Reduction Act and have been assigned OMB control number 2070–0091.

List of Subjects in 40 CFR Part 763

Environmental protection, Asbestos, Asbestos in schools (AHERA), Hazardous substances, Reporting and recordkeeping requirements, State and local governments, Worker protection.

Dated: March 30, 1995.

Jane Saginaw,

Regional Administrator, Region VI.

[FR Doc. 95–8873 Filed 4–10–95; 8:45 am]

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DEPARTMENT OF TRANSPORTATION

Office of the Secretary

Coast Guard

46 CFR Parts 401, 403, and 404

[OST Docket No. 50248]
[CGD 92–072]

RIN 2105–AC21

Great Lakes Pilotage Rate Methodology

AGENCY: Office of the Secretary, DOT.

ACTION: Final rule; request for comments.

SUMMARY: The Department of Transportation (the Department) is amending the regulations concerning Great Lakes pilotage by amending the procedures for determining Great Lakes pilotage rates, and revising the financial reporting requirements mandated for Great Lakes pilot associations. The purpose of these changes is to improve the ratemaking process. This final rule does not change the existing Great Lakes pilotage rates and charges.

DATES: This rule is effective on June 12, 1995. Comments must be received on or before May 11, 1995. Late-filed comments will be considered only to the extent practicable.

ADDRESSES: Comments should be sent, preferably in triplicate, to Docket Clerk, OST Docket No. 50248, U.S. Department of Transportation, 400 7th St. SW., room PL–401, Washington, DC 20590. Comments will be available for inspection at this address from 9 a.m. to 5:30 p.m., Monday through Friday. Commenters who wish the receipt of their comments to be acknowledged should include a stamped, self-addressed postcard with their comments. The Docket Clerk will date-stamp the postcard and mail it back. Unless otherwise indicated, documents referred to in this preamble are also available for inspection or copying at this address. Comments should not be sent to the Coast Guard docket.

FOR FURTHER INFORMATION CONTACT: Scott A. Poyer, Project Manager, Merchant Vessel Personnel Division, Office of Marine Safety, Security and Environmental Protection (G-MVP/12) room 1210, U.S. Coast Guard Headquarters, 2100 Second Street, SW., Washington, DC 20593–0001, (202) 267–6102, or Steven B. Farbman, Office of the Assistant General Counsel for Regulation and Enforcement, 400 7th St. SW., room 10424, Washington, DC 20590, (202) 366–9306.

Regulatory History

On December 7, 1988, the Department of Transportation published the Great Lakes Pilotage Study Final Report (1988 DOT Pilotage Study). The study revealed weaknesses in accounting for the expenses incurred by the pilot associations and the need to formally establish the factors used in establishing pilotage rates. On April 25, 1990, the Coast Guard published a final rule (55 FR 17580) establishing improved audit requirements and general guidelines and procedures to be followed in ratemaking (CGD 92–072).

In May 1990, the Inspector General (IG) for the Department of Transportation initiated an audit of Coast Guard oversight of Great Lakes pilotage. The final report of the audit (Audit of the U.S. Coast Guard's Oversight and Management of the Great Lakes Pilotage Program), detailing further issues affecting the basis for Great Lakes pilotage rates, was issued on December 14, 1990.

On August 2, 1991, a DOT Task Force was formed to: (1) Develop an interim rate adjustment; and (2) establish a new pilotage ratemaking methodology. On June 5, 1992, an interim rate increase was published (CGD 89–104). The DOT Task Force then developed a new pilotage ratemaking methodology, which the Coast Guard published in a notice of proposed rulemaking (NPRM) (59 FR 17303) dated April 12, 1994.

The NPRM proposed to amend the Great Lakes pilotage regulations by establishing new procedures for determining Great Lakes pilotage rates and revising the financial reporting requirements mandated for Great Lakes pilot associations (CGD 92–072). The NPRM also announced a public hearing that was held in Cleveland, OH on May 20, 1994. The comment period for the NPRM ended on July 11, 1994.

In response to the NPRM and the public hearing, the Coast Guard received 31 comments and two requests for additional public meetings to explain the proposals contained in the NPRM. In the **Federal Register** (59 FR 18774) on April 20, 1994, the Coast Guard announced that it would conduct two public meetings. The first public meeting was held in Chicago, IL on May 3, 1994. The second public meeting was held in Massena, NY on May 5, 1994.

The Coast Guard also received one request to extend the comment period for the NPRM. Because the comment period for the NPRM was 90 days, the Coast Guard determined that there was sufficient time to submit comments. Therefore, the comment period was not extended.

Background and Purpose

Under the Great Lakes Pilotage Act of 1960 (Pub. L. 86–555, 46 U.S.C. 9301 *et seq.*) (the Act), vessels of the United States operating on register and foreign vessels must engage a U.S. or Canadian registered pilot when traversing the waters of the Great Lakes. The Act vests the Secretary of Transportation with responsibility for setting pilotage rates. Section 9303 of the Act provides that the Secretary shall prescribe by regulation rates and charges for pilotage services, giving consideration to the public interest and the costs of providing the services. This authority, except for the authority to enter into, revise or amend arrangements with Canada, has been delegated to the Commandant of the Coast Guard by 49 CFR 1.46(a). This authority has been further delegated to the Director, Great Lakes Pilotage (the Director).

Currently, the navigable waters of the Great Lakes are divided into eight pilotage areas. United States registered pilots, along with their Canadian counterparts, provide pilotage services in areas 1, 2, 4, 5, 6, 7, and 8. Pilotage area 3 (the Welland Canal) is currently a wholly-Canadian area where only Canadian pilots provide services. Pilotage areas 2, 4, 6, and 8 are ‘‘undesignated waters.’’ Pilotage areas 1, 5, and 7 are ‘‘designated waters.’’ Pilots are required to direct navigation of vessels in designated waters. Pilots are required to be on board and available to direct navigation in undesignated waters. The seven U.S. pilotage areas are grouped together into three pilotage districts. District 1 consists of areas 1 and 2. District 2 consists of areas 4 and 5. District 3 consists of areas 6, 7, and 8. Each district has its own pilot association.

Section 9305 of the Pilotage Act provides that the Secretary of Transportation, subject to the concurrence of the Secretary of State, may make agreements with the appropriate agency of Canada to prescribe joint or identical rates and charges. The latest Memorandum of Arrangements between the United States and Canada, dated January 18, 1977, specifies that the Secretary of Transportation of the United States of America and the Minister of Transport of Canada will establish regulations imposing identical rates. A copy of this Memorandum of Arrangements is available in the docket and may also be obtained by writing to Mr. Scott Poyer at the address listed under **FOR FURTHER INFORMATION CONTACT**, above. In the past, consultations between the United States and Canada resulted in nominally identical U.S. and Canadian rates.

However, there are differences in the cost bases and in the operating organizations of the U.S. and Canadian pilots, particularly with regard to pilot compensation. These differences need to be taken into account in reaching identical U.S. and Canadian rates. As a result, the ratemaking methodology contained in this final rule would not translate directly into new rates, but rather would form the basis for proposals to be negotiated with Canada.

Discussion of Comments and Changes

Although the Coast Guard issued the NPRM under authority delegated to the Commandant by the Secretary, the Secretary is issuing the final rule. Under 49 CFR 1.43(a), the Secretary may exercise powers and duties delegated or assigned to officials other than the Secretary.

Because the Secretary is issuing this final rule, the Department is consolidating Coast Guard Docket No. 92–072 into OST Docket No. 50248. All further pleadings should be filed in the new docket at the docket address listed above.

The Coast Guard received 31 comments on the NPRM. Twenty comments were from Great Lakes Pilots, Great Lakes Pilot Associations, or employees of these associations. Six comments were from shippers, ports, and associations representing the Great Lakes maritime industry. Five comments were from unions or professional organizations that represent pilots. Some of the comments addressed issues that were not the subject of this rulemaking. The Department is responding only to those comments relating to this rulemaking.

All comments were carefully considered, and in response to the comments significant changes have been made to the proposals that were published in the NPRM. The NPRM proposed changes to 46 CFR part 403, which deals with accounting and financial reporting requirements, and 46 CFR part 404, which details ratemaking procedures.

Most of the comments criticized the NPRM for being overly complex and unwieldy. In response to this criticism, the regulations that were proposed in the NPRM have been cut by approximately two thirds, with no sacrifice of fairness or substance. Accounting requirements have been streamlined for easier use, financial reporting requirements have been reduced, and the proposed ratemaking methodology has been revised to make it less complex.

The NPRM elements that received the strongest objections from the public were proposals to change the way pilotage rates are charged on the Great Lakes. Almost everyone who commented on the proposed rule objected to the proposals to create a class of ‘‘ancillary services’’ and to recalculate point-to-point pilotage charges based on hourly fees. These proposals were found in Step 7 of appendix A to part 404. The majority of commenters felt that the proposals for hourly pilotage fees would degrade safety by creating an incentive for vessels to go faster in order to avoid or reduce pilotage costs. Commenters also objected to labeling some pilotage services such as docking and undocking as ‘‘ancillary services’’ and allowing fees for these services to be set purely at the discretion of the Director. There were concerns that purely discretionary rates would not be predictable for shippers or pilots.

In response to the comments from pilots, shippers, unions and most other commenters, the NPRM proposal to charge fees on an hourly basis has been modified. The Department agrees with the expressed concerns regarding undue complexity and possible disincentives for operational safety, and has therefore rewritten Step 7 of appendix A to part 404. This final rule retains the current method for charging pilotage rates to various users, which specifies charges for specific travel segments. If concerns are raised in the future regarding the equity of the way in which pilotage rates are charged, this issue may be reopened. However, no changes will be made without a proceeding that provides for public involvement.

There were many objections from pilots and shippers to the proposal that the timing of rate reviews be determined by the Director of Great Lakes Pilotage. Several alternatives were suggested, but most comments indicated that it would be more appropriate if a rate review were conducted at least every one, two, or three years in order to keep pilotage rates current. The Department agrees with these comments. The provision in 46 CFR 404.1(b), which gave the Director authority to determine the timing of rate reviews, has been revised in response to the public comments received. Section 404.1(b) now requires the Director to conduct a detailed audit of pilot association expenses and use the ratemaking procedures in appendix A of part 404 to set base pilotage rates at least once every five years. The Director of Great Lakes Pilotage will initiate the new methodology as soon as possible after the effective date of this rule using the most current audit reports available. If interested parties request reviews more often than once every five years, the Director can review the request, and conduct a special audit and ratemaking if the Director concludes that a reasonable basis for conducting a review has been established.

In the intervening years between the five-year or special audits, pilotage rates proposed for coordination with Canada will be reviewed annually using a simplified procedure detailed in appendix C to part 404. This annual review procedure addresses public comments that a less complicated ratemaking process would be faster and less burdensome on all parties.

During the regular five-year audit of the Great Lakes pilot associations and the corresponding rate review, the Director will calculate an ‘‘expense multiplier’’ for each pilot association using the most recent regular and/or special audit data. This expense multiplier is the ratio of all other expenses, including a return element, to pilot compensation expense in unit cost terms for the base period analyzed. When target pilot compensation is determined for a prospective annual rate period, total economic costs can be easily determined by increasing such pilot compensation by the multiplier. Use of this ratio avoids the need to recalculate other expenses and the return element each year in order to review the rates. Moreover, since this review procedure focuses on changes in unit costs, i.e., total economic costs per bridge hour, between the base period and the new rate period, the need to project revenues for the new period is also avoided. Finally, this calculation will not change the rate structure; it will merely change proposed rates uniformly by the percentage change in unit costs.

Most pilots, and organizations representing pilots, commented on the NPRM's proposal to continue the Department policy of maintaining income comparability between Great Lakes Registered Pilots, and masters/chief mates on Great Lakes vessels. This policy was established as a result of the

1988 DOT Pilotage Study, which examined many alternatives and selected the master/chief mate target for pilot compensation. Commenters believed pilots should earn more than masters/chief mates. Among the many alternatives proposed by commenters were: Comparability with State pilots; comparability with Canadian pilots; automatic cost-of-living allowances; overtime bonuses; and work hour/travel time/rest time adjustments. No single alternative appeared to represent a consensus. After considering all the alternatives, the Department is keeping the pilot compensation methodology proposed in the NPRM. This is fully consistent with the recommendation in the 1988 DOT Pilotage Study, which states, ''The study team believes that pilot compensation should be tied to the local economy. The use of local masters and mates pay scales has the important impact of tying pilot compensation to regional industry pay levels. Salaries of pilots, like those of teachers, physicians, lawyers, and other professionals, are tied to the fluctuations of supply and demand for their services in their particular locality. In this fashion, Great Lakes pilots share in the fortunes of the Great Lakes.'' Commenters offered no new information that alters this assessment.

There were several objections from Great Lakes Pilot Associations and their employees to the proposed new 46 CFR part 403, as published in the NPRM. Commenters objected that this part was unduly burdensome for small pilot associations and should be eliminated in order to streamline the regulations, and reduce costs to the pilot associations. After careful consideration, and in light of the lesser requirements of the procedures for the annual reviews of base pilotage rates, the Department agrees with the public comments and has greatly streamlined part 403. Specific account numbers and detailed account descriptions have been removed in favor of a requirement that financial records of the association be kept in accordance with generally accepted accounting principles. Associations are required to complete and retain annual financial statements and an audit by a certified public accountant. However, reporting requirements have been reduced to require that audits only be forwarded to the Director once every five years, or by special request. At the same time, associations must keep in mind that answers challenging proposed cost disallowances or other applications of the ratemaking methodology, as well as *ad hoc* requests for rate reviews, must be based on full and adequate financial records.

Two commenters from two of the three Great Lakes Pilot Associations objected to the proposed requirement that the financial records of the associations be retained for a period of ten years, and proposed an alternative three-year requirement that would conform to Internal Revenue Service (IRS) requirements. The Department does not agree. The Department does not use the financial records of the pilot association for the same purpose as the IRS. On several occasions the Director has accessed historical data to ensure that only reasonable expenses have been included in ratemaking calculations. For this reason, the Department is adopting the proposed requirement regarding the 10-year retention of financial records.

The Department anticipates implementing all the rate reviews under the methodologies adopted in this rulemaking proceeding through additional public procedures. Following a review, the Department will publish its tentative findings and any proposed rate changes, and it will request the comment of interested parties on the calculations. (Comments seeking reconsideration of our rate methodology will not be addressed through this process.) The Department will then seek to coordinate any proposed change in rates, as modified by any warranted corrections, with Canadian authorities. Following the coordination process, the Department will establish final rates to be effective for the designated future rate period. Both the proposed and final rate documents will be served on the pilot associations and other interested persons requesting in writing to be placed on the service list in this docket; both documents will also be published in the **Federal Register**.

Although the Coast Guard received no comments on the section pertaining to the uniform pilot's source form, the Department is making a slight modification to clarify that the format for source forms is approved by the Director of Great Lakes Pilotage and issued by the pilot associations. The ''Pilot's Source Form—Great Lakes Pilotage,'' referred to in the NPRM, is not an official United States Government form.

The Department is also removing several subparts as part of our streamlining of the accounting regulations. Subparts B, C, D, and G, as contained in the NPRM, have been eliminated, and subparts E, F, and H have been redesignated subparts B, C, and D, respectively.

There were several objections from employees and representatives of the District 3 pilot association to the proposed revision to 46 CFR 404.05, which provided that profit sharing expenses not be recognized for ratemaking purposes. Commenters argued that profit sharing for employees of the District 3 pilot association is part of their recognized pension plan, and employees of this association would be unfairly penalized if this proposal were adopted. The Department agrees and has changed the wording of the proposed paragraph to allow reasonable profit sharing expenses for non-pilot employees only. Profit sharing that benefits pilots will be considered part of pilot compensation.

Several comments from both pilots and shippers, as part of the overall objection to the complexity of the proposal, argued that the market-equivalent Return-on-Investment (ROI) provisions of 46 CFR 404.5(a)(4), Step 5 of appendix A, and the formulas contained in appendix B should not be included. Some members of the public objected to allowing a return on the capital that pilots had invested in their pilot associations on the grounds that this would encourage pilots to make investments that were unrelated to pilotage, and thereby increase pilotage fees. Other commenters believed that the ROI provisions made the ratemaking formula in appendix A too complicated. The Department carefully considered these comments and believes that we have significantly reduced the proposal's complexity and burden. However, a return element is an important component of cost-based rate methodologies. Rates that have been set without a return element have been vulnerable to legal challenge and do not meet the goals of the investigations and audits that underlie this rulemaking. Also, in order to negotiate with the Canadians we must have rates that can withstand scrutiny as to their conformity to sound ratemaking principles. The Department believes it is only fair to allow pilots a return on the capital they invest. The Department also believes that sufficient safeguards against excessive investment are in place because 46 CFR 404.5(a)(4) specifically stipulates that capital that is not necessary and reasonable for the provision of pilotage services will not be allowed for ratemaking purposes.

Final Rule With Request for Comments

The Department is issuing this document as a final rule but is also providing an opportunity for comment. This rulemaking document is within the scope of the NPRM. The primary purposes of the final rule have not changed from the NPRM stage: to standardize the financial reporting of Great Lakes pilotage associations, and to clarify the methodology to be used in future ratemakings. We believe that we have responded to all the concerns expressed in the comments to the NPRM. Nevertheless, we want to give the public an additional opportunity to present its views to us, given the changes that we have made to the NPRM. Accordingly, even though the final rule will be effective on June 12, 1995, we will consider any new matters presented to us during the 30-day comment period. We will make revisions to this rule if we believe they are warranted.

Executive Order 12866

This rule is a significant regulatory action under section 3(f) of Executive Order 12866 and has been reviewed by the Office of Management and Budget under that order. It is significant under the regulatory policies and procedures of the Department of Transportation (44 FR 11040; February 26, 1979) because a rulemaking affecting the setting of pilotage rates is controversial and of significant interest to the public.

The Department expects the economic impact of this rule to be minimal. This rule does not represent a significant departure from the current ratemaking process, and there are no expected increases in costs. Therefore, a full regulatory evaluation is not necessary.

Small Entities

Under the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*), the Department must consider whether this final rule will have a significant economic impact on a substantial number of small entities. ''Small entities'' include independently owned and operated small businesses that are not dominant in their field and that otherwise qualify as ''small business concerns'' under section 3 of the Small Business Act (15 U.S.C. 632). This final rule should have little or no impact on small entities that pay pilotage rates or that receive income from pilotage rates. Because it expects the impact of this proposal to be minimal, the Department certifies under 5 U.S.C. 605(b) of the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*) that this final rule will not have a significant economic impact on a substantial number of small entities.

Collection of Information

This rule contains collection-of-information requirements. The Department has submitted the requirements to the Office of Management and Budget (OMB) for review under section 3504(h) of the Paperwork Reduction Act (44 U.S.C. 3501 *et seq.*), and OMB has approved them. The part numbers are parts 401 and 403 and the corresponding OMB approval number is OMB Control Number 2115–0616.

Federalism

The Department has analyzed this final rule under the principles and criteria contained in Executive Order 12612, and has determined that this rule does not have sufficient federalism implications to warrant the preparation of a Federalism Assessment. Under 49 CFR 1.46(a) the Secretary delegates to the Commandant of the authority to carry out the Great Lakes Pilotage Act of 1960, as amended, except the authority to enter into, revise, or amend arrangements with Canada.

State action addressing pilotage regulation is preempted by 46 U.S.C. 9306, which provides that a State or political subdivision of a State may not regulate or impose any requirement on pilotage on the Great Lakes.

Environment

The Department considered the environmental impact of this final rule and concluded that under section 2.B.2 of Commandant Instruction M16475.1B, this rule is categorically excluded from further environmental documentation. The rule is procedural in nature because it deals exclusively with ratemaking and accounting procedures. Therefore, this is included in the categorical exclusion in subsection 2.B.2.1,—Administrative actions or procedural regulations and policies that clearly do not have any environmental impact. A Categorical Exclusion Determination has been placed in the docket.

List of Subjects in 46 CFR Parts 401, 403, and 404

Administrative Practice and Procedure, Great Lakes, Navigation (water), Penalties, Reporting and Recordkeeping Requirements, Seamen.

For the reasons set out in the preamble, the Department proposes to amend parts 401, 403, and 404 of title 46 of the Code of Federal Regulations as follows:

PART 401—[AMENDED]

1. The authority citation for part 401 is revised to read as follows:

Authority: 46 U.S.C. 6101, 7701, 8105, 9303, 9304; 49 CFR 1.45, 1.46. 46 CFR 401.105 also issued under the authority of 44 U.S.C. 3507.

2. In § 401.110 the introductory text of paragraph (a) and paragraph (a)(9) are revised, and paragraph (a)(16) is added to read as follows:

§ 401.110 Definitions.

(a) As used in this chapter:

* * * * *

(9) *Director* means Director, Great Lakes Pilotage. Communications with the Director may be sent to the following address: Director, Great Lakes Pilotage (G–MVP–7), 2100 2nd St., SW., Washington, DC 20593.

* * * * *

(16) *Association* means any organization that holds or held a Certificate of Authorization issued by the Director of Great Lakes Pilotage to operate a pilotage pool on the Great Lakes.

3.–4. Part 403 is revised to read as follows:

PART 403—GREAT LAKES PILOTAGE UNIFORM ACCOUNTING SYSTEM

Subpart A—General

Subpart B—Inter-Association Settlements

Subpart C—Reporting Requirements

Subpart D—Source Forms

Authority: 46 U.S.C. 8105, 9303, 9304; 49 CFR 1.46.

Subpart A—General

§ 403.100 Applicability of system of accounts and reports.

Each Association shall keep its books of account, records and memoranda, and make reports to the Director in accordance with the guidelines of the Generally Accepted Accounting Principles (GAAP) issued by the Financial Accounting Standards Board. These guidelines are available by writing to the Director, Great Lakes Pilotage at the address listed in § 401.110(a)(9) of this chapter.

§ 403.105 Records.

(a) Each Association shall maintain the general books of account and all books, records, and supporting memoranda in such manner as to provide, at any time, full information relating to any account. Supporting memoranda must provide sufficient information to verify the nature and character of each entry and its proper classification.

(b) Each Association shall maintain all books, records and memoranda in a manner that will readily permit audit and examination by the Director or the Director's representatives. All books, records and memoranda shall be protected from loss, theft, or damage by fire, flood or otherwise, and shall be retained for 10 years unless otherwise authorized by the Director.

§ 403.110 Accounting entities.

Each Association shall be a separate accounting entity. However, the records shall be maintained with sufficient particularity to allocate items to each pilotage pool operation or nonpool operation and to support the equitable proration of items that are common to two or more pilotage pools.

§ 403.115 Accounting period.

Each Association subject to this part shall maintain its accounts on a calendar year basis unless otherwise approved by the Director.

§ 403.120 Notes to financial statements.

(a) All matters that are not clearly identified in the body of the financial statements of the Association, but which may materially influence interpretations or conclusions that may reasonably be drawn in regard to financial condition or earnings of the Association, shall be clearly and completely stated as footnotes to the financial statements.

(b) Financial items that are not otherwise required to be reported in the Association financial statements, but which may affect ratemaking calculations, are required to be reported to the Director in the notes to the financial statements. Any financial items that are not reported to the Director will not be considered by the Director during ratemaking procedures contained in part 404 of this chapter.

Subpart B—Inter-Association Settlements

§ 403.200 General.

Each Association that shares revenues and expenses with the Canadian Great Lakes Pilotage Authority (GLPA) shall submit settlement statements regarding these activities. The settlement statements shall be completed in accordance with the terms of agreements between the United States and Canada and guidance from the Director of Great Lakes Pilotage.

Subpart C—Reporting Requirements

§ 403.300 Financial reporting requirements.

(a) General:

(1) The financial statements shall list each active account, including subsidiary accounts.

(2) The financial statements, together with any other required statistical data, shall be submitted to the Director within 30 days of the end of the reporting period, unless otherwise authorized by the Director.

(3) An officer of the Association shall certify the accuracy of the financial statements.

(b) Required Reports:

(1) Every five years, or when specially requested by the Director, each Association shall furnish the Director the Association's annual financial statements audited in accordance with generally accepted auditing standards by an independent certified public accountant.

(2) Each Association shall furnish the Director a copy of all settlement statements annually.

Subpart D—Source Forms

§ 403.400 Uniform pilot's source form.

(a) Each Association shall record pilotage transactions on a form approved by the Director. The approved form shall be issued to pilots by authorized United States pilotage pools.

(b) Pilots shall complete forms in detail as soon as possible after completion of assignment and return the entire set to the dispatching office, together with adequate support for reimbursable travel expenses.

(c) Upon receipt by the Association, the forms shall be completed by insertion of rates and charges as specified in part 401 of this chapter.

(d) Copies of the form shall be distributed as follows:

(1) Original to accompany invoice;

(2) First copy to Director;

(3) Second copy to billing office for accounting record;

(4) Third copy to pilot's own Association for pilot's personal record;

(5) Fourth copy to corresponding Canadian Association or agency for office use.

(e) Associations shall account by number for all pilot source forms issued.

5. Part 404 is revised to read as follows:

PART 404—GREAT LAKES PILOTAGE RATEMAKING

Sec.

Authority: 46 U.S.C. 8105, 9303, 9304; 49 CFR 1.46.

§ 404.1 General ratemaking provisions.

(a) The purpose of this part is to provide guidelines and procedures for Great Lakes pilotage ratemaking. Included in this part are explanations of the steps followed in developing a pilotage rate adjustment, the analysis used, and the guidelines followed in arriving at the pilotage rates contained in part 401 of this chapter.

(b) Great Lakes pilotage rates shall be reviewed and, if necessary, adjusted annually in accordance with the procedures detailed in appendix C to this part. At least once every five years the Director shall complete a thorough audit of pilot association expenses and establish pilotage rates in accordance with the procedures detailed in § 404.10. An interested party or parties may also petition the Director for a review at any time. The petition must present a reasonable basis for concluding that a review may be warranted. If the Director determines, from the information contained in the petition, that the existing rates may no longer be reasonable, a full review of the pilotage rates will be conducted. If the full review shows that pilotage rates are within a reasonable range of their target, no adjustment to the rates will be initiated.

§ 404.5 Guidelines for the recognition of expenses.

(a) The following is a listing of the principal guidelines followed by the Director when determining whether expenses will be recognized in the ratemaking process:

(1) Each expense item included in the rate base is evaluated to determine if it is necessary for the provision of pilotage service, and if so, what dollar amount is reasonable for that expense item. Each Association is responsible for providing the Director with sufficient information to show the reasonableness of all expense items. The Director will give the Association the opportunity to defend any expenses that are questioned. However, subject to the terms and conditions contained in other provisions of this part, expense items that the Director determines are not reasonable and necessary for the provision of pilotage services will not be recognized for ratemaking purposes.

(2) In determining reasonableness, each expense item is measured against one or more of the following:

(i) Comparable or similar expenses paid by others in the maritime industry,

(ii) Comparable or similar expenses paid by other industries, or

(iii) U.S. Internal Revenue Service guidelines.

(3) Lease costs for both operating and capital leases are recognized for ratemaking purposes to the extent that they conform to market rates. In the absence of a comparable market, lease costs are recognized for ratemaking purposes to the extent that they conform to depreciation plus an allowance for return on investment (computed as if the asset had been purchased with equity capital). The portion of lease costs that exceed these standards is not recognized for ratemaking purposes.

(4) For each Association, a market-equivalent return-on-investment is allowed for the net capital invested in the Association by its members. Assets subject to return on investment provisions are subject to reasonableness provisions. If an asset or other investment is not necessary for the provision of pilotage services, the return element is not allowed for ratemaking purposes.

(5) For ratemaking purposes, the revenues and expenses generated from Association transactions that are not directly related to the provision of pilotage services are included in ratemaking calculations as long as the revenues exceed the expenses from these transactions. For non-pilotage transactions that result in a net financial loss for the Association, the amount of the loss is not recognized for ratemaking purposes. The Director reviews non-pilotage activities to determine if any adversely impact the provision of pilotage service, and may make ratemaking adjustments or take other steps to ensure the provision of pilotage service.

(6) Medical, pension, and other benefits paid to pilots, or for the benefit of pilots, by the Association are treated as pilot compensation. The amount recognized for each of these benefits is the cost of these benefits in the most recent union contract for first mates on Great Lakes vessels. Any expenses in excess of this amount are not recognized for ratemaking purposes.

(7) Expense items that are not reported to the Director by the Association are not considered by the Director in ratemaking calculations.

(8) Expenses are appropriate and allowable if they are reasonable, and directly related to pilotage. Each Association must substantiate its expenses, including legal expenses. In general, the following are not recognized as reasonable expenses for ratemaking purposes:

(i) Undocumented expenses;

(ii) Expenses for lobbying;

(iii) Expenses for personal matters;

(iv) Expenses that are not commensurate with the work performed; and

(v) Any other expenses not directly related to pilotage.

(9) In any Great Lakes pilotage district where revenues and expenses from Canadian pilots are commingled with revenues and expenses from U.S. pilots, Canadian revenues and expenses are not included in the U.S. calculations for setting pilotage rates.

(10) Reasonable profit sharing for non-pilot employees of pilot associations will be allowed as an expense for ratemaking purposes. Profit sharing that benefits pilots will be treated as part of pilot compensation.

§ 404.10 Ratemaking procedures and guidelines.

(a) Appendix A to this part is a description of the types of analyses performed and the methodology followed in the development of a base pilotage rate. Ratemaking calculations in appendix A of this part are made using the definitions and formulas contained in appendix B of this part. Appendix C of this part is a description of the methodology followed in the development of annual reviews to base pilotage rates. Pilotage rates actually implemented may vary from the results of the calculations in appendices A, B and C of this part, because of agreements with Canada requiring identical rates, or because of other circumstances to be determined by the Director. Additional analysis may also be performed as circumstances require. The guidelines contained in § 404.05 are applied in the steps identified in appendix A to this part.

(b) A separate ratemaking calculation is made for each of the following U.S. pilotage areas:

Area 1—the St. Lawrence River;
Area 2—Lake Ontario;
Area 4—Lake Erie;
Area 5—the navigable waters from South East Shoal to Port Huron, MI;
Area 6—Lakes Huron and Michigan;
Area 7—the St. Mary's River; and
Area 8—Lake Superior.

Appendix A to Part 404—Ratemaking Analyses and Methodology

Step 1: Projection of Operating Expenses

(1) The Director projects the amount of vessel traffic annually. Based upon that projection, the Director forecasts the amount of fair and reasonable operating expenses that pilotage rates should recover. This consists of the following phases:

(a) Submission of financial information from each Association;

(b) determination of recognizable expenses;

(c) adjustment for inflation or deflation; and

(d) final projection of operating expenses. Each of these phases is detailed below.

Step 1.A.—Submission of Financial Information

(1) Each Association is responsible for providing detailed financial information to the Director, in accordance with part 403 of this chapter.

Step 1.B.—Determination of Recognizable Expenses

(1) The Director determines which Association expenses will be recognized for ratemaking purposes, using the guidelines for the recognition of expenses contained in § 404.05. Each Association is responsible for providing sufficient data for the Director to make this determination.

Step 1.C.—Adjustment for Inflation or Deflation

(1) In making projections of future expenses, expenses that are subject to inflationary or deflationary pressures are adjusted. Costs not subject to inflation or deflation (e.g., depreciation, long-term leases, pilot compensation, etc.) are not adjusted. The inclusion of an inflation or deflation adjustment does not imply that pilotage rates will be automatically adjusted each shipping season. The inflation or deflation adjustment is only made during the expense projection phase of a full-scale pilotage rate review.

Annual cost inflation or deflation rates will be projected to the succeeding navigation season, reflecting the gradual increase or decrease in cost throughout the year.

For ratemaking calculations begun after January 1, 1996, the actual annual experienced change in operational costs per pilot assignment for each pilotage area will be used to project the inflation or deflation adjustment. For ratemaking calculations begun prior to January 1, 1996, the inflation or deflation adjustment will be based on the preceding year's change in the North Central Region's Consumer Price Index as calculated by the U.S. Bureau of Labor Statistics.

Step 1.D.—Projection of Operating Expenses

(1) Once all adjustments are made to the recognized operating expenses, the Director projects these expenses for each pilotage area. In doing so, the Director takes into account foreseeable circumstances that could affect the accuracy of the projection. The Director will determine, as accurately as reasonably practicable, the ''projection of operating expenses.''

Step 2: Projection of Target Pilot Compensation

(1) The second step in the Great Lakes pilotage ratemaking methodology is to project the amount of target pilot compensation that pilotage rates should provide in each area. This step consists of the following phases:

(a) Determination of target rate of compensation;

(b) determination of number of pilots needed in each pilotage area; and

(c) multiplication of the target compensation by the number of pilots needed to project target pilot compensation needed in each area. Each of these phases is detailed below.

Step 2.A.—Determination of Target Rate of Compensation

(1) Target pilot compensation for pilots providing services in undesignated waters approximates the average annual compensation for first mates on U.S. Great Lakes vessels. The average annual compensation for first mates is determined based on the most current union contracts, and includes wages and benefits received by first mates.

(2) Target pilot compensation for pilots providing services in designated waters approximates the average annual compensation for masters on U.S. Great Lakes vessels. It is calculated as 150% of the compensation earned by first mates on U.S. Great Lakes vessels.

Step 2.B.—Determination of Number of Pilots Needed

(1) The basis for the number of pilots needed in each area of designated waters is established by dividing the projected bridge hours for that area by 1,000. Bridge hours are the number of hours a pilot is aboard a vessel providing basic pilotage service.

(2) The basis for the number of pilots needed in each area of undesignated waters is established by dividing the projected bridge hours for that area by 1,800.

(3) In determining the number of pilots needed in each pilotage area, the Director is guided by the results of the calculations in steps 2.A. and 2.B. However, the Director may also find it necessary to make adjustments to these numbers in order to ensure uninterrupted pilotage service in each area, or for other reasonable circumstances that the Director determines are appropriate.

Step 2.C.—Projection of Target Pilot Compensation

(1) The ''projection of target pilot compensation'' is determined separately for each pilotage area by multiplying the number of pilots needed in that area by the target pilot compensation for pilots working in that area.

Step 3: Projection of Revenue

(1) The third step in the Great Lakes pilotage ratemaking methodology is to project the revenue that would be received in each pilotage area if existing rates were left unchanged. This consists of a projection of future vessel traffic and pilotage revenue.

Step 3.A.—Projection of Revenue

(1) The Director generates the most accurate projections reasonably possible of the pilotage service that will be required by vessel traffic in each pilotage area. These projections are based on historical data and all other relevant data available. Projected demand for pilotage service is multiplied by the existing pilotage rates for that service, to arrive at the ''projection of revenue.''

Step 4: Calculation of Investment Base

(1) The fourth step in the Great Lakes pilotage ratemaking methodology is the calculation of the investment base of each Association. The investment base is the recognized capital investment in the assets employed by each Association required to support pilotage operations. In general, it is the sum of available cash and the net value of real assets, less the value of land. The investment base will be established through the use of the balance sheet accounts, as amended by material supplied in the Notes to the Financial Statement. The formula used in calculating the investment base is detailed in Appendix B to this part.

Step 5: Determination of Target Rate of Return on Investment

(1) The fifth step in the Great Lakes pilotage ratemaking methodology is to determine the Target Rate of Return on Investment. For each Association, a market-equivalent return-on-investment (ROI) is allowed for the recognized net capital invested in the Association by its members.

(2) The allowed ROI is based on the rate of the most recent return on stockholder's equity for a representative cross section of transportation industry companies, including maritime companies, with a minimum rate equal to the interest rate incurred by the Associations for debt capital, and a maximum rate of 20 percent.

(3) Assets subject to return on investment provisions must be reasonable in both purpose and amount. If an asset or other investment is not necessary for the provision of pilotage services, that portion of the return element is not allowed for ratemaking purposes.

Step 6: Adjustment Determination

(1) The next step in the Great Lakes pilotage ratemaking methodology is to insert the results from steps 1, 2, 3, and 4 into a formula that is based on a basic regulatory rate structure, and comparing the results to step 5. This basic regulatory rate structure takes into account revenues, expenses and return on investment, and is of the following form:

Line	Ratemaking projections for basic pilotage
1.	+ Revenue (from step 3)
2.	− Operating Expenses (from step 1)
3.	− Pilot Compensation (from step 2)
4.	= Operating Profit/(Loss)
5.	− Interest Expense (from Audit reports)
6.	= Earnings Before Tax
7.	− Federal Tax Allowance
8.	= Net Income
9.	Return Element (Net Income + Interest)
10.	+ Investment Base (from step 4)
11.	= Return on Investment

(2) The Director will compare the projected return on investment (as calculated using the formula above) to the target return on investment (from step 5), to determine whether an adjustment to the base pilotage rates is necessary. If the projected return on investment is significantly different from the target return on investment, the revenues that would be generated by the current pilotage rates are not equal to the revenues that would need to be recovered by the pilotage rates.

(3) The base pilotage revenues that are needed are calculated by determining what change in projected revenue will make the target return on investment equal to the projected return on investment. This ''projection of revenue needed'' is used in determining the basis for proposed adjustments to the base pilotage rates. The mechanism for adjusting the base pilotage rates is discussed in Step 7 below. The required return, tax, and interest elements may be considered additions to the operating expenses and pilot compensation components of the base pilotage rates.

STEP 7: Adjustment of Pilotage Rates

The final step in the Great Lakes pilotage ratemaking methodology is to adjust base pilotage rates if the calculations from Step 6 show that pilotage rates in a pilotage area should be adjusted, and if the Director determines that it is appropriate to go forward with a rate adjustment. Rate adjustments are calculated in accordance with the procedures found in this step. However, pilotage rates calculated in this step are subject to adjustment based on requirements of the Memorandum of Arrangements between the United States and Canada, and other supportable circumstances that may be appropriate.

(2) Pilotage rate adjustments are calculated for each area by multiplying the existing pilotage rates in each area by the rate multiplier. The rate multiplier is calculated by inserting the result from the steps detailed above into the following formula:

Line	Ratemaking projections
1.	+ Revenue Needed (from step 6)
2.	÷ Revenue (from step 3)
3.	= Rate multiplier

Appendix B to Part 404—Ratemaking Definitions and Formulas

The following definitions apply to the ratemaking formula contained in this appendix.

(1) Operating Revenue—means the sum of all operating revenues received by the Association for pilotage services, including revenues such as docking, moveage, delay, detention, cancellation, and lock transit.

(2) Operating Expense—means the sum of all operating expenses incurred by the Association for pilotage services, less the sum of disallowed expenses.

(3) Target Pilot Compensation—means the compensation that pilots are intended to receive for full time employment. For pilots providing services in undesignated waters, the target pilot compensation is the average annual compensation for first mates on U.S. Great Lakes vessels. For pilots providing services in designated waters, the target pilot compensation is 150% of the average annual

compensation for first mates on U.S. Great Lakes vessels.

(4) Operating Profit/(Loss)—means Operating Revenue less Operating Expense and Target Pilot Compensation.

(5) Interest Expense—means the reported Association interest expense on operations, as adjusted to exclude any interest expense attributable to losses from non-pilotage operations.

(6) Earnings Before Tax—means Operating Profit/(Loss), less the Interest Expense.

(7) Federal Tax Allowance—means the Federal statutory tax on Earnings Before Tax, for those Associations subject to Federal tax.

(8) Net Income—means the Earnings Before Tax, less the Federal Tax Allowance.

(9) Return Element (Net Income plus Interest)—means the Net Income, plus Interest Expense. The return element can be considered the sum of the return to equity capital (the Net Income), and the return to debt (the Interest Expense).

(10) Investment Base (separately determined)—means the net recognized capital invested in the Association, including both equity and debt. Should capital be invested in other than pilotage operations, that capital is excluded from the rate base.

(11) Return on Investment—means the Return element, divided by the Investment Base, and expressed as a percent.

Investment Base Formula

(1) Regulatory Investment (Investment Base) is the recognized capital investment in the useful assets employed by the pilot groups. In general, it is the sum of available cash and the net value of real assets, less the value of land. The investment base is established through the use of the balance sheet accounts, as amended by material supplied in the Notes to the Financial Statement.

(2) The Investment Base is calculated using financial data from the Great Lakes pilot associations, as audited and approved by the Director. The Investment Base would be calculated as follows:

Description

Recognized Assets:
+ Total Current Assets
− Total Current Liabilities
+ Current Notes Payable
+ Total Property and Equipment (Net)
− Land
+ Total Other Assets

= Total Recognized Assets

Non-Recognized Assets
+ Total Investments and Special Funds

= Total Non-Recognized Assets

Total Assets
+ Total Recognized Assets
+ Total Non-Recognized Assets

= Total Assets

Recognized Sources of Funds
+ Total Stockholders' Equity
+ Long-Term Debt
+ Current Notes Payable
+ Advances from Affiliated Companies
+ Long-Term Obligations-Capital Leases

= Total Recognized Sources

Non-Recognized Sources of Funds
+ Pension Liability
+ Other Non-Current Liabilities
+ Deferred Federal Income Taxes
+ Other Deferred Credits

= Total Non-Recognized Sources

Total Sources of Funds
+ Total Recognized Sources
+ Total Non-Recognized Sources

= Total Sources of Funds

(3) Using the figures developed above, the Investment Base is the Recognized Assets times the ratio of Recognized Sources of Funds to Total Sources of Funds.

Appendix C to Part 404—Procedures for Annual Review of Base Pilotage Rates

The ratemaking methodology detailed in appendix A is used by the Director to determine base pilotage rates at least once every five years, as required by § 404.1. In the intervening years the Director will review, if warranted by cost changes, recalculate base pilotage rates proposed for coordination with Canada using the following procedures:

Step 1: Calculate the total economic costs for the base period (i.e. pilot compensation expense plus all other recognized expenses plus the return element) and divide by the total bridge hours used in setting the base period rates;

Step 2: Calculate the ''expense multiplier,'' the ratio of other expenses and the return element to pilot compensation for the base period;

Step 3: Calculate an annual ''projection of target pilot compensation'' using the same procedures found in Step 2 of appendix A;

Step 4: Increase the projected pilot compensation in Step 3 by the expense multiplier in Step 2;

Step 5: Adjust the result in Step 4, as required, for inflation or deflation;

Step 6: Divide the result in Step 5 by projected bridge hours to determine total unit costs;

Step 7: Divide prospective unit costs in Step 6 by the base period unit costs in Step 1;

Step 8: Adjust the base period rates by the percentage change in unit costs in Step 7. For example if the total economic costs per bridge hour is $30.00 for the base period and $33.00 for the prospective rate period, then the rates established for the base period would be increased by 10% to determine the proposed rates for the prospective rate period, which would then be subject to negotiation with Canada.

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Frederico Pena,

Secretary of Transportation.

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