over 1957	1958 over 1950
215 Meats, fresh, not otherwise specified.....	-4.8	19
343 Phosphate rock.....	-4.5	6
633 Cement, natural and portland.....	-1.9	3
085 Potatoes, other than sweet.....	-1.7	18
Oil bearing crops ¹	-1.7	19
Fresh vegetables ¹	-1.7	14
655 Scrap paper and rags.....	-1.5	30
749 Liquors, malt.....	-1.9	11

¹ These groupings of individual commodity classes are shown at the request of the Department of Agriculture. "Oil bearing crops" include commodity classes 037 to 047, 097 and 105; "fresh fruits," classes 049 through 069; "fresh vegetables," classes 077 through 089 (including 085 which is also shown separately).

Variation in the degree of change in average rate levels for the commodity classes, as shown herein, is due primarily to the effect of differing rate adjustments applied to traffic categories by the railroads. As explained elsewhere, the area of fluctuation in average revenue from causes other than rate adjustments should be relatively small in these indexes.¹ The upward trend in the level of rates which might have resulted from the general rate increases authorized by the Commission during the postwar period, which varied in percentage by territorial movements and were subject to numerous exceptions and holddowns, was further modified not only by the extent to which carriers applied the increases, but also by rate reductions in individual instances to meet competition. In 1954 and 1955 when no new general rate increases were authorized, the general level of rates trended downward, reflecting the effect of individual reductions. Ex parte No. 212 provided selective, rather than horizontal, increases consisting of percentage increases, flat increases, and percentage increases sub-

¹ Statement RI-1, March 1958.

ject to maximums or minimums. Certain commodities and movements were exempted entirely. The rate actions took into account many factors, including the need for increased revenues, cost of service, possible diversion of traffic to other modes of transportation, and an effort to distribute the burden of increase over as many commodities as possible.

Commodity class 337, petroleum crude, has been dropped from the list of commodity classes which are shown separately for two reasons. First, the number of carloads of crude petroleum as reported in the sample has declined over the years to 345 in 1958. (See footnote 1 of table 1.) Second, a comparative examination of 1957 and 1958 sample waybills indicates that the operation of newly constructed pipelines has apparently diverted entirely certain carload traffic movements of crude petroleum and caused an appreciable distortion in the index for this commodity class.

TABLE 1.—Indexes for average freight rates for commodity groups and selected commodity classes¹

[1950=100]

Item	Index								Approximate standard deviation
	1951	1952	1953	1954	1955	1956	1957	1958	
All commodities.....	102	109	111	109	108	112	118	121	0.5
Group I. Products of agriculture.....	102	108	110	110	109	112	117	119	.5
Class 001 Wheat.....	101	108	113	113	112	115	121	126	1.0
003 Corn.....	102	108	109	112	111	116	124	124	1.0
033 Cotton in bales.....	102	113	119	116	115	108	105	109	4.0
Oil bearing crops ²	103	112	113	114	113	116	121	119	4.0
Fresh fruits ²	101	106	107	107	106	109	114	116	.5
Fresh vegetables ²	101	106	108	107	108	110	116	114	.5
085 Potatoes, other than sweet.....	101	108	110	109	110	112	120	118	1.0
101 Sugarbeets.....	106	110	122	124	125	126	137	145	3.0
199 Product of agriculture, n.o.s.....	99	112	114	114	109	117	120	124	3.0
Group II. Animals and products.....	102	110	113	112	112	116	123	122	.5
Class 203 Cattle and calves, S.D.....	103	112	115	114	114	118	127	133	1.0
215 Meats, fresh, n.o.s.....	103	111	114	114	113	118	125	119	1.0
Group III. Products of mines.....	102	108	109	108	107	110	115	118	.5
Class 301 Anthracite coal, n.o.s.....	101	107	109	109	108	109	113	115	.5
305 Bituminous coal.....	101	107	108	106	105	109	111	113	.5
307 Coke.....	102	108	109	107	107	110	113	118	1.5
309 Iron ore.....	103	110	110	111	110	115	125	138	.5
323 Clay and bentonite.....	103	112	115	114	114	119	129	136	1.0
325 Sand, industrial.....	105	114	113	109	108	113	121	128	1.0
327 Gravel and sand, n.o.s.....	103	108	110	108	109	110	116	118	1.0
329 Stone and rock: Broken, ground and crushed.....	103	108	110	110	108	111	117	118	1.0
331 Fluxing stone and raw dolomite.....	104	110	111	112	113	117	129	136	1.0
339 Asphalt.....	101	110	111	111	109	112	117	122	1.0
341 Salt.....	102	108	109	107	108	109	112	118	1.0
343 Phosphate rock.....	102	109	112	113	105	108	111	106	1.5
399 Products of mines, n.o.s.....	101	110	110	109	110	114	124	129	2.5
Group IV. Products of forests.....	102	110	113	113	113	117	124	127	.5
Class 401 Logs, butts, and bolts.....	102	108	114	110	110	116	125	138	1.5
403 Posts, poles, and piling, wooden.....	101	111	110	113	114	118	126	127	1.5
409 Pulpwood.....	104	111	113	111	109	112	118	119	.5
411 Lumber, shingles, and lath.....	102	110	112	113	113	117	124	127	.5
499 Products of forests, n.o.s.....	103	110	116	114	117	121	133	141	2.5
Group V. Manufactures and miscellaneous.....	102	110	112	110	108	112	119	123	.5
Class 501 Gasoline.....	99	104	105	104	100	102	106	106	.5
503 Fuel, road and petroleum residual oils, n.o.s.....	99	104	106	104	103	104	110	114	1.0
505 Lubricating oils and greases.....	100	107	111	111	110	114	125	129	1.0
507 Petroleum products, refined, n.o.s.....	101	109	112	111	113	116	124	126	.5
527 Chemicals, n.o.s.....	101	105	108	106	104	118	124	128	1.0
533 Sodium (soda) products.....	99	107	108	106	104	107	116	119	1.0
539 Fertilizers, n.o.s.....	102	110	114	113	111	112	119	121	1.0
573 Iron, pig.....	104	113	114	113	114	117	125	136	1.5
575 Iron and steel: Billet, bloom, and ingot.....	103	112	113	108	104	111	123	125	2.0
577 Iron and steel: Bar, rod, and slab.....	101	108	110	107	105	109	118	128	2.0
583 Manufactured iron and steel.....	103	111	113	102	97	104	114	116	1.0

See footnotes at end of table.

TABLE 1.—Indexes of average freight rates for commodity groups and selected commodity classes¹—Continued

[1950=100]

Item	Index								Approximate standard deviation
	1951	1952	1953	1954	1955	1956	1957	1958	
Group V. Manufacturers and miscellaneous—Continued									
Class 687 Iron and steel pipe and fittings, n.o.s.	103	111	114	108	101	100	110	114	1.0
595 Machinery and machines, n.o.s.	103	112	116	115	116	121	128	133	1.0
613 Automobiles, passenger	102	103	103	105	103	108	115	122	1.0
623 Vehicle parts, n.o.s.	103	113	115	114	113	119	130	138	1.0
633 Cement: Natural and portland	103	110	112	110	104	102	105	103	.5
645 Lime, n.o.s.	102	110	113	113	111	116	125	131	1.0
655 Scrap paper and rags	104	113	115	114	116	122	132	130	1.0
659 Printing paper, n.o.s.	103	110	113	112	109	111	121	122	1.0
669 Paperboard, fiberboard, and pulpboard	103	111	114	111	104	104	110	111	1.0
671 Wallboard	102	111	114	110	108	110	117	118	1.0
697 Glass bottles, jars, and packing glasses, n.o.s.	101	108	109	109	109	115	124	131	1.0
707 Refrigerators, freezing apparatus, and parts	103	112	114	115	115	119	129	134	.5
715 Furniture, n.o.s.	102	110	112	113	114	118	127	134	1.0
749 Liquors, malt	102	110	113	111	103	104	112	111	1.0
759 Sugar	102	107	110	110	109	114	119	119	1.5
763 Food products, n.o.s., in cans and packages, not frozen	99	105	107	106	105	107	110	110	1.0
773 Feed, animal and poultry, n.o.s.	103	112	115	116	118	124	128	128	1.5
779 Containers, metal	103	112	115	114	116	122	132	141	.5
783 Containers, fiberboard, and paperboard, K.D.	103	112	114	117	115	119	130	133	1.5
789 Scrap iron and scrap steel	105	112	115	111	108	113	122	132	.5
793 Furnace slag	102	107	107	107	105	109	116	119	1.0
797 Waste materials, n.o.s.	103	108	113	112	112	122	129	137	4.0
799 Manufactures and miscellaneous, n.o.s.	102	111	108	110	105	111	118	122	3.5
Group VI. Forwarder traffic	103	113	114	112	112	115	124	130	1.0

¹ Only classes having more than approximately 1,000 cars in the sample are shown separately. The group indexes cover all classes in the group.

² These groupings of individual commodity classes are shown at the request of the Department of Agriculture. "Oil bearing crops" include commodity classes 037 to 047, 097 and 105; "Fresh fruits," classes 049 through 069; "Fresh vegetables," classes 077 through 089 (including 085 which is also shown separately).

Table 2. Indexes of average freight rates for territorial movement in total and by commodity group

Table 2 shows the indexes of average freight rates for intraterritorial and interterritorial movements in total and by major commodity groups for the period 1951 through 1958. The indexes show rate increases from 1950 through 1958 higher within official and western trunkline than within the other territories. The percentage changes from 1957 to 1958 and from 1950 to 1958 are as follows:

Intraterritorial—All commodities	Percentage change		
	1958 over 1957	1958 over 1950	
Official	3.4		23
Southern	-9		11
Western trunkline	4.2		25
Southwestern	1.7		18
Mountain-Pacific	2.6		19

The largest percentage increases in average interterritorial rates, all commodities, for the year 1958 over 1957, are shown for movements from Western Trunk Line to Mountain-Pacific (4.2 percent) Official to Southwestern (3.5 percent), Mountain-Pacific to Official (3.4 percent), and Official to Western Trunk Line, Official to Mountain-Pacific, and Southwestern to Western Trunk Line (all 3.3 percent). Percentage decreases in 1958 from 1957 are shown for rates on movements from Western Trunk Line to Official (0.8 percent) and Western Trunk Line to Southwestern (0.9 percent).

The following table summarizes the percentage changes in rates on interterritorial movements in 1958 over 1957 and from the base year 1950:

INTERTERRITORIAL MOVEMENTS—ALL COMMODITIES, PERCENTAGE CHANGE
1958 OVER 1957

From—	To—				
	Official	Southern	Western Trunk Line	Southwestern	Mountain-Pacific
Official.....		1.7	3.3	3.5	3.3
Southern.....	0			0	
Western Trunk Line.....	-.8			-.9	4.2
Southwestern.....	1.7	1.8	3.3		
Mountain-Pacific.....	3.4		2.5	2.6	

INTERTERRITORIAL MOVEMENTS—ALL COMMODITIES, PERCENTAGE CHANGE
1958 OVER 1950

Official.....		17.0	25.0	18.0	26.0
Southern.....	18.0			14.0	
Western Trunk Line.....	23.0			12.0	24.0
Southwestern.....	21.0	15.0	27.0		
Mountain-Pacific.....	21.0		24.0	20.0	

TABLE 2.—Indexes of average freight rates for territorial movement in total and by commodity group¹

[1950=100]

Item	Index								Approximate standard deviation
	1951	1952	1953	1954	1955	1956	1957	1958	
Official to Official:									
All commodities.....	103	110	111	109	107	112	119	123	0.5
I. Products of agriculture.....	102	109	112	112	111	115	123	126	1.0
II. Animals and products.....	104	111	113	113	114	117	125	128	.5
III. Products of mines.....	102	108	109	107	106	110	115	119	.5
IV. Products of forests.....	104	114	114	115	115	119	130	134	1.0
V. Manufactures and miscellaneous.....	103	111	113	109	107	112	123	127	.5
VI. Forwarder traffic.....	103	113	115	116	116	119	133	142	1.0
Official to Southern:									
All commodities.....	101	108	111	107	105	108	115	117	.5
V. Manufactures and miscellaneous.....	101	109	112	107	106	109	116	118	.5
Official to Western Trunk Line:									
All commodities.....	103	111	112	112	110	112	121	125	.5
V. Manufactures and miscellaneous.....	102	111	113	112	110	112	121	125	1.0
Official to Southwestern:									
All commodities.....	102	108	109	108	105	103	114	118	1.0
V. Manufactures and miscellaneous.....	102	109	109	109	105	103	114	117	1.0
Official to Mountain-Pacific:									
All commodities.....	101	111	113	111	111	115	122	126	2.0
V. Manufactures and miscellaneous.....	101	111	112	111	110	115	122	127	2.0

See footnote at end of table.

TABLE 2.—Indexes of average freight rates for territorial movement in total and by commodity group¹—Continued

[1950=100]

Item	Index								Approximate standard deviation
	1951	1952	1953	1954	1955	1956	1957	1958	
Southern to Official:									
All commodities.....	102	109	112	112	109	112	118	118	0.5
I. Products of agriculture.....	100	105	108	108	108	112	116	107	1.5
III. Products of mines.....	102	108	111	110	107	110	116	119	.5
IV. Products of forests.....	102	112	115	115	115	121	129	134	.5
V. Manufactures and miscellaneous.....	102	111	115	113	109	111	117	116	.5
Southern to Southern:									
All commodities.....	102	109	112	109	106	108	112	111	.5
I. Products of agriculture.....	101	107	112	111	109	108	105	104	1.5
III. Products of mines.....	101	107	109	107	104	106	110	108	.5
IV. Products of forests.....	104	112	116	114	113	116	121	119	1.0
V. Manufactures and miscellaneous.....	102	109	113	108	105	108	112	113	1.0
Southern to Southwestern:									
All commodities.....	101	109	112	109	107	108	114	114	1.5
Western Trunk Line to Official:									
All commodities.....	102	110	112	112	112	116	124	123	.5
II. Animals and products.....	102	111	113	113	112	117	124	120	1.0
V. Manufactures and miscellaneous.....	101	1094	111	111	110	114	123	127	1.5
Western Trunk Line to Western Trunk Line:									
All commodities.....	102	109	111	111	111	114	120	125	.5
I. Products of agriculture.....	103	109	112	113	113	117	124	127	.5
II. Animals and products.....	104	111	115	115	116	119	124	127	1.0
III. Products of mines.....	102	109	109	109	109	113	119	126	.5
IV. Products of forests.....	99	105	109	108	108	108	123	131	2.5
V. Manufactures and miscellaneous.....	101	109	112	111	110	113	118	120	.5
Western Trunk Line to Southwestern:									
All commodities.....	101	110	112	108	106	106	113	112	1.0
Western Trunk Line to Mountain-Pacific:									
All commodities.....	102	111	112	111	110	113	119	124	1.0
V. Manufactures and miscellaneous.....	102	112	113	113	110	115	121	125	1.0
Southwestern to Official:									
All commodities.....	101	106	108	107	106	112	119	121	1.0
V. Manufactures and miscellaneous.....	101	106	106	106	104	112	118	120	1.0
Southwestern to Southern:									
All commodities.....	100	106	109	107	105	109	113	115	1.0
Southwestern to Western Trunk Line:									
All commodities.....	101	110	112	111	111	114	123	127	.5
V. Manufactures and miscellaneous.....	101	109	112	111	111	114	123	127	1.0
Southwestern to Southwestern:									
All commodities.....	101	108	111	111	109	111	116	118	.5
I. Products of agriculture.....	102	110	115	114	108	107	109	112	1.0
III. Products of mines.....	102	107	110	112	111	113	118	121	1.0
IV. Products of forests.....	102	109	110	110	109	115	123	120	1.0
V. Manufactures and miscellaneous.....	100	107	109	109	109	111	116	118	.5
Mountain-Pacific to Official:									
All commodities.....	102	107	109	108	108	112	117	121	.5
I. Products of agriculture.....	101	105	106	105	105	107	112	114	.5
IV. Products of forests.....	102	108	110	110	110	114	120	124	1.0
Mountain-Pacific to Western Trunk Line:									
All commodities.....	102	109	112	111	110	114	121	124	.5
I. Products of agriculture.....	102	109	110	111	109	112	118	120	1.0
IV. Products of forests.....	102	109	112	113	113	117	124	128	1.0
Mountain-Pacific to Southwestern:									
All commodities.....	101	109	110	108	106	111	117	120	1.0
Mountain-Pacific to Mountain-Pacific:									
All commodities.....	100	107	109	110	108	111	116	119	.5
I. Products of agriculture.....	100	108	112	111	110	112	119	119	1.0
III. Products of mines.....	101	106	106	108	107	109	114	117	.5
IV. Products of forests.....	100	109	112	113	114	117	124	129	.5
V. Manufactures and miscellaneous.....	100	107	108	109	106	108	113	117	1.0

¹ Only movements having approximately 1,000 cars or more in the sample are shown. Territorial totals cover all shipments in that movement, regardless of the number of cars in the commodity group.

Table 3. *Indexes of average freight rates for interstate and intrastate rates by commodity group*

Table 3 indicates that average interstate and intrastate rates for all commodities combined experienced approximately the same year-to-year changes for the 5-year period 1951 through 1955. Slight differences are shown in 1952 and 1955 when the interstate rate index was 1 point higher than the intrastate rate index. For 1956 and particularly for both 1957 and 1958, the level of interstate rates is somewhat higher. The more marked increase in interstate rates is due mainly to the fact that general rate increases in some States became effective at a later date than increases on interstate traffic, and in some instances were not as large.

Between 1957 and 1958, all major commodity groups show increases with respect to both interstate and intrastate rates, except for interstate rates on animals and products which remained the same. The largest increases appear for products of mines in interstate rates, and animals and products in intrastate rates.

Table 3 also compares the degree of increase since 1950 in interstate rates with intrastate rates for each of the commodity groups. The 23-percent rise in interstate rates for manufactures and miscellaneous as compared with the 15-percent increase in intrastate rates on the same group is the largest spread. The interstate index also shows greater increase since 1950 for products of mines (19 percent versus 14 percent). The intrastate indexes are slightly higher for products of agriculture (120 versus 119) and for products of forests (128 versus 127). For 1957 the indexes for products of forests were identical. The intrastate index for animals and products rose 6 points in 1958 from 1957 while the interstate index remained unchanged. As a result, the increase in intrastate rates since 1950 for this group again exceeded that for interstate rates as it had in 1953, 1954, 1955, and 1956.

TABLE 3.—*Indexes of average freight rates for interstate and intrastate rates by commodity group*

[1950=100]

Item	Index								Approximate standard deviation
	1951	1952	1953	1954	1955	1956	1957	1958	
Interstate rates:									
All commodities.....	102	109	111	109	108	112	119	122	0.5
I. Products of agriculture.....	102	108	110	110	109	111	117	119	.5
II. Animals and products.....	102	110	113	112	112	116	122	122	.5
III. Products of mines.....	102	108	109	108	107	111	115	119	.5
IV. Products of forests.....	102	110	112	112	112	116	124	127	.5
V. Manufactures and miscellaneous.....	102	110	112	110	108	112	120	123	.5
Intrastate rates:									
All commodities.....	102	108	111	109	107	110	114	116	.5
I. Products of agriculture.....	102	110	113	115	113	115	118	120	1.0
II. Animals and products.....	101	108	114	116	117	120	119	125	1.5
III. Products of mines.....	102	107	108	107	106	108	112	114	.5
IV. Products of forests.....	102	111	116	116	115	119	124	128	1.0
V. Manufactures and miscellaneous.....	102	108	111	109	106	107	113	115	.5

Table 4. *Indexes of average freight rates by commodity groupings corresponding to Bureau of Labor Statistics classification for wholesale commodity price index¹*

Table 4 is designed to conform as closely as possible to the classification of commodities utilized in the construction of the wholesale commodity price index of the BLS, Department of Labor. The sharpest increases in the indexes for 1958 over 1957 are shown for machinery and motive products, 7 points (at 134); metals and metal products and furniture and household durables, 6 points each (at 126 and 133, respectively); and hides, skins, and leather products, 5 points (at 130). The index for the commodity grouping, tobacco manufactures and bottled beverages (at 112), declined by 1 point from the 1957 level.

¹ Prepared at the request of the Bureau of Labor Statistics which designated the commodity group classifications.

TABLE 4.—Indexes of average freight rates by commodity groupings corresponding to Bureau of Labor statistics classification for wholesale commodity price index¹

Item	Index								Approximate standard deviation
	1951	1952	1953	1954	1955	1956	1957	1958	
All commodities.....	102	109	111	109	108	112	118	121	0.5
Farm products.....	102	108	111	111	110	112	118	120	.5
Processed foods.....	101	107	110	109	108	111	115	115	.5
Textile products and apparel.....	100	109	113	111	108	109	115	116	1.0
Hides, skins, and leather products.....	100	111	113	112	112	116	125	130	1.5
Fuel, power, and lighting materials.....	101	107	109	106	106	109	113	114	.5
Chemicals and allied products.....	101	108	111	110	107	113	120	122	1.0
Rubber and rubber products.....	100	109	111	110	110	114	121	122	1.5
Lumber and wood products.....	102	110	112	112	112	116	123	127	.5
Pulp, paper, and allied products.....	103	111	113	111	108	110	118	120	.5
Metal and metal products.....	103	111	113	108	105	110	120	126	.5
Machinery and motive products.....	102	111	113	113	113	118	127	134	.5
Furniture and household durables.....	102	111	113	113	113	118	127	133	.5
Nonmetallic minerals—structural.....	103	110	112	111	109	111	119	121	.5
Tobacco manufactures and bottled beverages.....	102	108	111	110	105	107	113	112	1.0
Miscellaneous.....	102	111	112	112	110	115	122	125	2.0

¹ Prepared at request of Bureau of Labor Statistics which designated commodity group classifications.

GENERAL NOTES CONCERNING THE INDEX

The accuracy of these indexes is affected in part by sampling fluctuation and in part by changes in the consist of the traffic. The traffic categories used in the study have been selected in a manner so as to minimize the revenue effect of changes in the consist of traffic. However, certain conditions do exist which may affect individual indexes. For example, in commodity class 203, cattle and calves, there are movements of feeder cattle and fat cattle which have different rates. Consequently, a change in the proportion of these two types of cattle could affect the average revenue for the traffic categories within this class in such a way as not properly to reflect changes in rate. Similar shifts in proportions are possible in other classes, especially in the miscellaneous not otherwise specified classes. In general, however, these shifts are not serious.

Sometimes particular commodities are reclassified and shifted from one class to another by the Freight Traffic Statistics Committee.² One such case occurred in 1950 when two heavy loading commodities moving in substantial quantities (carbonate of potash and muriate of potash) were shifted from class 539, fertilizers, not otherwise specified, to class 527, chemicals, not otherwise specified. This shift made a substantial reduction in the average revenue of the chemicals, not otherwise specified class, which, of course, was reflected in the index. It was also sufficiently large to have an appreciable effect on the territorial indexes of southwestern to official traffic for the years prior to 1950. A change of this nature would also result in a temporary distortion of the index as computed under the present chain procedure, but there would be an automatic compensation in the index for the following year and the discrepancy would not affect succeeding indexes. This inherent ability of the chain index to automatically adjust for changes in consist is one of the reasons for adopting it for the computation of the rate indexes.

Theoretically, each index could have been calculated from a 100-percent sample of the shipments. However, most of the indexes developed from the 1 percent sample should not deviate from such indexes based upon all shipments by more than the associated standard deviation. Occasional deviations of twice or more than twice that amount, however, are possible. Consequently, approximate standard deviations² are included in the tables to give an indication

¹ Comprises representatives of the Association of American Railroads, the railroads, and this Bureau.

² These approximations are based upon two estimates made by different methods for different periods of time which yielded substantially similar results. In the first estimate, traffic categories were divided into 10 random subsamples, and, in the second estimate, the waybill cards were separated into 5 subsamples and 5 sets of traffic categories were prepared. In each estimate, indexes were computed for each subsample and the differences between these indexes provided a measure of the standard deviation.

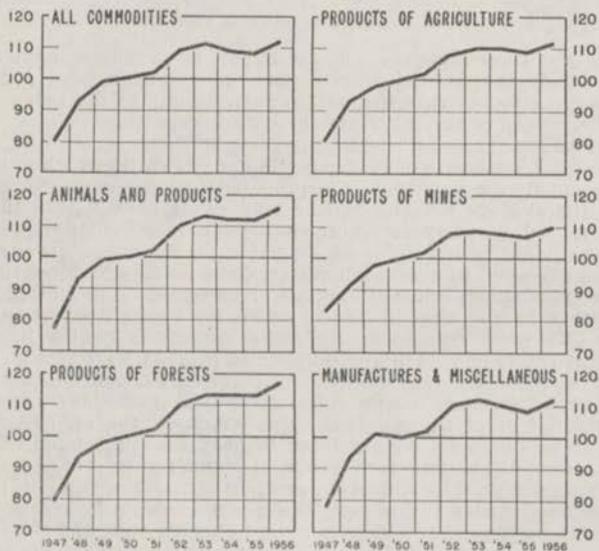
of the sampling stability of each index. In other words, the indexes shown here may be either greater or less than similar indexes computed from all of the traffic. The possible magnitude of these differences is indicated by the applicable standard deviation which should be considered when making comparisons between the various indexes.

For a description of the methods used in constructing the rate index see statement RI-1, 1948-56, March 1958.

INTERSTATE COMMERCE COMMISSION, Bureau of Transport Economics and Statistics

indexes of average Freight Rates on Railroad Carload Traffic 1948-1956

1950 = 100



Statement RI-1
1948-1956

March 1958
Washington, D. C.

This release, issued as information, has not been adopted by the Interstate Commerce Commission.

FOREWORD

This statement is the seventh in a series of annual indexes of average freight rates on railroad carload traffic. It includes information previously published for the years 1948-55 and adds results for the year 1956.

The report was prepared by R. T. Smith. Other members of the staff participated directly or indirectly.

E. R. JELSMAN, *Director.*

INDEXES OF AVERAGE FREIGHT RATES, 1948-56

COMMODITY GROUPS AND SELECTED COMMODITY CLASSES

A marked increase over the 2 previous years, reversing the downward trend started in 1954, is reflected in the 1956 index of average freight rates on total rail carload traffic. The all-commodities index for 1956 stands at 112, an increase of 4 points over the 1955 level. An average increase of 5.5 percent in general freight rates was granted in *Ex Parte 196*, effective March 7, 1956. This accounts, in the main, for the rise in the index during 1956. The major changes in group indexes, with increases of 4 points, occurred in "Animals and products" (116), "Products of forests" (117), and "Manufactures and miscellaneous" (112). Increases of 3 points took place in the indexes of the three remaining groups, with "Products of agriculture" rising to 112, "Products of mines" to 110 and "Forwarder traffic" to 115.

Sharp increases occurred in a number of commodity classes. The indexes for class 575, "Iron and steel: Billet, bloom, and ingot" and class 583, "Manufactured iron and steel" now stand at 111 and 104 respectively, an increase for each class of 7 points over 1955, and 19 and 8 points respectively, above the 1948 level. A 6-point increase in the indexes for classes 401, "Logs, butts, and bolts" (at 116) and 779, "Metal containers" (at 122), brings them to 23 and 31 points respectively above the 1948 level. Other larger-than-average increases include a 5-point rise for the following classes with accompanying 1956 indexes:

No. 003, "Corn" (at 116), No. 309, "Iron ore" (at 115), No. 323, "Clay and bentonite" (at 119), No. 325, "Sand, industrial" (at 113), No. 613, "Automobiles, passenger" (at 108), No. 759, "Sugar" (at 114) and No. 789, "Scrap iron and scrap steel" (at 113). Virtually the only significant decrease in the indexes during the year occurred for class 033, "Cotton in bales," with a 7-point reduction to 108, the lowest level since 1951. The sharp decline in this index is due to a marked reduction made in the rates in order to meet competition.¹

Table 1 shows the indexes for average freight rates for commodity groups and selected commodity classes with 1950 as 100. An estimate of the standard deviation for each index is also given and the table covers the calendar years 1948 through 1956. The indexes for all commodities combined rose during this period from 93 in 1948 to 111 in 1953 and then declined to 108 in 1955, but increased to 112 in 1956. Similar trends are noted in each of the major commodity groups although, of course, they show moderate differences from the overall indexes. The upward trend produced by general rate increases has been modified in many instances by individual reductions. This modification of the trend is clearly evident in the results for 1954 and 1955, but also appeared in previous years as, for example, in the group index for "Manufactures and miscellaneous" which showed a reduction from 101 in 1949 to 100 in 1950.

Data for selected commodity classes for 1947 may be found in prior years' issues of these indexes. In 1947 the index for all commodities was 80 with "Products of agriculture" and "Forwarder traffic" also at 80. "Products of mines" at 83 exceeded the overall index, but "Animals and products" (77), "Products of forests" (79) and "Manufactures and miscellaneous" (78) were below the index for all commodities. Examples of commodities for which the indexes for 1956 were greater than those for 1947 by more than 50 percent were as follows: No. 003, "Corn," 55 percent; No. 331, "Fluxing stone and raw dolomite," 56 percent; No. 573, "Pig iron," 63 percent; No. 577, "Iron and steel; bar rod and slab," 51 percent; No. 707, "Refrigerators, freezing apparatus and parts," 68 percent; No. 779, "Containers, metal," 65 percent; and No. 789, "Scrap iron and scrap steel," 53 percent.

¹ I. & S. Docket No. 6588, "Cotton-Southwest to Southern Territory."

TERRITORIAL MOVEMENT BY COMMODITY GROUPS

The territorial pattern of changes reflects a tendency for greater increases in the East although there was a 3-point increase for both western trunkline and mountain-Pacific. The 5-point increase in the index for official reflects a rise of 5 points in the "Manufactures and miscellaneous" index from 107 to 112. The index for official now equals that for all commodities while that for western trunkline is 2 points greater at 114 and the indexes for southwestern and mountain-Pacific are less at 111 each and for southern is less at 108. Table 2 shows, in detail, differences in the 1956 territorial indexes. Increases are shown in 1956 for all commodities for southwestern to official (at 112) and mountain-Pacific to southwestern (at 111), with increments of 6 and 5 points, respectively, in the indexes.

INTER- AND INTRASTATE RATES BY COMMODITY GROUPS

Table 3 indicates a small but consistent difference between interstate and intrastate average rate increases since 1948. The indexes for interstate rates during 1956 have increased more than those for intrastate rates for all commodity groups except "Products of agriculture" and "Products of forests" where the increments were 2 and 4 points, respectively, for both classes of rates.

The overall indexes for the two classes of traffic have moved in similar fashion since 1948. There was a sharper increase from 1947 to 1948 in the interstate rates, from 79 to 93 as against 82 to 93 for intrastate rates, which was due principally to the fact that general rate increases in some States were authorized at a later date than they became effective for interstate traffic and the increases granted in many cases were not as great.² The 1956 indexes also indicate differences in changes since 1950 in the major commodity groups. The greatest is in "Manufactures and miscellaneous" where the interstate index for 1956 is 112 as against the intrastate index of 107. The interstate index is also higher for "Products of mines" but lower for "Products of agriculture," "Animals and products," and "Products of forests."

COMMODITY GROUPINGS CORRESPONDING TO WHOLESALE COMMODITY PRICE INDEX

Table 4 shows the indexes of average freight rates by a commodity grouping which has been designed to fit as nearly as possible the classification used by the Bureau of Labor Statistics for its wholesale commodity price index. The table was prepared at the request of the Bureau of Labor Statistics which designated the commodity group classifications. Highest increases in the indexes for 1956 were 6 points for "Chemicals and allied products" (at 113) and 5 points each for "Metals and metal products" (at 110, "Machinery and motive products" (at 118) and "Furniture and household durables" (at 118).

GENERAL RATE INCREASES

The first postwar general rate increase of about 6.5 percent became effective on July 1, 1946, but the indexes cannot be extended to cover this period by the present method because the basic waybill data was not collected for the year 1946. An estimate has been made, however, of approximate indexes for the rate level as of June 30, 1946, which may be of interest for comparative purposes. The overall index on that date (with 1950=100) was 67, "Products of agriculture," 69; "Animals and products," 64; "Products of mines," 73; "Products of forests," 66; and "Manufactures and miscellaneous," 64.

There were a number of general rate increases during the years 1947 through 1952. The increase on January 1, 1947, was estimated to average approximately 10.4 percent and, subsequently, increases followed: October 13, 1947, 8.9 percent; January 5, 1948, 7.6 percent; May 6, 1948, 3.6 percent; August 21, 1948, 1 percent;

² See this Bureau's statement No. 5237, "Indexes of Average Comparative Intrastate Freight Rates, 1950."

January 11, 1949, 5.2 percent; and on September 1, 1949, 3.7 percent. There were no general increases in 1950 but additional ones were granted on April 4, 1951, 2.4 percent; August 28, 1951, 4 percent; May 2, 1952, 6.8 percent; and on March 7, 1956, 5.5 percent. It will be noted that the indexes indicate a smaller effective change in average rates than the arithmetical accumulation of these authorized increases due in part to the fact that some of the increases were not put into effect immediately upon authorization, and also to individual reductions following the general increases.

GENERAL NOTES CONCERNING THE INDEX

The accuracy of these indexes is affected in part by sampling fluctuation and in part by changes in the consist of the traffic. As explained below, the traffic categories used in the study have been selected in a manner so as to minimize the revenue effect of changes in the consist of traffic. However, certain conditions do exist which may affect individual indexes. For example, in commodity class 203, "Cattle and calves," there are movements of feeder cattle and fat cattle which have different rates. Consequently, a change in the proportion of these two types of cattle could affect the average revenue for the traffic categories within this class in such a way as not properly to reflect changes in rates. Similar shifts in proportions are possible in other classes, especially in the miscellaneous n.o.s. classes. In general, however, these shifts are not serious.

Sometimes particular commodities are reclassified and shifted from one class to another by the Freight Traffic Statistics Committee.³ One such case occurred in 1950 when two heavy loading commodities moving in substantial quantities (carbonate of potash and muriate of potash) were shifted from class 539, "Fertilizers, n.o.s.," to class 527, "Chemicals, n.o.s." This shift made a substantial reduction in the average revenue of the "Chemicals, n.o.s." class, which, of course, was reflected in the index. It was also sufficiently large to have an appreciable effect on the territorial indexes of southwestern to official traffic for the years prior to 1950. A change of this nature would also result in a temporary distortion of the index as computed under the present chain procedure, but there would be an automatic compensation in the index for the following year and the discrepancy would not affect succeeding indexes. This inherent ability of the chain index to automatically adjust for changes in consist is one of the reasons for adopting it for the computation of the rate indexes.

Theoretically, each index could have been calculated from a 100 percent sample of the shipments. However, most of the indexes developed from the 1 percent sample should not deviate from such indexes based upon all shipments by more than the associated standard deviation. Occasional deviations of twice or more than twice that amount, however, are possible. Consequently, approximate standard deviations⁴ are included in the tables to give an indication of the sampling stability of each index. In other words, the indexes shown here may be either greater or less than similar indexes computed from all of the traffic. The possible magnitude of these differences is indicated by the applicable standard deviation which should be considered when making comparisons between the various indexes.

³ Prior to Dec. 1, 1949, the Freight Commodity Classification Committee.

⁴ These approximations are based upon two estimates made by different methods for different periods of time which yielded substantially similar results. In the first estimate, traffic categories were divided into 10 random subsamples, and, in the second estimate, the waybill cards were separated into 5 subsamples and 5 sets of traffic categories were prepared. In each estimate, indexes were computed for each subsample and the differences between these indexes provided a measure of the standard deviation.

TABLE 1.—*Indexes of average freight rates for commodity groups and selected commodity classes*¹

[1950=100]

Item	Index								Approximate standard deviation
	1948	1949	1951	1952	1953	1954	1955	1956	
All commodities.....	93	99	102	109	111	109	108	112	0.5
Group I. Products of agriculture.....	93	98	102	108	110	110	109	112	.5
Class 001 Wheat.....	93	95	101	108	113	113	112	115	1.0
003 Corn.....	94	95	102	108	109	112	111	116	1.0
033 Cotton in bales.....	92	98	102	113	119	116	115	108	1.0
Oil bearing crops ²	91	99	103	112	113	114	113	116	4.0
Fresh fruits ²	95	99	101	106	107	107	106	109	.5
Fresh vegetables ²	95	99	101	106	108	107	108	110	.5
085 Potatoes, other than sweet.....	94	99	101	108	110	109	110	112	1.0
101 Sugar beets.....	96	103	105	110	122	124	125	126	3.0
199 Products of agriculture, n.o.s.....	94	105	99	112	114	114	109	117	3.0
Group II. Animals and products.....	93	99	102	110	113	112	112	116	.5
Class 203 Cattle and calves, s.d.....	94	98	103	112	115	114	114	118	1.0
215 Meats, fresh, n.o.s.....	90	98	103	111	114	114	113	118	1.0
Group III. Products of mines.....	91	98	102	108	109	108	107	110	.5
Class 301 Anthracite coal, n.o.s.....	90	99	101	107	109	109	108	109	.5
305 Bituminous coal.....	89	98	101	107	108	106	105	109	.5
307 Coke.....	91	97	102	108	109	107	107	110	1.5
309 Iron ore.....	95	99	103	110	110	111	110	115	.5
323 Clay and bentonite.....	95	98	103	112	115	114	114	119	1.0
325 Sand, industrial.....	91	98	105	114	113	109	108	113	1.0
327 Gravel and sand, n.o.s.....	98	102	103	108	110	108	109	110	1.0
329 Stone and rock: broken, ground and crushed.....	93	100	103	108	110	110	108	111	1.0
331 Fluxing stone and raw dolomite.....	88	98	104	110	111	112	113	117	1.0
337 Petroleum, crude.....	96	99	101	109	107	102	100	102	1.5
339 Asphalt.....	94	100	101	110	111	111	109	112	1.0
341 Salt.....	93	98	102	108	109	107	108	109	1.0
343 Phosphate rock.....	95	100	102	109	112	113	105	108	1.5
309 Products of mines, n.o.s.....	98	100	101	110	110	109	110	114	2.5
Group IV. Products of forests.....	93	98	102	110	113	113	113	117	.5
Class 401 Logs, butts, and bolts.....	93	99	102	108	114	110	110	116	1.5
403 Posts, poles, and piling, wooden.....	92	97	101	111	110	113	114	118	1.5
409 Pulpwood.....	98	100	104	111	113	111	109	112	.5
411 Lumber, shingles, and lath.....	92	98	102	110	112	113	113	117	.5
499 Products of forests, n.o.s.....	95	100	103	110	116	114	117	121	2.5

See footnote at end of table.

TABLE 1.—Indexes of average freight rates for commodity groups and selected commodity classes²—Continued

[1950=100]

Item	Index								Approximate standard deviation
	1948	1949	1951	1952	1953	1954	1955	1956	
Group V. Manufactures and miscellaneous.....	94	101	102	110	112	110	108	112	0.5
Class 501 Gasoline.....	99	104	99	104	105	104	100	102	.5
503 Fuel, road, and petroleum residual oils, n.o.s.....	98	104	99	104	106	104	103	104	1.0
505 Lubricating oils and greases.....	100	108	100	107	111	111	110	114	1.0
507 Petroleum products, refined, n.o.s.....	91	100	101	109	112	111	113	116	.5
527 Chemicals, n.o.s.....	105	114	101	105	108	106	104	118	1.0
533 Sodium (soda) products.....	92	105	99	107	108	106	104	107	1.0
539 Fertilizers, n.o.s.....	93	98	102	110	114	113	111	112	1.0
573 Iron, pig.....	90	96	104	113	114	113	114	117	1.5
575 Iron and steel: Billet, bloom, and ingot.....	92	97	103	112	113	108	104	111	2.0
577 Iron and steel: Bar, rod, and slab.....	92	99	101	108	110	107	105	109	2.0
583 Manufactured iron and steel.....	96	103	103	111	113	102	97	104	1.0
587 Iron and steel pipe and fittings, n.o.s.....	94	100	103	111	114	108	101	100	1.0
595 Machinery and machines, n.o.s.....	93	97	103	112	116	115	116	121	1.0
613 Automobiles, passenger.....	90	98	102	103	103	105	103	108	1.0
623 Vehicle parts, n.o.s.....	92	97	103	113	115	114	113	119	1.0
633 Cement: Natural and portland.....	92	98	103	110	112	110	104	102	.5
645 Lime, n.o.s.....	90	97	102	110	113	113	111	116	1.0
655 Scrap paper and rags.....	92	99	104	113	115	114	116	122	1.0
659 Printing paper, n.o.s.....	90	99	103	110	113	112	109	111	1.0
669 Paperboard, fibreboard and pulpboard.....	94	100	103	111	114	111	104	104	1.0
671 Wallboard.....	92	97	102	111	114	110	108	110	1.0
697 Glass bottles, jars, and packing glasses, n.o.s.....	94	103	101	108	109	109	109	115	1.0
707 Refrigerators, freezing apparatus, and parts.....	89	97	103	112	114	115	115	119	.5
715 Furniture, n.o.s.....	90	99	102	110	112	113	114	118	1.0
749 Liquors, malt.....	98	103	102	110	113	111	103	104	1.0
759 Sugar.....	95	99	102	107	110	110	109	114	1.5
763 Food products, n.o.s., in cans and packages, not frozen.....	98	104	99	105	107	106	105	107	1.0
773 Feed, animal and poultry, n.o.s.....	95	99	103	112	115	116	118	124	1.5
779 Containers, metal.....	91	98	103	112	115	114	116	122	.5
783 Containers, fibreboard and paperboard, k.d.....	91	99	103	112	114	117	115	119	1.5
789 Scrap iron and scrap steel.....	90	97	105	112	115	111	108	113	.5
793 Furnace slag.....	96	104	102	107	107	107	105	109	1.0
797 Waste materials, n.o.s.....	96	105	103	108	113	112	112	122	4.0
799 Manufactures and miscellaneous, n.o.s.....	100	103	102	111	108	110	105	111	3.5
Group VI. Forwarder traffic.....	101	106	103	113	114	112	112	115	1.0

¹ Only classes having more than approximately 1,000 cars in the sample are shown separately. The group indexes cover all classes in the group.

² These groupings of individual commodity classes are shown at the request of the Department of Agriculture. "Oil-bearing crops" include commodity classes 037 to 047, 097 and 105; "Fresh fruits," classes 049 through 069; "Fresh vegetables," classes 077 through 089 (including 085 which is also shown separately).

TABLE 2.—*Indexes of average freight rates for territorial movement in total and by commodity group*¹

[1950=100]

Item	Index								Approximate standard deviation
	1948	1949	1951	1952	1953	1954	1955	1956	
Official to official:									
All commodities.....	91	99	103	110	111	109	107	112	0.5
I. Products of agriculture.....	88	97	102	109	112	112	111	115	1.0
II. Animals and products.....	91	99	104	111	113	113	114	117	.5
III. Product of mines.....	90	98	102	108	109	107	106	110	.5
IV. Products of forest.....	91	99	104	114	114	115	115	119	1.0
V. Manufactures and miscellaneous.....	92	100	103	111	113	109	107	112	.5
VI. Forwarder.....	106	110	103	113	115	116	116	119	1.0
Official to southern:									
All commodities.....	92	100	101	108	111	107	105	108	.5
V. Manufactures and miscellaneous.....	92	100	101	109	112	107	106	109	.5
Official to western trunk line:									
All commodities.....	92	99	103	111	112	112	110	112	.5
V. Manufactures and miscellaneous.....	92	99	102	111	113	112	110	112	1.0
Official to southwestern:									
All commodities.....	94	97	102	108	109	108	105	103	1.0
V. Manufactures and miscellaneous.....	94	97	102	109	109	109	105	103	1.0
Official to mountain-Pacific:									
All commodities.....	94	99	101	111	113	111	111	115	2.0
V. Manufactures and miscellaneous.....	94	99	101	111	112	111	110	115	2.0
Southern to official:									
All commodities.....	91	98	102	109	112	112	109	112	.5
I. Products of agriculture.....	94	99	100	105	108	108	108	112	1.5
III. Products of mines.....	90	97	102	108	111	110	107	110	.5
IV. Products of forests.....	90	97	102	112	115	115	115	121	.5
V. Manufactures and miscellaneous.....	92	98	102	111	115	113	109	111	.5
Southern to southern:									
All commodities.....	95	101	102	109	112	109	106	108	.5
I. Products of agriculture.....	96	101	101	107	112	111	109	108	1.5
III. Products of mines.....	94	100	101	107	109	107	014	106	.5
IV. Products of forests.....	94	98	104	112	116	114	113	116	1.0
V. Manufactures and miscellaneous.....	97	104	102	109	113	108	105	108	1.0
Southern to southwestern:									
All commodities.....	91	99	101	109	112	109	107	108	1.5
Western trunkline to official:									
All commodities.....	91	98	102	110	112	112	112	116	.5
II. Animals and products.....	91	98	102	111	113	113	112	117	1.0
V. Manufactures and miscellaneous.....	93	100	101	109	111	111	110	114	1.5
Western trunkline to western trunkline:									
All commodities.....	95	99	102	109	111	111	111	114	.5
I. Products of agriculture.....	92	96	103	109	112	113	113	117	.5
II. Animals and products.....	94	98	104	111	115	115	116	119	1.0
III. Products of mines.....	96	99	102	109	109	109	109	113	.5
IV. Products of forests.....	93	98	99	105	109	108	108	108	2.5
V. Manufactures and miscellaneous.....	96	100	101	109	112	111	110	113	.5
Western trunkline to southwestern:									
All commodities.....	96	100	101	110	112	108	106	106	1.0
Western trunkline to mountain-Pacific:									
All commodities.....	95	99	102	111	112	111	110	113	1.0
V. Manufactures and miscellaneous.....	94	99	102	112	113	113	110	115	1.0
Southwestern to official:									
All commodities.....	102	109	101	106	108	107	106	112	1.0
V. Manufactures and miscellaneous.....	105	113	101	106	106	106	104	112	1.0
Southwestern to southern:									
All commodities.....	92	101	100	106	109	107	105	109	1.0
Southwestern to western trunkline:									
All commodities.....	97	103	101	110	112	111	111	114	.5
V. Manufactures and miscellaneous.....	98	104	101	109	112	111	111	114	1.0
Southwestern to southwestern:									
All commodities.....	97	100	101	108	111	111	109	111	.5
I. Products of agriculture.....	99	95	102	110	115	114	108	107	1.0
III. Products of mines.....	93	99	102	107	110	112	111	113	1.0
IV. Products of forests.....	93	97	102	109	110	110	109	115	1.0
V. Manufactures and miscellaneous.....	98	102	100	107	109	109	109	111	.5

See footnote at end of table.

TABLE 2.—*Indexes of average freight rates for territorial movement in total and by commodity group*¹—Continued

[1950=100]

Item	Index								Approximate standard deviation
	1948	1949	1951	1952	1953	1954	1955	1956	
Mountain-Pacific to official:									
All commodities.....	95	99	102	107	109	108	108	112	0.5
I. Products of agriculture.....	96	99	101	105	106	105	105	107	.3
IV. Products of forests.....	94	99	102	108	110	110	110	114	1.0
Mountain-Pacific to western trunkline:									
All commodities.....	95	99	102	109	112	111	110	114	.5
I. Products of agriculture.....	94	98	102	109	110	111	109	112	1.0
IV. Products of forests.....	93	98	102	109	112	113	113	117	1.0
Mountain-Pacific to southwestern:									
All commodities.....	95	99	101	109	110	108	106	111	1.0
Mountain-Pacific to mountain-Pacific:									
All commodities.....	96	99	100	107	109	110	108	111	.5
I. Products of agriculture.....	93	98	100	108	112	111	110	112	1.0
III. Products of mines.....	96	99	101	106	106	108	107	109	.5
IV. Products of forests.....	93	98	100	109	112	113	114	117	.5
V. Manufactures and miscellaneous.....	98	101	100	107	108	109	106	108	1.0

¹ Only movements having approximately 1,000 cars or more in the sample are shown. Territorial totals cover all shipments in that movement.

TABLE 3.—*Indexes of average freight rates for inter- and intrastate rates by commodity group*

[1950=100]

INTERSTATE RATES

Item	Index								Approximate standard deviation
	1948	1949	1951	1952	1953	1954	1955	1956	
All commodities.....	93	99	102	109	111	109	108	112	0.5
I. Products of agriculture.....	93	98	102	108	110	110	109	111	.5
II. Animals and products.....	93	99	102	110	113	112	112	116	.5
III. Products of mines.....	91	98	102	108	109	108	107	111	.5
IV. Products of forests.....	92	98	102	110	112	112	112	116	.5
V. Manufactures and miscellaneous.....	94	101	102	110	112	110	108	112	.5

INTRASTATE RATES

All commodities.....	93	99	102	108	111	109	107	110	0.5
I. Products of agriculture.....	92	97	102	110	113	115	113	115	1.0
II. Animals and products.....	96	98	101	108	114	116	117	120	1.5
III. Products of mines.....	93	99	102	107	108	107	106	108	.5
IV. Products of forests.....	95	98	102	111	116	116	115	119	1.0
V. Manufactures and miscellaneous.....	95	100	102	108	111	109	106	107	.5

TABLE 4.—*Indexes of average freight rates by commodity groupings corresponding to Bureau of Labor statistics classification for wholesale commodity price index*¹

[1950=100]

Item	Index								Approximate standard deviation
	1948	1949	1951	1952	1953	1954	1955	1956	
All commodities.....	93	99	102	109	111	109	108	112	.5
Farm products.....	94	99	102	108	111	111	110	112	.5
Processed foods.....	93	100	101	107	110	109	108	111	.5
Textile products and apparel.....	95	104	100	109	113	111	108	109	1.0
Hides, skins, and leather products.....	94	99	100	111	113	112	112	116	1.5
Fuel, power, and lighting materials.....	91	99	101	107	109	106	106	109	.5
Chemicals and allied products.....	96	104	101	108	111	110	107	113	1.0
Rubber and rubber products.....	92	97	100	109	111	110	110	114	1.5
Lumber and wood products.....	93	98	102	110	112	112	112	116	.5
Pulp, paper, and allied products.....	93	100	102	111	113	111	108	110	.5
Metals and metal products.....	94	100	103	111	113	108	105	110	.5
Machinery and motive products.....	92	98	102	111	113	113	113	118	.5
Furniture and household durables.....	91	100	102	111	113	113	113	118	.5
Nonmetallic minerals—structural.....	94	99	103	110	112	111	109	111	.5
Tobacco manufactures and bottled beverages.....	97	102	102	108	111	110	105	107	1.0
Miscellaneous.....	96	102	102	111	112	112	110	115	2.0

¹ Prepared at the request of the Bureau of Labor Statistics which designated the commodity group classifications.

METHOD OF CONSTRUCTING THE RATE INDEX

The phrase "average freight rate" as used in connection with these indexes refers to the average price per hundredweight charged by the railroads for carload shipments. To simplify handling, these shipments have been grouped by "traffic categories" determined by the commodity class, short-line length of haul (mileage block), type of rate, and territorial movement.¹ The sample shipments for each year fall into about 30,000 of these traffic categories. The Commission in its waybill tabulations has published statements showing for the years 1947 through 1956 the number of carloads, tons, revenue, and average revenue per hundred pounds, for the traffic included in its 1 percent carload waybill sample, distributed according to these categories.² These statements provide the basic data from which the indexes are computed.

The indexes of average freight rates for the years 1947 through 1950 are ratios of weighted averages. The unit is the "traffic category" defined above and the tonnages used as weights in constructing the averages are those which moved in each of these categories in the base year 1950. All of the traffic categories in each of the years for which there was a corresponding category in 1950 were used in constructing the indexes. Such categories included about

¹ Shipments are classified according to—

(a) The 261 carload commodity classes listed in appendix I of the Commission's order of Sept. 24, 1946, *In the Matter of Freight Commodity Statistics, Steam Roads*.

(b) The territorial movements within and between the territories: (1) Official; (2) southern; (3) western trunk line; (4) southwestern; (5) mountain-Pacific.

(c) (1) Intrastate or (2) interstate rates. Interstate rates are further classified according to (1) classification ratings; (2) commodity rates; and (3) exception to the classification ratings.

(d) Short-line lengths of haul in 25 mileage blocks.

² Mileage block distribution of traffic and revenue.

95 percent of the total tonnage in each of the years. The elimination of the unmatched traffic categories as between 1950 and each of the comparing years has little or no effect on the computed indexes.

From—	To—	From—	To—	From—	To—	From—	To—	From—	To—
1.....	24	150	199	400	449	800	899	1,600	1,799
25.....	49	200	249	450	499	900	999	1,800	1,999
50.....	74	250	299	500	599	1,000	1,199	2,000	2,499
75.....	99	300	349	600	699	1,200	1,399	2,500	2,999
100.....	149	350	399	700	799	1,400	1,599	3,000	Over

	Statement numbers						
	1947	1948	1949	1950	1951	1952	1953-56
Products of agriculture.....	4922	4942	5039	5136	5248	5343	MB-1
Animals and products.....	4924	4947	5040	5137	5249	5344	MB-2
Products of mines.....	4925	504	5043	5138	5250	5345	MB-3
Products of forests.....	4926	503	5044	5139	5251	5346	MB-4
Manufactures and miscellaneous.....	4934	5010	5045	5132	5246	5347	MB-5
	501	5014	5047	5133			
	502	5016	5048	5135			

Computations were made for each of the indexes for the years 1947 and 1948. The traffic categories for the base and comparing years were matched, the base year tons converted to hundredweight, and the comparing year average revenue per hundredweight applied to determine the comparing year constructive revenue for the category. The base period revenue and the corresponding comparing year's constructive revenue for each of the categories included in the group for which an index was to be calculated were then aggregated and the ratio determined. An improved procedure was used in developing the indexes for 1949 in that carload traffic moving on less-carload or any-quantity rates, or which was rebilled, or was moved on transit balances, was excluded from each of the traffic categories in 1949 and 1950 before the index computations were made. Similar exclusions have been made from the 1951 through 1955 traffic. A change in computation procedure was also made effective starting with the indexes for 1951 which are linked to the old series in 1950.

The indexes for 1951 and 1952 were recomputed by the "chain" method and those for subsequent years added by the same method. This procedure consists essentially of calculating the percentage change in average rates for adjacent years and then chaining the results to the previously calculated index to arrive at the index for the current year. An example will make this clear, using bituminous coal shipments at commodity rates in official territory.

The first step is to calculate the constructive revenues for each mileage block category by applying the revenue per ton for that category for each pair of adjacent years to the average tonnage shipped in those years.

For example, in the first mileage block of the text table on page 13 the average tonnage for 1950 and 1951 was 2,380 and the revenue per ton was \$0.89 for 1950 and \$1.05 for 1951. Applying these rates to the common tonnage figure yields a constructive revenue of \$2,118 for 1950 and \$2,499 for 1951. Similar computations were performed for the rest of the mileage block categories for the years 1950-51, and also for the paired years 1951-52. The next step was to add

these constructive revenues, which in the example total \$6,472,886 and \$6,605,518 for 1950-51, and \$6,522,893 and \$6,896,857 for 1951-52. These show that the average change from 1950 to 1951 was 2 percent and from 1951 to 1952 it was 5.7 percent.

The next step is to "chain" these percentage increases to get the index series. Since 1950 is the base it set at 100 and the indicated ratio of 1951 to 1950 of 102 percent gives directly an index of 102 for 1951. The 1952 index is secured by using the previously calculated 1951 index and the calculated percentage change from 1951 to 1952. The 1952 index is, therefore, $102 \times 1.057 = 107.814$, or 108 after rounding. Similar computations would produce indexes for 1953 and succeeding years.

The change in procedure resulted in only minor corrections to the results obtained by the old method for the years 1951 and 1952. Most of these were of only 1 percentage point and the largest was a four point reduction in class 797, waste materials, n.o.s., from 112 to 108 for the year 1952. There was a three point reduction in class 527, chemicals, n.o.s., from 104 to 101 for the year 1951 and a scattering of two point changes.

*Bituminous coal at commodity rates in official territory*¹

Mile block starting with—	Average tons ²	Revenue per ton		Constructive revenue		Average tons ²	Revenue per ton		Constructive revenue	
		1950	1951	1950	1951		1951	1952	1951	1952
1.....	2,380	\$0.89	\$1.05	\$2,118	\$2,499	2,732	\$1.05	\$0.78	\$2,869	\$2,131
25.....	18,666	1.32	1.31	24,639	24,452	23,385	1.31	1.36	30,634	31,804
50.....	20,657	1.46	1.51	30,159	31,192	18,974	1.51	1.57	28,651	29,789
75.....	82,787	1.41	1.43	116,730	118,385	77,029	1.43	1.50	110,151	115,544
100.....	101,415	2.18	2.27	221,085	230,212	89,383	2.27	2.41	202,899	215,413
150.....	111,773	2.55	2.60	285,021	290,610	113,644	2.60	2.77	295,474	314,794
200.....	166,260	2.91	3.05	483,817	507,093	145,721	3.05	3.25	444,449	473,593
250.....	189,778	3.22	3.32	611,085	630,063	185,705	3.32	3.54	616,541	657,396
300.....	249,224	3.28	3.40	817,455	847,362	225,318	3.40	3.62	766,081	815,651
350.....	403,966	3.45	3.57	1,393,683	1,442,159	426,067	3.57	3.76	1,521,059	1,602,012
400.....	275,856	3.64	3.67	1,004,116	1,012,392	280,586	3.67	3.87	1,029,751	1,085,808
450.....	122,006	4.11	4.02	501,445	490,464	132,422	4.02	4.23	532,336	590,145
500.....	188,875	4.36	4.33	823,495	817,829	184,674	4.33	4.57	799,638	843,900
600.....	23,040	4.89	5.01	112,666	115,430	20,847	5.01	5.23	104,443	109,030
700.....	6,125	5.26	5.53	32,218	33,871	4,779	5.53	5.74	26,428	27,431
800.....	1,953	5.75	4.89	11,230	9,550	1,719	4.89	5.33	8,406	9,162
900.....	319	6.03	6.13	1,924	1,955	503	6.13	6.23	3,083	3,134
Total.....	1,965,080			6,472,886	6,605,518	1,933,488			6,522,893	6,896,857

¹ Basic data from statements Nos. 5138, 5250, and 5345.

² Total tons for 1950 and 1951 divided by 2.

³ Total tons for 1951 and 1952 divided by 2.

As previously stated, factors other than changes in freight rates might affect the average revenue per hundredweight for a traffic category. The average revenue effect of such differences, however, must necessarily be small as compared to the effect of rate changes if the resulting indexes are to provide a satisfactory measure of changes in average rates. Careful study indicates that this requirement is substantially satisfied in the method used here. The traffic categories chosen as units for comparison in this study were initially established to be as nearly homogeneous with respect to rate characteristics as is practicable. The mileage blocks are shorter where changes in the rate progression are most rapid, the various territorial movements are kept separate, as are movements on interstate and intrastate rates, and there is further classification by commodity class and type of rate. Consequently, the area of fluctuation in average revenue from causes other than changes in the rate is relatively small in each of such traffic categories.

Under certain conditions, however, changes in the consist of the traffic within traffic categories can result in comparative revenues which do not so exactly reflect the actual changes in average rates. Such conditions occur most commonly in the commodity classes which are composed of many miscellaneous items, such as the various N.O.S. classes. There are also cases where specific commodity items have been shifted from one class to another during the years

involved through the action of the Freight Traffic Statistics Committee⁵ consisting of representatives of the Association of American Railroads, the railroads, and this Bureau. It is reasonable to expect that where haphazard fluctuations about the average do occur, they are likely to be as often above the average in one category as below the average in another, so that there is a tendency for these errors to compensate rather than to accumulate. The net effect is that the changes in the average revenues noted will usually reflect quite closely the actual changes in the average rates. However, in cases where whole commodities have been shifted from one class to another the resulting categories are no longer strictly comparable. This lack of comparability might affect the index temporarily but an automatic adjustment will correct it in succeeding years.

MAY 1, 1961.

Senator E. L. BARTLETT,
Chairman, Merchant Marine and Fisheries Subcommittee, Senate Committee on Interstate and Foreign Commerce:

At the hearing conducted by your subcommittee on March 6, 1961, relating to the shipping problems of the noncontiguous areas of the United States, you requested that I submit for the record certain information as a supplement to the testimony which I presented in person. You asked for the following: (1) the present cost of living differential for Federal employees in Hawaii; (2) the present volume of barge operations between Hawaii and the mainland United States; (3) a list of the ocean freight rate increases in the Hawaii-mainland trade from World War II to the present; and (4) a summary of the effect of ocean freight rates on the Hawaiian pineapple industry.

I am hopeful that the following may serve as a response to your requests:

1. Cost-of-living differential

The cost-of-living differential now paid to classified employees of the Federal Government living in Hawaii is 17.5 percent.

2. Barge operations: Hawaii-mainland

I believe that the volume of barge operations between Hawaii and the mainland has not been a major factor, both in absolute terms and when considered in relation to the volume of conventional shipping in this trade. Although we have endeavored to verify this statistically with the Maritime Administration, the Census Bureau, the Corps of Engineers (Department of the Army), and our own board of harbor commissioners, unfortunately all have been unable to furnish us with up-to-date statistics. However, we do know that in 1958, there was a total absence of any dry-cargo movement on non-self-propelled vessels in the Hawaiian trade—other than between and among the component islands of the Hawaiian chain (cf. "Waterborne Commerce of the United States, Calendar Year 1958," Department of the Army, Corps of Engineers, pt. 4, p. 201).

3. Post-World War II freight rate increases

In attachment VIII of the prepared statement which I presented on March 6, 1961, there is set forth a table of the increases in the ocean freight rates in the Pacific coast-Hawaii trade beginning with the increase which became effective on February 1, 1961. In exhibit No. 4 to the statement presented to your subcommittee on March 13, 1961, by Mr. Randolph Sevier, president of Matson Navigation Co., there is included in the second column thereof a list of the increases in the rate per ton of general merchandise carried in this trade; this list begins with the rate which was in effect on July 1, 1946 and indicates all of the increases which had become effective prior to April 15, 1961. On April 13, 1961, the Federal Maritime Board suspended until August 15, 1961, the effective date of an additional general increase of approximately 10 percent in the Pacific coast-Hawaii trade and on shipments from ports in Hawaii to ports on the gulf and Atlantic coasts of the mainland.

4. Effect of ocean freight rates on the Hawaiian pineapple industry

Pineapple is one of the principal bases of the Hawaiian economy. It provides year-round employment for over 8,000 people and peak harvest season employment for a total of approximately 24,000. Annual payrolls are over \$38 million and local purchases by the industry are approximately \$37 million. In total, the Hawaiian pineapple production is valued at \$118 million.

⁵ Prior to Dec. 1, 1949, the Freight Commodity Classification Committee.

The industry is now being faced with a cost-price squeeze in the market of the mainland United States where it must compete with other mainland fruits and, of more significance, with an ever-growing volume of canned pineapple imported from foreign areas. Hawaii's annual production of over 12.5 million cases of canned pineapple (24/2½ case basis) accounts at present for some 55 percent of the world's supply. This represents a decline of some 16 percent from Hawaii's percentage of the world market supply in 1950. Hawaii's participation in the mainland market has similarly declined with ocean freight costs forming an increasingly significant element in this trend.

The total of canned pineapple imports into the mainland have increased from 2 million cases (24/2½ case basis) in 1958 to 2.3 million in 1959 and to 2.6 million in the first 10 months of 1960. Over half a million cases of this increase represents imports of pineapple from foreign countries which are entering the U.S. market as new competitors or, as in the case of Taiwan, markedly increasing an already firmly established foothold. Cases imported from these areas for the first 10 months of 1960 were as follows:

Australia.....	\$1,267
Japan.....	3,383
Malaya/Singapore.....	84,292
South Africa.....	84,084
Taiwan (Formosa).....	309,528
Total.....	562,554

These foreign pineapple can be sold in the United States at lower prices than Hawaiian pineapple, as indicated by the following comparative prices for a case of 24/2 choice sliced pineapple:

From—	West coast price	East coast price
Hawaii.....	\$5.60	\$5.90
Malaya.....	4.85	5.05
Taiwan.....	4.75	4.70

Foreign pineapple can be sold at lower prices because foreign costs are lower. These costs include a number of different items, a substantial factor being the overseas freight cost. It is important to note that it costs more to ship pineapple from Hawaii to the mainland Atlantic coast of the United States than from any other major producing area, in spite of the fact that many of the foreign producing areas are farther away.

Comparative current freight rates per ton on canned pineapple from Hawaii and from competing foreign areas to U.S. Atlantic ports are as follows:

From—	To Atlantic ports
Hawaii.....	\$31.05
Malaya.....	27.68
Philippines.....	26.34
Taiwan (Formosa).....	26.34
South Africa.....	17.86
Mexico.....	15.88

Freight rates are also an important factor with respect to the competition of mainland fruits to Hawaiian pineapple. Pineapple has to pay \$22.05 per ton to get its product to the west coast which is a cost none of the mainland fruits have to bear. In addition, pineapple must stand the freight costs on everything it brings from the mainland to produce its product. Thus, ocean freight costs have a double significance for pineapple in Hawaii, which is over 2,000 miles from the source of supply of what is needed to produce the product, and the same distance from the nearest market for the finished product.

The future of the Hawaiian pineapple industry and to a proportionate degree the economy of Hawaii depends upon its ability to compete in the mainland marketplace.

There is no Hawaiian pineapple producer who could not expand his present production if the mainland market would permit. However, instead of being able to increase production, the trend has been the other way. One producer

went out of business in 1957. Another has substantially reduced its planted acreage and another has announced it is closing down operations altogether. A large pineapple cannery (Hawaiian Canneries) has announced that it will discontinue operations of its cannery at Kapaa, Kauai, after the completion of the 1962 harvest. This termination is of dire consequences to the economy of Kauai in view of the fact that this cannery now engages some 300 year-around employees and increases its employment to approximately 1,500 during the summer months.

The pineapple industry of Hawaii is making a commendable effort to maintain top quality with lower costs and to improve efficiency. Our sole advantage now, however, is the demonstrably better quality of Hawaiian pineapple. In large part, because the ocean freight costs of U.S. ships are significantly higher than those of foreign lines bringing competing pineapple products to the mainland market, the Hawaiian pineapple industry is no longer able to enjoy any price advantage in the mainland market even though it is closer to the mainland than any of the major foreign pineapple suppliers. As Mr. John J. Tolan, secretary-treasurer of the Pineapple Growers Association of Hawaii, pointed out to Mr. Wilfred Goding, of your subcommittee, in a letter dated December 14, 1960, quoting from a speech by Mr. Foster L. Wildron, director of research of Matson Navigation Co.:

"* * * With foreign ships costing less than half of ours and crew wages less than a third of ours it is not surprising that Formosan pineapple can be delivered to the west coast at a transport rate as low as that for your own product."

Very truly yours,

SHIRO KASHIWA,
Attorney General, State of Hawaii.

ALASKA STEAMSHIP CO.,
Washington, D.C., April 18, 1961.

HON. WARREN MAGNUSON,
*Senate Office Building,
Washington, D.C.*

DEAR WARREN: At the close of the subcommittee hearings on the noncontiguous trades there was not sufficient time to question Mr. Skinner on his statement or on general problems connected with maritime service to Alaska.

Senator Bartlett indicated that the committee would be interested in supplementary questions.

We have reviewed the general testimony and wish to supplement our statement in the form of questions that might have been propounded by your committee in an effort to amplify our statement. We submit this material as an addendum to Mr. Skinner's statement.

Sincerely,

HENRY W. CLARK, *Vice President.*

ALASKA STEAMSHIP CO.,
April 18, 1961.

Question. We have seen frequent references to barge competition in the Alaska trade. Do you feel barge transport has a future?

Answer. While the overall tonnage in the Alaska trade has not increased in the past 4 or 5 years that proportion carried by regulated barges has increased, and there are no accurate statistics as to what has been carried by unregulated barges. There is no question but what barge transport can be more economical because they have no manning on the barge and the tug carries a crew of 14 whereas our ships carry crews of 42 to 48; and as I pointed out in my original statement, labor is 73 percent of our costs. This includes longshoring labor as well as the crew, nevertheless the crew costs are a major factor. On the other hand, barges do not adhere to a fixed schedule, particularly if they are forced to navigate in unprotected waters. This current winter three barges were driven ashore in storms, one of them a total loss. Aside from this, their average time of transit is 2 or 3 days longer than ours, and frequently many more days than that.

Cargo on barges is more exposed to the weather than on ships. It is our firm belief that the economy of Alaska is dependent on regular frequently scheduled steamship service.

We believe there is a place for barge competition, but the only barge competition we have faced to date is that regulated service which has limited itself to the so-called rail belt. Because the overall volume of Alaska cargo is so small, the inroads made by contract barges and unregulated barges has posed a serious threat to our operations.

Question. In your testimony you advocated additional personnel for the Federal Maritime Board to permit more extensive policing of the trades. Could you illustrate what you have in mind?

Answer. We face constant competition from barge operators who, in our opinion, do not comply with existing statutes of either the Coast Guard or the Maritime Board. They are able to attract certain cargoes by quoting rates which are not on file. With an adequate staff the Maritime Board could investigate reports of such activities promptly and take those necessary steps that would insure that laws were applied equally to all carriers serving the trade.

Question. You spoke of the small volume and the high costs of the Alaska trade. Would you regard this is a marginal trade?

Answer. We definitely do; the best proof is the fact that 130 carriers have come and gone from the trade in 65 years. I append herewith an exhibit from docket 881 showing the total revenues and expenses with the net results after taxes for the 5 years 1955-59 in the Alaska trade. This will show you that at no time have we made a fair return on our investment and that in 1957 we operated at a loss and in 1959 with a total operation of \$16 million our profit was less than \$100,000.

Question. You state that in your opinion maritime rates do not have as much impact in the prices or economy of Alaska as often contended. To what do you attribute the high cost of living and doing business in Alaska? I appreciate you covered this partly in a verbal answer to Senator Bartlett in the hearing but you may wish to expand on this.

Answer. As I stated orally, the defense program which is the single biggest factor in the economy of Alaska is both a help and a burden. Alaska's economy is based on defense construction wage levels, which were artificially too high in the days when the contractors were actively bidding for labor. The distances to Alaska and within Alaska and the sparse population increase transportation costs. These factors, together with the weather, preclude many large warehouses so that the merchants in an effort to keep down inventories urge frequent sailings which are often made with small tonnage.

Question. Do you feel freight rates can hurt the economy of Alaska?

Answer. There is no question but what any one of the spiraling costs if they continue without any more control than they have had in the past will have a very profound impact.

As I have mentioned, between 1947 and 1960 longshoring costs in Alaska have increased over 120 percent. In that same period our crew costs have increased from 147 to 235 percent with an average increase of 157 percent. These do not include overtime costs.

We again urge strongly an impartial objective study of the relationship of transportation costs to the ultimate cost to the consumer be made. Such a study would give us more factual appreciation of the impact of transportation costs on the economy.

Question. Chairman Stakem stated that FMB did not favor certificates of convenience and necessity because he felt they would stifle competition. We note you favor these certificates. Why?

Answer. We felt that the improvements we have made in our operation notably unitization and containerization have not arisen from competition but from the rising costs in shipping. We desperately need better productivity if we are to keep even or nearly so with the spiraling costs. Certificates, as we understand them, would not be issued to a single carrier so we would still have competition from the leaders in the trade. Our interest in them is that they would eliminate the unregulated, irresponsible operator.

Question. Do you feel that the suggestions you made can avoid rate increases?

Answer. As stated to you, I could not predict whether they would avoid rate increases, but they certainly would minimize them.

Question. You state that rate increases in the Alaska trade have totaled 56.4 percent from 1947 to 1960, whereas evidence was presented showing a larger increase for both Hawaii and Puerto Rico in the same period. Is it not true that the base rate was higher for Alaska in 1947 and consequently the percentages do not reflect the same monetary increases?

Answer. It is difficult to compare rates between the various areas. In some cases the other areas are higher than Alaska and in other cases lower, but in any event the Alaskan consumer has not had to deal with as many or as great increases in his transportation costs since the war as the other non-contiguous areas. We can assume that he had adjusted himself to the Alaska economy the same as the consumers in the other areas have adjusted themselves to their economies in 1947.

Question. Your present fleet was acquired from war shipping. Have you any program for replacement?

Answer. Our ships are now carried by Maritime on a 25-year life basis, which gives us 10 more years according to all accounting procedures. We have kept our ships in A-1 repair and have spent hundreds of thousands of dollars on modernization; consequently we regard this statutory ship life as a minimum.

Beyond this we have never been able to set aside any reserve for new construction. The possibility of using replacement ships from the subsidized lines does not offer much help because larger, more expensive ships are not enough faster to make them as economical as the ships we are now operating. Frankly, we feel the replacement problem, while not immediately upon us, is one of our most serious concerns.

Question. Your statement refers to the fact that Alaska has unequal status with the other noncontiguous areas as regards cabotage because of the third proviso of section 27 of the Merchant Marine Act of 1920. Would you explain this in more detail.

Answer. Because of geographical position we face the possibility of carriage from interior United States through interior Canada to a Canadian port, thence to Alaska.

For example, Canadian National Railway has applied to the Trans-Continental Freight Bureau to publish rates between Prince Rupert and Ketchikan based on using Canadian National Railway from midwestern points to Prince Rupert and Canadian flag tug and barge Prince Rupert to Ketchikan.

The rate has not yet been published, and the service has not been inaugurated, but it is quite possible that such service may be offered in the near future thus draining cargo from U.S. rail lines and U.S. vessels. I know of no justification for permitting Canadian-flag vessels to participate in purely domestic U.S. commerce. Canadian law is explicit in reserving all Canadian domestic traffic to Canadian-flag vessels.

Question. While you are not yet faced with direct competition from foreign carriers, is there any indirect impact?

Answer. In the past year foreign imports to Alaska have increased 100 percent. Practically all of this increase is from Japan. This means that American suppliers are losing part of their usual market, and the American carriers lose the tonnage. There has been substantial increases in shipments of building supplies including cement, plywood, nails, reinforcing and structural steel, hardware, etc., by the Japanese. It is in this growing market that we are getting indirect foreign competition. The new pulp mill at Sitka, Alaska, which provides the Japanese owners with a source of raw material, also provides westbound cargo for Jap ships. It is perhaps natural that they should try to develop an eastbound cargo to Alaska—the 100-percent growth previously mentioned is proof of their success.

HENRY W. CLARK,
Vice President.

[From brief of Alaska Steamship Co. before the Federal Maritime Board in docket No. 881, Feb. 24, 1961, p. 29]

TABLE IV

	Year—				
	1955	1956	1957	1958	1959
Total revenues.....	\$14,285,065	\$14,644,466	\$13,521,327	\$15,718,157	\$16,185,665
Total expenses.....	13,563,146	14,006,732	13,539,369	14,848,824	15,992,656
Net result before Federal income taxes.....	721,919	637,734	(18,042)	869,333	193,009
Estimated Federal income taxes.....	375,398	331,621	(1)	452,053	100,365
Net result after Federal income taxes.....	346,521	306,113	† (18,042)	417,280	92,644
Operating ratio.....	97.57	97.91	100.13	97.34	99.43

† Loss.

MATSON NAVIGATION Co.,
Washington, D.C., April 13, 1961.

Re domestic offshore shipping

Mr. GERALD GRINSTEIN,
Subcommittee on Merchant Marine and Fisheries,
Senate Office Building, Washington, D.C.

DEAR MR. GRINSTEIN: On the conclusion of the hearing on domestic offshore shipping on March 13-14, 1961, before the Subcommittee on Merchant Marine and Fisheries, Mr. Randolph Sevier requested our Honolulu office to ascertain whether mainland companies pay a cost of living allowance to their employees in Hawaii, a subject discussed at the hearing.

We have only been able to find one company that definitely pays a differential. This is Pan American World Airways, who pay a 25 percent differential on base pay up to a maximum of \$75 per month. We unofficially understand that this is being discontinued on July 1, 1961.

United Air Lines, we understand, gives a small increase to nonmanagement personnel, but it is not considered a cost of living differential. Also it is not taken away from the employee when the employee leaves Hawaii for reassignment. United apparently has several types of pay schedules based on where the employee is stationed. As an example, wages for nonmanagement personnel in Los Angeles are less than in Hawaii, but more than in New York. There does not seem to be a standard set percentage increase.

We have checked with the Hawaii Employers Council, who indicate that Lockheed Aircraft provides a differential. However, we have been unable to learn what that is. There is no indication that any other company pays a differential. The Government seems to be the main source of such differential pay.

Sincerely,

A. J. PESSEL.

APPENDIX A

PUERTO RICO'S PROBLEM WITH THE U.S. MARITIME LAWS

The laws of the United States affect the maritime commerce of Puerto Rico in numerous ways. However, Puerto Rico's specific and peculiar problem to be discussed in this memorandum arises from the interaction of postwar economic developments with two particular provisions:

1. The application (by the Foraker Act of 1900) of the coastwise shipping laws to trade between Puerto Rico and the continental United States which is thus confined to service by American-built, American-operated, and American-manned vessels under the U.S. flag.

2. The limitation to foreign trades under the Merchant Marine Act of 1936 of both the operating and construction cost differential subsidies which thus do not benefit trade between Puerto Rico and the continental United States.

The limitation of the shipping trade between Puerto Rico and the continental United States to U.S. vessels serves the primary purpose of the U.S. maritime laws—to maintain for reasons of national policy an adequate American merchant marine. The consequence is that the high cost of U.S. flag service is borne by the commerce and the people of Puerto Rico.

As a result of postwar economic developments, this cost borne by Puerto Rico has become a heavy, discriminatory burden, unjust to the people of Puerto Rico and in conflict with the national interest of the United States. There is no reason to believe that the Congress ever intended to impose such a burden, nor is it necessary to perpetuate it in order to serve the intended purposes of the U.S. maritime laws.

The economic trends which are responsible for making this special burden of Puerto Rico excessive and discriminatory have not stopped. In fact, consequences of the developments which have already occurred have not yet been fully felt. It can clearly be foreseen that these consequences will, within another few years, seriously impede the efforts of the Commonwealth of Puerto Rico to improve its economy and to raise the severely depressed living standard of its people, unless corrective action is taken.

It is the purpose of this memorandum to show how the unintended burden on Puerto Rico has arisen, to demonstrate its size and to explore means by which it can be alleviated without violating the basic purpose of maintaining an American merchant marine of adequate size.

PUERTO RICO HEAVILY DEPENDS ON COMMERCE WITH THE CONTINENTAL UNITED STATES

Puerto Rico is a small island but it also is the home of more than 2 million people. Rhode Island and Delaware are the only States with a smaller land area but 25 of the 50 States have a smaller population. Puerto Rico's population density of 685.1 per square mile (1960 census) is exceeded only by that of Rhode Island (693.5 per square mile) and is almost 12 times the average of the continental United States (58.9).

If the United States was as heavily populated as Puerto Rico, its territory would hold nearly all the people in the world. Yet Puerto Rico's natural resources are narrowly limited. Puerto Ricans must satisfy many of their needs with goods grown or made elsewhere and they have depended on such goods ever since the island was discovered in the days of Columbus. To develop a decent standard of living, Puerto Ricans must bring in not only a large portion of their necessities but also capital goods and raw materials to make products for shipment to other markets.

With a net income of \$1,311 million in the fiscal year 1960, Puerto Rico bought goods from other areas in the amount of \$912 million (83 percent of it from the continental United States) and sold goods in the amount of \$612 million (97 percent to the continental United States). The total of its two-way oversea trade thus amounted to more than its net income. In contrast, total imports and exports of the United States by land and by water have in recent years been well under 10 percent of net national income. Puerto Rico's dependence on its oversea trade with the continental United States is at least a dozen times greater than the dependence of the United States on all its foreign commerce.

The sealanes between Puerto Rico and the mainland are the highways connecting Puerto Rico with the States. The importance of efficient interstate highway transportation to economic progress and national defense is well recognized by the institution of the Interstate Highway System. Efficient transportation at reasonable cost is needed with equal urgency on the sealanes that are the highways between Puerto Rico and the States.

Puerto Rico's standard of living has risen rapidly in the last decade but per capita income still is under half that of Mississippi, the lowest ranking among the States, and a little under one-quarter of the U.S. average. Puerto Rico needs much further improvement. As its development progresses in ever-increasing integration with the economy of the United States, its dependence on oversea transport also is bound to increase further. Careful estimates indicate that total dry cargo shipments and receipts must be expected to rise by about two-thirds in the next 15 years if Puerto Rico's development is to proceed on its expected and sorely needed course. Burdensome shipping rates impose a serious handicap on this essential progress.

PUERTO RICO PAYS HEAVY FREIGHT CHARGES BOTH WAYS

As the overwhelming proportion of Puerto Rico's oversea trade is interchanged with the continental United States, cargo has to be carried over a substantial distance—more than 1,000 miles to the nearest Florida ports; about 1,600 miles to New York, Philadelphia and Baltimore where the heaviest traffic is concentrated; somewhat further to the important gulf ports of Mobile, New Orleans and Houston; and two or three times as far to the Pacific ports from which Puerto Rico also receives heavy loads. Thus, freight charges necessarily are substantial. And Puerto Rico has to pay them both ways, coming and going.

Ordinarily, it is difficult to determine who bears the burden of transportation charges. In regard to any individual transaction, it is, of course, easy enough to find out whether the buyer or the seller makes the actual freight payment to the carrier. But, other important, though less obvious, factors must be considered. First, the freight-paying buyer may, because of competitive pressure, be able to reduce his price to the seller by the amount of the freight or by part of it; conversely, the freight-paying seller may be able to raise his price to the buyer by the amount of freight or part of it. Second, the buyer who bears the freight cost without purchase price adjustment, may pass it on to his customer, or the seller who bears it may pass this cost back to his supplier. Moreover, when more than one transaction is to be considered, it must be recognized that market conditions create differing situations for different commodities and also for the same commodity at different times.

Because of all these difficulties, it has become an accepted convention in analysis covering any large aggregate of cargo movements to assume that the freight cost is split evenly between sellers and buyers, shippers, and recipients. Because of the law of averages, it is assumed that the actual distribution is more likely to approximate such an even split than any other division of transportation cost. While this assumption may be valid in many cases, it is not at all realistic in regard to traffic between Puerto Rico and the continental United States.

Puerto Rico's purchases from the continent, while representing a large share of Puerto Rican supplies, amount to only a very small fraction of demand on the many times larger U.S. market. Absorption of freight by mainland sellers might result in a reduction of price to ultimate consumers in Puerto Rico and thus lead to an increase in local demand. However, even if this increase were percentage-wise large, it still would be a hardly noticeable addition to demand in the mainland market. Consequently, there is no incentive for mainland sellers to absorb freight charges to Puerto Rico. These charges must be borne by the economy and the people of Puerto Rico, except under unusual and rare circumstances.

Similarly, Puerto Rico's shipments to the continent, while representing a large share of Puerto Rico's production, account for only a small fraction of mainland supplies of most of the products concerned. There are some exceptions which will presently be discussed. In the ordinary situation, the Puerto Rican share of mainland supplies is too small to affect mainland prices. That is, the Puerto Rican product delivered in New York will bring the same price as an identical product made in that city. The freight must be borne by the Puerto Rican seller.

Among the apparent exceptions, raw sugar is most prominent, since Puerto Rico supplies the mainland market with a much larger share of this commodity than of any other important one. However, under the quotas and other features of the marketing system established by the Sugar Act, the delivered cost of the Puerto Rican supply cannot exert any significant influence on the sugar price. Puerto Rican producers get the same mainland price no matter what their production and delivery costs may be. Thus, transportation charges for sugar are borne by Puerto Rico.

Puerto Rican manufacturers may also supply a substantial proportion of the mainland market in a few specialty items, notably brassieres. In these instances, it may be more difficult to determine where the freight charges are ultimately borne, but these items have low transportation costs, are often shipped by air, and certainly account for a minute portion of the total ocean freight bill. Another situation in which the freight charge distribution is difficult to appraise, may be that of Puerto Rican tobacco. While this product does not account for a large portion of the total mainland tobacco supply, its characteristics are sufficiently distinct to establish a separate market and only a detailed analysis

of that market would indicate where the transportation cost is borne. Yet, even if it were all borne by mainland buyers, it would not greatly affect the distribution of the total ocean freight bill for Puerto Rico's commerce with the continental United States.

It follows from all the foregoing that there may be some situations in which Puerto Rico does not have to pay all of the freight for its shipments to the mainland. Without an exhaustive study, it is impossible to say that no similar situation exists from time to time in regard to Puerto Rican cargo receipts from the continent. It is clear, however, that the share of the total ocean freight bill paid by the mainland economy must be very small indeed. While the statement that Puerto Rico pays the total freight charges both coming and going may not be literally and precisely correct, it certainly is so nearly accurate as to be descriptive of the actual facts. Even if it can be said only with some qualifications that Puerto Rico pays the total freight bill both ways, there is no doubt but that the burden of any differential between low and high transportation costs falls on the economy and the people of Puerto Rico.

U.S. FLAG SERVICE IS ESPECIALLY EXPENSIVE

Due to geographic and economic conditions, Puerto Rico would in any event have to carry a heavy burden of transportation costs for its commerce with the continental United States. Its distance from mainland sources of supplies and markets necessarily involves a large freight bill. Much of its trade consists of bulky goods of limited value. The inevitably heavy freight burden is aggravated, however, by the mandatory and exclusive use of U.S. shipping services. It is not necessary here to explain that—or why—operation of U.S. flag vessels is substantially more expensive than ship operation under foreign flags. For vessels operating regularly in foreign trade, the recognized operating cost differential is made up by Federal subsidy. In trade between Puerto Rico and the continental United States, this differential is borne by the economy and the people of Puerto Rico as part of the freight charges they pay.

Operating cost differentials recognized for subsidy purposes in foreign services by the Maritime Administration in 1956, 1957, and 1958 average 71.9 percent of wage costs, 21.4 percent of subsistence costs, 30.5 percent of maintenance and repair costs, 18 percent of hull and machinery insurance, and 55 percent of protection and indemnity insurance. Since then, some of the recognized differentials have been slightly revised, others increased. The net change has not been significant and the 1958 rates still provide the best basis for estimating the operating cost differential borne by Puerto Rico due to the obligatory use of U.S.-flag vessels for its shipping services to and from the continental United States.

The volume of cargo carried and the operating costs incurred by the carriers in regular service between Puerto Rican ports on the one hand and Atlantic and gulf ports on the other hand are known in detail from the record of the investigation of rates and charges in these services conducted by the Federal Maritime Board between 1957 and 1959 (docket No. 807). Detailed computations based on these data and on the average operating differentials quoted above are shown in appendix A. These computations indicate that the operating differential borne by Puerto Rico in these services averaged \$4.04 per long ton of cargo in 1957.

The carriers' freight revenues in these same trades averaged \$29.93 per long ton in 1957. Freight rates in these services are subject to regulation by the Federal Maritime Board. If the carriers' costs had been lower by the operating differential, their charges would have been lower by at least the same amount and would have averaged no more than \$25.89 per long ton in 1957. The operating differential borne by the economy of Puerto Rico thus was equal to a surcharge of 15.6 percent on top of the freight cost that would have prevailed if the mandatory U.S.-flag service did not involve especially high operating costs.

Equally detailed information is not available for the services between Puerto Rico and ports on the Pacific coast. Because of the much longer distance, the operating cost differential per ton of cargo is certainly larger than on the Atlantic and gulf routes.¹ On the other hand, the operating cost differential is

¹ Data available from the Federal Maritime Board investigation of the general increase in Pacific coast-Puerto Rico rates (docket No. 903), while not conclusive, would support an estimate placing the operating cost differential at \$6.93 and the surcharge at 18.3 percent.

probably somewhat smaller for that portion of dry cargo which moves in bulk between Puerto Rico and the continental United States and for which also no detailed cost information is available. However, much of this bulk traffic is carried by the same operators and in the same or similar vessels as the liner traffic to and from Atlantic and gulf ports. Consequently, the assumption of an operating cost differential equal to that found in liner service cannot be far wrong for these bulk movements. Probably the only exception is the heavy movement of cement to Florida, a private shipping operation of the cement producer. If this movement is excluded from consideration, it can be assumed that, on the average, the operating cost differential for all cargo traffic (except cement) between Puerto Rico and the continental United States (including bulk movements as well as movements from and to Pacific ports) is about the same as the differential computed for liner traffic from and to Atlantic and gulf ports; that is, \$4.04 per long ton of cargo in 1957. While no dependable figures are available for a more recent year, the present operating cost differential is likely to be somewhat higher.

THE BURDEN ON PUERTO RICO IS EXCESSIVE AND DISCRIMINATORY

Official statistics on the total volume of ocean traffic between Puerto Rico and the continental United States are provided and analyzed in appendix B. These data show that the dry cargo movement on which Puerto Rico bears the surcharge of the operating differential for U.S.-flag shipment amounted to 2,738,000 short tons in 1959. The previously computed 1957 operating cost differential of \$4.04 per long ton (or \$3.61 per short ton) therefore amounts to a total of almost \$10 million. Since ship operating cost differentials continued to rise after 1957, it is safe to say that the cost of the operating differential to the people of Puerto Rico now exceeds \$10 million.

This surcharge on the ocean freight bill is distributed throughout Puerto Rico's economy in several ways. The surcharge on incoming goods is reflected principally in higher prices to the consumer and thus is a reduction of his real buying power. However, it also affects the prices of producers' goods and thus the cost of production in Puerto Rico. Where this production is for the local market, the ultimate effect on the consumer is approximately the same as that of the surcharge on consumer goods. Where the production is for the mainland market, the effect of the surcharge on incoming producers' goods is merged with the effect of the surcharge on products going to the mainland. The two combine to reduce the net revenue of the Puerto Rican factors of production. Some of this reduction may be absorbed by lower profits of Puerto Rican enterprise but most of it is likely to be reflected in lower wage payments. The total surcharge thus has the effect of reducing the standard of living of the people of Puerto Rico.

In order to appraise the significance of this burden, it is best to compare it with the operating differential subsidies paid by the Federal Government to ship operators in foreign trades. These subsidies are the means by which the burden of the operating differential in other U.S. shipping services is distributed to the taxpayers in the continental United States. The accounts of the Maritime Administration show operating differential subsidies of \$152.7 million for 1959. This amounted to \$0.89 per capita for the population of the continental United States (176,947,000 on July 1, 1959). In contrast, the burden of \$10 million on the Puerto Rican people (2,340,000 on the same date) amounted to \$4.28 per capita. Thus, the burden on each person is on the average five times as heavy in Puerto Rico as it is in the continental United States.

However, average personal income in Puerto Rico in 1959 was only \$511 as against \$2,165 in the continental United States. Thus, the cost of the maritime operating differential to the Puerto Rican people absorbed 84 cents out of every \$100 of their income, while the cost to the people on the continent amounted to only 3.8 cents per \$100 of income. For the identical purpose of keeping merchant ships in operation under the American flag, the people of Puerto Rico who can less afford it are contributing 5 times as much per person and 22 times as much in relation to income as the much wealthier population of the continental United States.

Yet, even these drastic figures do not tell the full story. They reflect only the operating cost differential on the traffic which actually moved between Puerto Rico and the continental United States in 1959. But, if there were no such burden, and if freight rates were correspondingly lower, the traffic would be larger. Approximately 56 percent of the value of Puerto Rico's merchandise

shipments (excluding petroleum and its products) are products of some 600 industrial plants established in the postwar period as a result of the determined and widely recognized development efforts of the Commonwealth Government. Since the decision to locate in Puerto Rico depends on comparative cost and since freight costs are for many industries an important factor, there can be no doubt that more new plants would have been established each year if there had been no operating cost differential and freight rates between Puerto Rico and the mainland had been lower.

The mandatory use of American-flag service thus has not only imposed a heavy surcharge on the Puerto Rican people for the traffic that actually moved; it also has slowed down industrial development and, with it, the reduction of Puerto Rico's high rate of chronic unemployment and the sorely needed improvement in the low living standard of its people.

ECONOMIC TRENDS THREATEN TO AGGRAVATE THE BURDEN

The excessive and discriminatory burden on the Puerto Rican economy demonstrated above arises from the mandatory use of U.S.-flag ships without the benefit of operating differential subsidy. When this kind of subsidy was confined to foreign trades in the Merchant Marine Act of 1936, economic conditions were different. It is due to several postwar developments that the burden has grown to its present importance.

In 1936, the economy of Puerto Rico was far less developed. Apart from the shipment of sugar, its traffic with the continental United States was quite small. There was no industrial development that could be slowed down by the high freight level. Moreover, the effect of the operating cost differential on the freight level was far more modest. All this began to change after the war and the change has been a continuous one, with the consequences becoming more important year after year.

It is hardly necessary to elaborate here on the progressing transformation of the Puerto Rican economy. It may suffice to point out that total dry cargo traffic with the mainland, which now exceeds 2.7 million tons, was little more than 1 million tons in the last few years before the war and around 1.5 million tons in the first few postwar years. Thus, the cargo movement on which Puerto Rico bears the operating cost differential has grown greatly. It must continue to grow if the development of the Puerto Rican economy is to progress.

While the cargo movement has been growing, the operating cost differential included in the freight bill has been rising at a much faster rate. The operating cost differential recognized by the Maritime Administration in foreign trades has increased almost every year since the end of the war. In the first few years after the war, subsidies covered a little more than 45 percent of American expenditures for items subject to operating cost differential. Today, the ratio is more than 60 percent. This means that the recognized differential has increased from little more than 80 percent of foreign costs to more than 150 percent—almost twice as much. Just as the operating cost differential in foreign trades has grown, a constantly increasing percentage has also been added to Puerto Rico's freight bill. There is no reason to believe that this rising trend has run its course. On the contrary, it must be expected to continue.

The same economic factors which are responsible for the uptrend in the cost of American ship operation, also are at work to increase another portion of Puerto Rico's freight bill which has not yet been considered—the cost of loading and discharging of cargo. In stevedoring as in shipping and shipbuilding, wages have kept pace with the rise in the general American wage level which has been supported by a rapid increase in productivity. But no such increase in productivity has occurred in shipping and shipbuilding, or in loading and discharging cargo. As a result, stevedoring expense also has steadily become heavier. In 1957 it averaged in liner service between Puerto Rico and Atlantic and gulf ports \$15.25 per long ton, or 51 cents out of every dollar of freight charges. In service between Pacific coast ports and Puerto Rico in 1959, stevedoring and related expenses averaged \$18.38 per long ton, or 54 cents out of every dollar of freight charges.

High stevedoring expenses together with high-level operating costs have made shipping inordinately expensive in the United States. This is dramatically illustrated by the sharp traffic decline in coastwise and intercoastal ship operations. While total economic activity in the United States (as measured by GNP in constant dollars) has in the last few years been more than double that of the years immediately before the war, coastwise tonnage of deep sea operators on the At-

lantic and gulf coasts, for example, has been only about one-quarter of the prewar level. Its relative importance thus has dropped to one-eighth, as shippers have found movement by rail and truck more economical for most cargoes.

No similar diversion of cargo to more economical transportation is possible in oversea trades. Yet, the technological lag and high cost of ocean shipping—and especially of ocean shipping under the American flag—is equally bothersome in these trades. The shipping industry is paying increasing attention to this problem. It is attempting to reduce costs by introducing vessels with lower operating expense and developing new methods of cargo handling in order to reverse the trend of growing stevedoring costs. With its freight bill already including a discriminatory, heavy, and growing surcharge to meet the operating cost differential of American vessels, Puerto Rico certainly needs to benefit from technological improvements to reduce its stevedoring cost.

Indeed, in the absence of such technological improvement the inevitable rise in stevedoring wages is bound to lead to a continuing increase in costs of transportation between Puerto Rico and the mainland. Cargo rates on the Puerto Rican routes have in recent years risen much more than the general price level. Rates of the most important service from Atlantic and gulf ports to Puerto Rico have been increased almost 50 percent in the past 10 years and rates from Pacific ports to Puerto Rico have risen even more. The upward trend in costs will necessarily continue unless the effect of wage increases can be neutralized by technological improvement. Yet, Puerto Rico's ability to benefit from such improvement unhappily is sharply curtailed by the U.S. maritime laws which require the use of American-built vessels but provide no means for getting such ships into service between Puerto Rico and the continental United States.

SHIP REPLACEMENT COSTS IMPEDE TECHNOLOGICAL PROGRESS

While some limited reductions in stevedoring costs can be achieved with vessels of traditional design by technological improvement in the handling of cargo, it is generally recognized that major reductions in both stevedoring and vessel operating costs depend on improved vessel design. This is dramatically illustrated by the profitable operation of vessels of modern construction in international trades in which shipping rates now are so low that older vessels cannot earn their depreciation. In trades like those between Puerto Rico and the continental United States where voyages are relatively short, cargo handling accounts for an especially heavy share of total cost. Therefore, it becomes especially urgent to avert continuous cost increases by the replacement of older vessels.

The four carriers now rendering the largest part of the services between Puerto Rico and the continental United States are using war-built C-1 and C-2 vessels which were acquired at relatively low prices. In their liner trade to the Atlantic and gulf ports, they employ the full-time equivalent of 14 such vessels for which they paid about \$16 million (including cost of betterments) and which have now been depreciated to about \$7 million. A Maritime Administration estimate placed the market value of these vessels in October 1958 at \$11.3 million. However, the cost of replacement by vessels built in American yards and of modern design—as, for example, the Maritime Administration's *Clipper*—is estimated at \$164 to \$187 million (the exact amount depending on the number ordered at any one time). Even to reproduce these vessels "as is" in American yards today is estimated to cost \$103 million.

A new investment of approximately \$170 million over and above the amounts now invested in these ships would be needed to replace them with modern vessels. While these ships handle the major part of Puerto Rico's traffic, they do not carry all of it. To assure the most efficient handling of all cargo between Puerto Rico and the mainland would require a new investment of more than \$200 million.

The need for such a vast investment over and above the capital now employed arises from the combination of three factors. First, a modern ship is a more complex piece of machinery and therefore more expensive. The significance of this factor may be indicated by the difference of about 70 percent between reproduction "as is" and replacement with modern vessels (although the difference would be considerably less if cost in foreign yards were considered). This additional investment needed to secure the modern design features is economically warranted, because it is more than offset by reduction in vessel operating and cargo expenses.

Second, the capital required for acquisition of the present ships was kept to a minimum by action of the Federal Government which made these vessels available at low prices under the Ship Sales Act of 1946. If the operators had at that time been compelled to acquire vessels at prices related to the cost of new construction in American yards, they would not have been able to resume normal service. Nor could they subsequently have expanded their operations with vessels purchased on such terms. The entire economic development of Puerto Rico would have been stymied without the postwar ship disposal programs. The Ship Sales Act of 1946 thus forestalled the development of far more serious problems by treating operators in Puerto Rican and other domestic trades on an equal basis with operators in foreign trades.

Third, like U.S.-flag operators on "essential trade routes," the operators of services between Puerto Rico and the mainland must under existing laws employ vessels built in American yards where costs are far higher than in foreign yards. However, unlike the Ship Sales Act of 1946, the ship replacement program established in recent years under the Merchant Marine Act of 1936 does not treat operators on Puerto Rican routes on an equal basis with those in foreign services who are entitled to construction differential subsidies.

In foreign trades, the replacement of old vessels by modern ships built in American yards is made possible by these construction differential subsidies which now cover approximately 50 percent of the cost of new vessels—plus a number of other Government supports. In addition to paying half or almost half of the cost of the new vessels, the Government takes back the old vessels at a fairly generous trade-in value, thus reducing the cash need to less than 40 percent of the new vessels' cost. Moreover, it will grant a 20-year loan equal to 75 percent of the operator's cost or else it will provide mortgage insurance up to 90 percent. Perhaps even more important, the Government has exempted from corporate income tax, in addition to depreciation, ship operators' profits set aside for the purpose of vessel replacement. For foreign trade operators, the true cost of replacing an old vessel with a modern ship built in an American yard is thus reduced to a small fraction of the new vessels' construction price.

Operators in trade between Puerto Rico and the continental United States also are compelled by law to employ only American-built vessels—but they would have to pay the full construction price. They are not eligible for construction differential subsidies nor is any substitute provision made to reduce the cost of vessels for service between Puerto Rico and the mainland, although this cost is virtually doubled by the requirement of the U.S. maritime laws that the vessels must be built in American shipyards. While the true cost of American-built ships for foreign trade operators is reduced by the U.S. Government to a small fraction of the construction cost, no Government assistance is available for ships to serve Puerto Rico.

It is hardly necessary to emphasize that, under these conditions, the huge gap between the value of the old vessels now serving Puerto Rico and the cost of new ones is prohibitive. The private operators cannot be expected to raise \$200 million or more for investment in new ships. Nor would vessel replacement on these terms do Puerto Rico much good; a reasonable return on the additional \$200 million capital investment would have to be covered by freight rates and would outweigh the saving to be expected from more efficient vessels. As the beneficial effect of the Ship Sales Act of 1946 runs out, some means must be found to facilitate the extension of the ship replacement program to the Puerto Rican routes. Otherwise, Puerto Rico has no prospect of receiving service with more modern vessels and thus stopping the trend toward higher and higher freight rates which seriously threaten the continuation of its economic development.

FEDERAL RATE REGULATION HAS NOT HELPED

Under the maritime laws of the United States, Puerto Rico's trade must be carried in American-built vessels under the American flag and with American crews. This requirement protects the shipping companies against foreign competition. The people of Puerto Rico have no protection from the heavy burden of high transportation costs which inevitably arises from the mandatory use of American service. The laws providing for rate regulation are designed only to preclude even higher charges due to exploitation of the carriers' protected position. Even this modest aim of rate regulation has been frustrated by the manner in which the Federal Maritime Board's regulatory powers have been exercised.

In recent years, due to the intervention of the Commonwealth of Puerto Rico (and of Hawaii and Alaska) the Board has investigated the carriers' proposed tariffs. These investigations, however, have been ineffective and exceedingly slow—and meanwhile the rate increases have been allowed to go into effect. To cite but the most blatant example: A general increase of 15 percent in rates from Atlantic and gulf ports to Puerto Rico, filed by the carriers on December 4, 1956, was allowed to go into effect on January 10, 1957, but the Board did not pass on its justification until April 28, 1960. The Commonwealth of Puerto Rico's appeal of the Board's approval of this and a subsequent rate increase provides the first court test of the standards of decision used by the Board since the inception of its responsibility for regulation of domestic shipping rates. The U.S. court of appeals has not yet rendered its decision in this proceeding, but, on key issues, the U.S. Department of Justice has supported the position of the Commonwealth rather than that of the Federal Maritime Board.

The ineffectiveness of regulatory control has combined with the economic trends of the postwar period to raise the transportation costs which Puerto Rico's economy must bear. Shipping rates from Atlantic and gulf ports to Puerto Rico have been increased five times in the postwar period. Some of these tariff increases varied as between commodities; others raised rates by uniform amounts or percentages. The average increases amounted to approximately the following percentages:

	<i>Percent</i>
Effective May 14, 1946.....	25
Effective May 10, 1948.....	11 $\frac{1}{4}$
Effective Nov. 12, 1951.....	14 $\frac{1}{4}$
Effective Jan. 10, 1957.....	15
Effective Jan. 15, 1958.....	12

Due to the cumulative effect of these increases, the rates are now more than twice as high as they were at the end of the war and 64 percent above the level established by the postwar adjustment of 1946. In the last 10 years alone, they have risen almost 50 percent. A tariff recently filed by the carriers would make further substantial increases if and when it were allowed to go into effect. Rates from west coast ports to Puerto Rico have risen even faster, some of them by almost 80 percent since 1951.

Because of the manner in which rate regulation has been administered, it is not possible to determine what proportion of the increase in the freight charges borne by Puerto Rico was an inevitable consequence of the interaction between U.S. maritime laws and postwar economic trends. More effective administration of the regulatory power almost certainly would have kept firmer brakes on the uptrend of rates. If the carriers had not been able to obtain with little difficulty any rate increase they considered necessary to offset rising costs, they might have made earlier and greater efforts to institute cost-saving methods of operation.

Although rate regulation has not helped in stimulating technological progress, a start has been made with the introduction of container ships, as the carriers have begun to recognize that indefinitely rising freight rates are bound eventually to throttle the development of traffic. Containerization alone, however, is not enough to offset the burden arising from the combined impact of cabotage restriction and high American operating expenses. Far more energetic efforts will have to be made to balance American wage levels by American technology, and these efforts depend on the feasibility of introducing vessels of modern design at costs which the traffic can bear.

FAIRNESS REQUIRES RELIEF FOR PUERTO RICO

Puerto Rico's economy and its people are caught in a squeeze between Federal maritime laws and economic trends in shipping and shipbuilding. As the maritime laws now stand, they require the carriage of goods between Puerto Rico and the continental United States in American-built vessels under the American flag and with American crews. Economic trends have made this kind of shipping service inordinately expensive.

In foreign trades, where the maritime laws provide for similar service, the excessive cost is borne by the Federal Government through operating and construction differential subsidies and other benefits provided for operators. None of these benefits are available to carry, or even share, the burden in trade between Puerto Rico and the continental United States which is the lifeline of the

Puerto Rican economy. Instead, the burden must be borne by the people of Puerto Rico—among all American citizens, those least able to pay.

The operating cost differential on the actually moving traffic between Puerto Rico and the continent taxes the Puerto Rican people with a surcharge 22 times as heavy relative to their income as the taxes levied on continental citizens in order to make up for the operating differential in their oversea trade. This surcharge, which also is slowing down Puerto Rico's industrial development and thus imposing an added burden, is bound to grow if present trends are allowed to run their course. It is further aggravated by the rising trend of stevedoring cost. Yet, the economically indicated remedy of technological progress is made inaccessible by the Federal mandate to use prohibitively costly American-built ships and the Government's failure to make up for this extra cost.

The Federal Government surely never meant to put this squeeze on the people of Puerto Rico. It required the use of American-flag service as part of its policy to maintain an American merchant marine and in line with international custom in regard to coastal shipment. It provided no subsidy for this service because no such subsidy seemed needed where operators are protected against foreign competition. It had no reason to anticipate that these rules would provide a framework for the development of an unexpected and heavy burden on the people of Puerto Rico. Yet, economic trends of the postwar period operating within this legal framework have brought the burden into existence. It clearly is an excessive and discriminatory one. And it is one which Puerto Rico cannot escape by using alternative means of mass transport.

Fairness requires a change in the framework of maritime laws which has given rise to this burden. A legally simple change in the framework would be the removal of the cabotage restriction—the opening up of shipping between Puerto Rico and the continental United States to the unrestricted competition of foreign operators. It is not possible to anticipate the results of such a step with certainty. It might or might not provide Puerto Rico with adequate shipping service free of the surcharge involved in the operating cost differential; and it might or might not attract modern tonnage with low operating cost and develop improved and cheaper cargo handling methods. Surely, however, the lower cost of foreign-flag operations and of shipbuilding abroad would reduce the surcharge on the freight bill which must be paid by the people of Puerto Rico through an increase in their cost of living and a reduction in their income.

Removal of the cabotage restriction would not be a step without precedent. No cabotage restriction is in effect between the Virgin Islands and the continental United States. The restriction also has been suspended from time to time for traffic to Alaska and in other places where American operators could not or would not provide adequate service. Puerto Rico, too, has at times suffered from complete lack of service from or to certain coastal areas of the mainland. At present, there is no service at all between Puerto Rico and the Great Lakes. Service between Puerto Rico and the Atlantic ports south of Hatteras and westbound service to the Pacific ports are both relatively inadequate. All these routes are of economic importance to Puerto Rico. Certainly, on routes where Puerto Rico does not obtain regular American-flag service, foreign ships should be allowed to fill the gap.

On the principal routes between Puerto Rico and the continental United States the difficulty does not center on the availability of service but on its high cost. While this is a very serious problem indeed, it can perhaps be solved without removal of the cabotage restriction. Its removal from these trades would affect a shipping activity much larger than those involved in any of the other instances cited above. In Puerto Rican trade, removal of the cabotage restriction would hurt ship operators who have been profitably serving Puerto Rico. It would also reduce the peacetime employment of American merchant vessels. This reduction would have a more serious impact on the national interest than is indicated by the mere number or tonnage of the vessels now serving the trade. Apart from the fact that this tonnage may be expected to grow with the development of Puerto Rico and the increase in its shipping needs, these vessels are much more certain to be available in case of an emergency than those plying the seven seas in foreign service to distant areas.

The government of the Commonwealth recognizes these drawbacks of a complete elimination of the cabotage restriction. While it would have no reason to oppose this approach to relief for Puerto Rico, other means of relief for Puerto Rico must be explored if the Federal Government does not desire to open up

the trade between Puerto Rico and the continental United States to foreign-flag services.

THE OPERATING COST DIFFERENTIAL SHOULD NOT BE BORNE BY PUERTO RICO

As long as the maritime laws require the use of American-flag vessels between Puerto Rico and the continental United States, this service will be burdened with operating costs higher than those occurring for merely geographic and economic reasons. There is only one justification for incurring such higher costs—the national interest in the American merchant marine. This added cost should not be borne by the people of Puerto Rico but by all the people of the United States through the Federal Government. It can be done in a simple and fair way by extending the operating cost differential subsidy to shipping between Puerto Rico and the continental United States.

To be sure, operators in this trade, in contrast to those in foreign trades, are not in competition with foreign flags. Basically, however, the subsidies provided to foreign trades are not intended to protect American-ship operators against competition but to serve the national interest of maintaining an active merchant marine. Since the same interest is served by restricting Puerto Rican operations to American-flag ships, it is equally justifiable that the operating cost differential be borne by the U.S. Government. As in foreign services, the subsidy payment would permit the maintenance of the service with lower freight revenues than would otherwise be needed.

Administration of operating cost differentials for Puerto Rican trade would have to differ in some respects from their administration for foreign trades. However, the necessary adjustments should not be difficult. Subsidies in foreign trades are computed by comparing actual American operating costs on each route with estimated costs of the foreign competitors serving the same route or area. With no foreign competition present, no such comparison could be made for the Puerto Rican routes. Instead, operating cost differentials could be assumed to equal the average of all differentials recognized by the Maritime Administration in foreign trades. This would have to be provided in the act. It would correspond to the underlying purpose of eliminating from freight rates that part of operating costs which is due to the difference between actual costs and foreign costs generally.

In foreign trades, the reflection in freight rates of the subsidy contribution to operating costs is assumed to be assured by the competition of foreign flags. The absence of such competition in trade between Puerto Rico and the continental United States would make it necessary to assure the reflection of subsidies in freight rates by some other means. This would present no basic difficulty in regard to the regular liner services whose rates are subject to regulatory control by the Federal Maritime Board, provided that the Board's regulatory control is administered more effectively than has been true in the past. Legislation extending operating differential subsidy to domestic offshore trades would have to assure that freight rates allowed by the Board would automatically be lowered as operators' costs were reduced by subsidy. To make this assurance effective, the legislation should include both procedural and substantive provisions requiring clearly and specifically that the Board's control over tariffs be exercised with dispatch and in accord with generally accepted principles of rate regulation in the public interest.

A special situation arises in regard to bulk shipments carried under charter parties, which in foreign trades are also supported by Government payments under separate laws. No operating differential subsidies are being granted for tramp shipping in foreign trades. Instead, nearly all the bulk cargo available for such shipping under the American flag is provided by the legal requirement that at least 50 percent of all shipments financed by the U.S. Government under the foreign aid, agricultural surplus disposal, and similar programs be carried in vessels under the American flag. This assurance of cargo by legal requirement is quite similar to the cabotage restriction applying to Puerto Rico. However, where the assurance takes the form of the 50-50 provision, the U.S. Government pays all or part of the freight for the shipments on American-flag vessels, while it does not pay the freight for the corresponding shipments on foreign vessels. This procedure is a substitute for operating cost subsidy, although the Maritime Administration plays only an advisory role in carrying it out and other agencies make the actual payments.

Extension of subsidy to bulk service between Puerto Rico and the continental United States would be justified, since the use of American ships in this

service is required by law, as it is under 50-50 provisions and for the same reason; namely, to assist in maintaining an American merchant marine. The form of the subsidy would have to be different as the U.S. Government does not finance the cargo. It should not be too difficult, however, to work out a procedure under which a certain share of freight payments for shipments of this kind would be refunded by the U.S. Government. Instead of payment by the agency in charge of the foreign aid or similar program under which the cargo is shipped, payment would have to be made by the Maritime Administration which also would determine the appropriate subsidy rate. This subsidy rate could most conveniently be based on the ratio between operating cost differential and freight charges prevailing in Puerto Rican liner trades.

These arrangements would shift the burden of the operating cost differential from the economy of Puerto Rico to the economy of the entire United States. They would do no more than relieve the Puerto Rican people of a surcharge now unfairly imposed on them, arising solely from the purpose of the U.S. Government to maintain American merchant ships in operation. This purpose could continue to be served by the cabotage restrictions, while the unduly high freight charges for cargo between Puerto Rico and the continental United States could be reduced.

PUERTO RICO NEEDS ACCESS TO TECHNOLOGICAL IMPROVEMENT

While operating differential subsidy would effect the most obviously discriminatory burden on Puerto Rico's trade with the continental United States, it would remedy only part of the difficulty and would remedy it only for a short time. The benefit of operating differential subsidy would almost certainly be wiped out again in a few years if Puerto Rico were to receive no help in bridging the gap between the value of old vessels and the price of new ones. Without such help, the trade would continue to be served with the old ships; and, without the benefit of technological progress in vessel design and cargo handling, stevedoring expenses would continue to drive freight rates up, even if the differential in vessel operating costs were covered by subsidy.

Lasting relief depends on the access to technological progress which requires the introduction of modern vessels and cargo handling methods. Only limited progress in this direction can be expected so long as operators in trade between Puerto Rico and the continental United States are obligated to have their vessels built in American yards but receive no assistance in defraying the prohibitive cost of such construction. Several ways, however, are available to remedy this difficulty.

One way of facilitating the acquisition of new American-built vessels for the Puerto Rican services is indicated by the precedent set when the vessels now serving the routes were acquired under the Ship Sales Act of 1946 which placed operators in these trades on the same footing as those in foreign services. The same can be done with the current vessel replacement program by an appropriate amendments to the Merchant Marine Act of 1936.

Like operators in foreign trades, those serving Puerto Rico can be given the benefit of construction subsidies, trade-in privileges, and assistance in financing of vessel replacements. These benefits have been extended in connection with rebuilding of vessels designed for broken stowage into container ships as well as new construction. Both rebuilding and new construction might be helpful in service between Puerto Rico and the continental United States where potential savings in cargo handling are probably more important than those that can be obtained in vessel operations.

A considerable variety of methods for reducing cargo handling costs have been developed in recent years. Some of these methods—like the use of pallets and containers—have been introduced in Puerto Rico service as elsewhere. Three container ships are now in operation. These ships are rebuilt C-2 vessels and are not as well adapted to the most efficient operation possible as would be new vessels specifically designed for this kind of service. However, such new vessels would require a much larger investment. Those now in service were made possible only by the low price of war-built and rapidly obsolescing ships. The additional investment was limited to the cost of rebuilding. Nevertheless, the savings in operating expense which necessarily have occurred in the container-ship operation have thus far led to no reduction in freight charges. Evidently, improvisations will not solve the problem.

More extensive use of cost-reducing devices and introduction of additional improvements require new ship designs. Only practical experience can decide

which of the various proposed improvements will be most efficient. They cannot be put to the test of practical experience, however, if the entire investment has to be supplied by the operators and has to be supported by freight charges. A way must be found to finance the necessary investment without nullifying the savings due to lower operating costs. Federal financing assistance is needed—in this trade as in foreign service—if real progress is to be attained within the foreseeable future.

Federal assistance has, in some special cases, also been provided in another form. Vessels have been constructed for the account of the Maritime Administration and placed into service under bareboat charters to private operators at rates which the traffic could reasonably bear. This procedure could also be applied to the development of new vessel types designed for rapid and cost-saving cargo handling. For, while such vessels would find useful employment in trade between Puerto Rico and the continental United States, their design might also serve the national interest in other ways. It might help to revive coastwise and intercoastal shipment and it might assist in the solution of wartime logistic problems of the military services.

There are many precedents in maritime and air transportation for Government action to stimulate technological development in the interest of both the defense and the commerce of the United States. Without such action, progress toward more efficient cargo handling in maritime operations is bound to be slow. The logical place where such progress can be stimulated to greatest benefit—and, therefore, at lowest net cost—is in short-haul trades. However, Federal support of such development in coastwise and intercoastal shipping would raise difficult problems as it would directly affect the competitive balance between shipping on the one hand and railroads and trucking on the other.

No such problems would arise in noncontiguous domestic trades. At the same time, the ultimate result of experiments with new vessel types and cargo-handling methods in these trades would accrue to the benefit of the entire U.S. economy and might well prove of considerable military value. Thus, it would seem a logical step for the Federal Government to participate in the development of such new types and to make the ships available for service between Puerto Rico and the mainland.

Whether the Federal Government builds its own ships for use in Puerto Rico service or facilitates construction of new vessels and rebuilding of old ones by private operators is perhaps of secondary importance. It is of primary importance, however, that some means be found to remove the roadblock against technological progress which results from the requirement that American-built ships be used, although shipbuilding in American yards without Government assistance is prohibitively expensive and simply impractical.

PUERTO RICO ALSO REQUIRES PASSENGER SERVICE

Before the war and during the first few postwar years, regular passenger service of satisfactory quality was provided by one or two American shipping lines between Puerto Rico and the mainland. Today, passage is offered only in the few berths available on the cargo ships. Service by passenger vessels has become extinct as a victim of the same combination of economic trends and U.S. maritime laws which has made cargo freight unduly expensive.

Passenger ships under American and foreign flags do travel in Caribbean waters but—because of U.S. maritime laws—they cannot serve Puerto Rico. Foreign ships are precluded by the cabotage restrictions from carrying passengers between Puerto Rico and the continental United States. American shipping lines can receive subsidy only for service to foreign ports; they would lose part of their subsidy if they included service between Puerto Rico and the mainland in their schedules. Thus, a change in U.S. maritime laws would be needed to restore passenger ship operation on this route. Such a change should not meet with serious objections.

The routes between Puerto Rico and the continental United States might well be treated for passenger ship service as parts of foreign trade routes. That is, American ships might be allowed to carry passengers between Puerto Rico and the mainland on their foreign voyages without losing a proportion of their subsidy. At the same time, the cabotage restriction might be lifted from passenger service, so that foreign ships could also enter this trade. If both these measures were taken, Puerto Rico would have a good chance of obtaining some passenger service of good quality.

Turnaround service, however, would also seem essential. Such service would involve a sizable passenger ship or perhaps two. If the ship is to be of reasonably good quality and must be one built in an American yard, the capital investment clearly becomes so large that it cannot be supported by operating revenue alone. The problem is the same as that of American passenger ships in foreign trades where both operating and construction differential subsidies are substantially larger for passenger vessels than for freighters. In order to secure from a private operator the kind of passenger service needed between Puerto Rico and the continental United States, similar construction and operating differential subsidies would have to be made available. In the alternative, a suitable Government-owned vessel could be put into private operation in this service on appropriate charter and operating subsidy terms, or a carrier could be permitted to use a foreign-built ship with the benefit of operating differential subsidy.

RELIEF FOR PUERTO RICO WILL HELP MAINLAND INDUSTRY AND IMPROVE THE U.S.
BALANCE OF PAYMENTS

Measures to secure more adequate cargo and passenger shipping services between Puerto Rico and the mainland are amply justified by the need to remove an unfair and discriminatory burden. Technological progress to halt the continuing rise of freight rates is essential to avert a serious threat to the future development of the Commonwealth economy. But Puerto Rico will, by no means, be the sole beneficiary of Federal action to these ends. Much of the benefit will accrue to American industry.

Puerto Rico's purchases from mainland industry and agriculture are large. In the fiscal year 1960, Commonwealth merchandise receipts amounted to \$912 million and 83 percent of this total came from the mainland. On a per capita basis, Puerto Rico is the largest oversea market of the continental United States, bar none. Sales to this market now are seven times as large as they were in 1939-40. There is only one limit to their further rapid expansion: Puerto Rico's capacity to pay. Cargo rates have a very large impact on this limit of Puerto Rico's mainland purchases.

The direct impact of freight charges on goods for Puerto Rican consumption is most readily apparent. Every dollar saved on these charges will be spent on additional purchases and will immediately increase the market for mainland merchandise by a dollar. The impact of freight savings on raw materials and equipment for production and on Puerto Rican products sent to the mainland is more difficult to trace but is relatively larger. These freight charges in the first instance affect Puerto Rican income from production, mainly wage payments, as was shown in an earlier section of this memorandum; thus, a dollar saved on freight for these goods, also adds a dollar to Puerto Rican purchases from mainland industries.

In addition, however, lower cargo rates for producers' goods from the mainland and for shipments to continental markets will stimulate Puerto Rico's industrial development, while higher freight charges will stultify it. As industry increases, Puerto Rican incomes rise and with it the purchases from mainland producers. To trace these relationships in quantitative detail would be difficult. It is clear, however, that over a period of time a dollar saved in freight charges will result in far more than a dollar's worth of increase in payments to mainland industries.

Along with the people of Puerto Rico, mainland industries will benefit from any measures taken to lighten the excessive burden of freight charges. Also, along with the people of Puerto Rico, the numerous mainland industries supplying their needs will be seriously harmed unless the threat of higher and higher freight rates is eliminated.

Mainland industries have been and will certainly continue to be by far the most important suppliers of Puerto Rico. However, their share in the Puerto Rican market is apt to decline if there is no change in the maritime freight situation. While shipments from the continental United States bear the full weight of American shipping costs, supplies from foreign countries can be landed by foreign ships at relatively lower freight rates. Lower shipping costs have already been a factor in shifting most of Puerto Rico's extensive lumber purchases from the United States to Canada. Freight charges also may have contributed to the heavy inroads into the Puerto Rican market made more recently by European cars and trucks and some other manufactured consumer goods.

As the difference in the levels of American and foreign shipping costs continue to grow, foreign industries will tend to increase their share of Puerto Rican markets at the expense of the present mainland suppliers. The high shipping costs between Puerto Rico and the mainland at the same time weaken the ability of Puerto Rican producers to compete with foreign imports in mainland markets. As both mainland goods in Puerto Rico and Puerto Rican goods on the mainland are displaced by foreign imports, high shipping rates do double damage to the U.S. balance of payments. Conversely, relief from the excess burden on the cost of shipping services between Puerto Rico and the mainland will doubly improve the balance of payments.

SOLUTION OF PUERTO RICO'S PROBLEMS IS ESSENTIAL TO THE U.S. MERCHANT MARINE
AND THE NATIONAL DEFENSE

While mainland suppliers of the Puerto Rican market will benefit from a solution of Puerto Rico's shipping problem, such a solution is of far greater importance to the maritime carriers. To be sure, as matters now stand, these carriers enjoy complete protection against undercutting by foreign competition, as such competition is excluded by the cabotage restriction. In time, however, this protection will prove to be worthless if rising costs can be covered only by rising freight rates which are bound to inhibit the growth of traffic and eventually to strangle a now thriving business.

This dire outcome would seem inevitable if no remedial action is taken. The continuing trend toward higher productivity in American industry generally is bound to result in rising wages. Maritime and stevedoring labor cannot be excluded from this prospective uptrend in wages. At the same time, the old vessels now in service will get older and less efficient. With no buffer available in the form of either vessel replacement or operating subsidies, higher wages can be paid only out of higher freight charges, and higher freight charges are bound to slow down and eventually strangle the development of Puerto Rico. Instead of continuing to rise, cargo volume may decline, making it all the more difficult to cover costs of operation, thus leading to new rate increases, intensifying the process of spiraling decline and converting shipping profits into losses.

Reliance on the protection of cabotage may work for a few more years. In the end, it is bound to prove futile. If its productive equipment steadily declines in efficiency and is not replaced, no industry can survive, no matter how well it may be protected against competition. The cabotage restriction may keep competitors out but it will not supply new ships nor more efficient cargo handling methods. It will not keep freight charges at a level conducive to increasing, or even maintaining, the volume of traffic.

Timely replacement of the old vessels now in operation between Puerto Rico and the continental United States will eventually prove to be crucial to the survival of the carriers serving this trade. But, it also will be important to the American merchant marine generally. This short-haul and heavy-volume trade is particularly well suited to develop the means which may serve to raise productivity in maritime transport. None of the world's maritime fleets is as dependent on such a productivity increase as the American merchant marine with its inevitably high wage level. It can greatly benefit on all its trade routes from such technological progress in ship operation and cargo handling as may be achieved by efforts to make Puerto Rico service more efficient.

The urgency of making ship operations and cargo handling more efficient has in the last few years been increasingly emphasized by Government and industry experts, especially in the extensive studies recently completed under the auspices of the National Academy of Sciences ("Project Walrus"). As yet, however, little progress has been made. Numerous technical and human difficulties which stand in the way are likely to be overcome only by practical experimentation. The best opportunity for such experimentation is offered by the domestic off-shore services, the only substantial overseas trades with both terminals under American jurisdiction. If such experimentation were sponsored by the Federal Government, the results would not only help Puerto Rico, but would assist in raising the productivity of the entire American merchant marine.

Solution of Puerto Rico's shipping problems will also greatly benefit the national defense. In contrast to the U.S.-flag ships sailing the seven seas, vessels serving Puerto Rico are certain to be in or near a U.S. port in the event of an emergency, and will be almost immediately available for defense service and will be relatively far less vulnerable to enemy capture, destruction, or internment. Thus, it makes a great deal of difference whether they are up-to-

date and efficient or old and outmoded. From the point of view of national defense, there may well be a better case for Government action to assure replacement of old vessels in this trade than for Government support of the replacement program well underway in the foreign trades. Moreover, the technological improvements which are especially necessary on these short-haul routes, may find wider application in military sea transport, just as they may be helpful in maintaining a large merchant fleet in peacetime service to be available in case of a war emergency.

There are, thus, many reasons beyond the interest of the Puerto Rican people why a solution of Puerto Rico's present maritime problems is eminently in the public interest.

VARIOUS REMEDIES NEED TO BE INVESTIGATED

As technological progress in shipping during the postwar period has lagged behind the rapid advances made in manufacturing, agriculture, and some other industries, the United States has been faced with a continually widening gap between wages and productivity in maritime transportation. The consequent rise in cost would have made it impossible for the American merchant marine to stay in operation if it had not received special support. In the interest of the national defense and the commerce of the United States, support has been provided on foreign trade routes through a series of actions taken by the Federal Government, with the cost distributed widely among the taxpayers.

The segment of the American merchant marine serving Puerto Rico has benefited from only one of these actions, the Ship Sales Act of 1946 whose effects are now rapidly vanishing as the wartime vessels become obsolete. Otherwise, the Federal Government has relied on the cabotage restriction to maintain this segment of the merchant marine in operation, as if the rising costs resulting from the gap between maritime productivity and technological progress in other industries were a handicap only in competition with foreign operators. In reality, however, the cost rise resulting from this productivity gap creates a burden wherever maritime transport under the U.S. flag is used. Unlike the former mainland users of maritime transport in coastwise and intercoastal service Puerto Rico cannot shift to land transport; and unlike the users of maritime transport in foreign trade, it does not find this special burden assumed by the Federal Government and widely distributed among the taxpayers.

The burden on the Puerto Rican people is, as has been shown, many times heavier than the burden on the mainland taxpayers. The clearly foreseeable further increase of this burden in the years to come threatens to strangle Puerto Rico's economic development. It thus also threatens the continued expansion, and perhaps even the maintenance, of maritime traffic between Puerto Rico and the continental United States. Yet, viable and growing U.S.-flag operation in this service is at least as important to the national defense as on any foreign route, entirely apart from the national interest in the continued improvement of Puerto Rico's economy.

The most serious of the problems created for Puerto Rico by present U.S. maritime policy is the lack of any prospect of replacement for the aging vessels now in service. This replacement might be made possible by following the precept of the Ship Sales Act of 1946 and extending to Puerto Rico services the financial replacement assistance available to operators in foreign trade. Alternatively, vessels suitably designed for Puerto Rico service might be built by the Federal Government and made available on terms the traffic can bear, or the operators might be permitted to have some new vessels built abroad. Any one of these measures, or any combination of them might be used to assure some substantial improvement in the prospects of fleet replacement.

The problem raised by the current high rate level also could be tackled in several alternative ways. Operating subsidy might be made available in the manner previously outlined in this memorandum for all Puerto Rican services. Carriers serving Puerto Rico in the course of foreign voyages could also be allowed to perform this service without deduction from their operating subsidy. This could be done without removing the cabotage restrictions. On the other hand, removal of these restrictions might, at least in part, substitute for operating subsidy. In any event, either removal of cabotage restrictions or introduction of operating subsidy might be employed to assure Puerto Rico of such services as are now entirely lacking both on certain cargo routes and on the most essential passenger routes.

Thus, a variety of means are available by which to modify those features of U.S. maritime policy which combined with the productivity gap to create Puerto

Rico's maritime problems. These policies were never intended to create the problems that have arisen, let alone the threat of more serious difficulties looming ahead. Yet, this has been their effect and changes are now needed. To be sure, proposals to revise any feature of the maritime policy of the United States must be appraised in the light of all the affected national interests. Fortunately, a variety of remedies is available to cure the difficulties now affecting and threatening maritime commerce between Puerto Rico and the mainland. Some suitable combination of such remedies surely can be fitted into a national program.

APPENDIX A

Computation of operating costs differential, Puerto Rico-Atlantic/Gulf Services, 1957

	Bull	Lykes	Waterman	Total, 3 carriers
Cargo carried (long tons).....	602,097	186,220	298,831	1,087,148
Freight revenue.....	\$20,686,957	\$3,787,724	\$3,114,991	\$32,539,592
Freight per long ton.....	34.36	20.07	27.16	29.93
Operating cost items:				
Wages.....	2,569,702	1,020,298	1,053,878	4,643,878
Subsistence.....	174,935	66,825	84,245	326,005
Repairs.....	344,577	333,529	349,675	1,027,781
Insurance, hull and machinery.....	157,801	63,040	61,395	282,236
Insurance, protection and indemnity.....	757,690	123,855	239,312	1,120,857
Operating cost differentials:				
Wages, 71.9 percent.....	1,847,616	733,594	757,738	3,338,948
Subsistence, 21.4 percent.....	37,436	14,301	18,027	69,764
Repairs, 30.5 percent.....	105,096	101,726	106,650	313,472
Insurance, hull and machinery, 18 percent.....	28,404	11,347	11,051	50,802
Insurance, protection and indemnity, 55 percent.....	416,730	68,120	131,622	616,472
Total differential.....	2,435,282	929,088	1,015,573	4,389,458
Differential per long ton.....	4.05	4.99	3.40	4.04
Differential as percent of freight.....	11.77	24.86	12.52	13.49

NOTE.—Data on cargo carried, freight revenue, and operating cost items are from exhibits of the carriers in docket No. 807. Data from Bull have been adjusted to eliminate expenses of the period when a strike interrupted service. Data for Alcoa have been omitted as Puerto Rico service is confined to the southbound legs of Alcoa voyages and the record does not contain sufficient information to judge whether allocations of cost between southbound and northbound legs are appropriate. Both the adjustment of Bull figures and the omission of Alcoa reduce the computed operating cost differential.

APPENDIX B

THE VOLUME OF DRY CARGO BETWEEN PUERTO RICO AND THE CONTINENTAL UNITED STATES

The best available statistics are published annually by the Corps of Engineers in "Waterborne Commerce of the United States." The latest available issue covers calendar year 1959. It contains complete data on traffic in the ports of San Juan, Ponce, and Mayaguez, broken down by commodities and showing separately receipts and shipments in "coastwise" trade (i.e., trade between Puerto Rico and the continental United States), imports and exports in foreign trade, and intraterritory shipments (including shipments between Puerto Rico and the Virgin Islands). The data on "coastwise" trade may be summarized as follows:

Mainland cargo traffic of 3 major Puerto Rican port, 1959

[In thousands of short tons]

	San Juan	Ponce	Mayaguez	Total
Receipts from mainland:				
Total cargo.....	1,250	195	143	1,588
Tanker cargo ¹	36			36
Dry cargo.....	1,214	195	143	1,553
Shipments to mainland:				
Total cargo.....	912	445	79	1,436
Tanker cargo ¹	484	40	52	576
Cement ²		287		287
Dry cargo.....	428	118	27	573
Dry cargo in and out.....	1,642	313	170	2,125

¹ Motor fuel, gas oil, kerosene, residual fuel oil, and inedible molasses.² Shipped by private carrier.

Shipments and receipts at other Puerto Rican ports are not covered in "Waterborne Commerce." However, a special report of the Corps of Engineers to the Puerto Rico Ports Authority shows dry cargo receipts of 59,462 tons and shipments of 128,105 tons at the port of Guanica and dry cargo receipts of 733 tons and shipments of 158,653 tons at the port of Jobos. In addition, a study of the U.S. Department of Agriculture shows shipments of 265,000 tons of sugar at the port of Aguadilla.

Thus, total dry cargo movements between the continental United States and Puerto Rico amounted to 2,738,000 tons in 1959.

