

# CRS Report for Congress

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## The Jones Act: An Overview

John F. Frittelli  
Analyst in Transportation  
Resources, Science, and Industry Division

### Summary

The Jones Act is a perennial issue in Congress. The Act requires that all waterborne shipping between points in the United States be carried by vessels built in the United States and owned and operated by Americans. The purpose of the Act is to ensure that the nation has a sufficient merchant marine and shipbuilding base to protect the nation's defense and commercial interests. Critics claim that the Act does not accomplish this goal and furthermore raises shipping costs, thereby making U.S. farmers and manufacturers less competitive. Jones Act supporters claim that the Act is needed to foster a domestic shipbuilding base that is vital for national security. Despite economic arguments against the Jones Act, efforts to repeal the Act have not been successful. This report will not be updated.

### Background

The Jones Act, section 27 of the Merchant Marine Act of 1920 (46 U.S.C. 883), has long been regarded as a cornerstone of U.S. maritime policy. The policy has been shaped by the concomitant goals of military preparedness and commercial vitality. The Act requires that all waterborne shipping between points within the United States be carried by vessels built in the United States, owned by U.S. citizens (at least 75%), and manned with U.S. citizen crews. The Act essentially bars foreign built and operated vessels from engaging in U.S. domestic commerce. The Act was named after Sen. Wesley L. Jones of Washington, chairman of the Senate Commerce Committee at the time.

The Jones Act of 1920 was not the first instance of protection for U.S. domestic shipping, rather it was a restatement of earlier prohibitions dating back to the first session of Congress. During World War I, prohibition of foreign ships was temporarily lifted in order to maintain an adequate supply of vessels for domestic commerce. Most of the U.S. fleet was called into service for the war effort. Prior to World War I, the domestic merchant fleet operated under an 1817 law, *An Act Concerning the Navigation of the United States*, 14<sup>th</sup> Congress. This law required that U.S. domestic shipping be conducted only with U.S. flagged vessels. Since only U.S. built ships could be flagged in the United States, the Act barred foreign competition. Earlier, in 1789 and 1790, the first session of Congress imposed duties and taxes on foreign built, foreign flag ships engaged in the U.S.

Atlantic coast trade. These duties and taxes were significant and made it difficult for foreigners to compete in U.S. coastwise trade. Foreign built and owned vessels were charged 50 cents/ton at each U.S. port while U.S. built and owned vessels were only charged 6 cents/ton. The Acts of 1789, 1790, and 1817 were intended to counteract existing laws in England and France that protected their merchant fleets. The British Navigation Acts date back to the 1600's and reserved England's foreign and domestic commerce to British built, owned and crewed vessels.<sup>1</sup> The Navigation Acts were aimed chiefly at Britain's rival in merchant shipping - the Dutch.

The Jones Act can be referred to as a "cabotage" law. The word "cabotage" probably derives from the French *caboter* meaning to sail coastwise or by the capes. Cabotage laws, in some form, are not unique to the maritime industry nor to the United States. Air cabotage laws prevent foreign airlines from carrying passengers or cargo between two U.S. cities but there is no requirement that the planes be built in the United States. In the cruise ship market, the counterpart to the Jones Act is the Passenger Services Act of 1886 (46 U.S.C. 289). This Act states, "No foreign vessel shall transport passengers between ports or places in the United States, under penalty of \$200 for each passenger so transported or landed."

Other countries also protect their domestic shipping fleets. A 1991 survey by the Maritime Administration (MARAD)<sup>2</sup> of 56 maritime countries (the United States included) found that 43 countries had some crewing restrictions, 37 countries had ownership provisions, and six countries had domestic construction requirements.

## Purpose of the Jones Act

**National Defense.** A primary purpose of the Jones Act is to foster a strong domestic maritime industry which can be mobilized rapidly in time of war or national emergency. All nations recognize the desire to build their military hardware domestically. The defense justification for protection of domestic shipping dates at least as far back as the first treatise on national economic policy written in 1776. In the *Wealth of Nations*, Adam Smith argued against the mercantile trade policies of his era in favor of free trade or *laissez faire*. However, when it came to domestic shipping, Smith believed this industry was a logical exception to free trade. He supported England's navigation laws: "The defense of Great Britain depends very much upon the number of its sailors and shipping. The act of navigation, therefore, very properly endeavors to give the sailors and shipping of Great Britain the monopoly of the trade of their own country."<sup>3</sup>

Two-and-a-quarter centuries later, Adam Smith's arguments for protecting a domestic fleet are still propounded today. Proponents of the Jones Act argue that the United States needs to maintain a commercial shipbuilding industry, including not only a skilled labor pool of welders and fitters, but also the industrial infrastructure that can be

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<sup>1</sup> The last of the British Navigation Acts was repealed in 1849.

<sup>2</sup> "By the Capes Around the World, A Survey of World Cabotage Practices," U.S. Department of Transportation, MARAD. Available at [<http://www.marad.dot.gov/publications/pubs.html>]

<sup>3</sup> Smith, Adam. *An Inquiry into the Nature and Causes of The Wealth of Nations* (Modern Library Edition, 1994), p. 492.

called upon when our national security is threatened. While the overwhelming bulk of U.S. military supplies and equipment is moved overseas by ship, some observers argue that given the long time needed to build new ships, the relatively brief duration of most recent wars, and the expanded inventory of government-owned sealift ships, the wartime importance of the shipbuilding industry has declined. For some observers, the best wartime national security argument for the Jones Act today is that it helps to maintain a pool of U.S. merchant sailors who can be called upon to man government-owned sealift ships that are reactivated to support the wartime sealift effort.

**Domestic Commerce.** A second purpose, or intent, of the framers of the Jones Act is to protect American sovereignty over domestic maritime commerce. There are three major waterborne trade lanes covered by the Jones Act: coastal ocean, Great Lakes, and inland waterways. Measured in tons, inland waterways is the largest of the three segments. In 1997, inland waterways represented 62% of the total volume of freight moved in the waterborne domestic market. Coastwise trade represented 26%, and the Great Lakes segment represented 12%.<sup>4</sup> More specifically, these trade lanes transport the following commodities:<sup>5</sup>

- ! Domestic crude oil from Alaska to California refineries;
- ! Grain via inland rivers from Midwest farms to Gulf Coast ports;
- ! Iron ore from Minnesota and Michigan to Great Lakes basin steel mills;
- ! Refined petroleum products along the East and Gulf coasts;
- ! Inter-plant movements of chemicals and fertilizers along the Gulf Coast;
- ! Appalachian coal to utilities throughout the Midwest; and
- ! Merchandise to/from Alaska, Hawaii, Puerto Rico, and the U.S. Pacific Islands.

The type of vessels that make up the Jones Act fleet reflects the preponderance in demand for inland river navigation rather than deep-sea coastal or Great Lakes navigation. Barges comprise 85% of the cargo capacity of the fleet whereas deep-sea ships only comprise 15%.<sup>6</sup> The largest category of deep-sea ships is liquid carriers (tankers) because 75% of the coastwise trade is in petroleum products. Critics of the Jones Act question whether a fleet predominantly composed of river barges qualifies as being militarily useful and whether the crew licensed for barge work would be qualified to work on deep-sea vessels in time of war.<sup>7</sup>

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<sup>4</sup> “An Assessment of the Marine Transportation System,” Sept. 1999, MARAD. Available at [<http://www.marad.dot.gov/publications/pubs.html>]

<sup>5</sup> “Capstone Paper\_Jones Act Repeal?” SUNY Maritime College, April 1, 2001, p.9. [[http://www.sunymaritime.edu/ACADEMICS/GRADUATE/forum/\\_forum\\_grad/00000019.htm](http://www.sunymaritime.edu/ACADEMICS/GRADUATE/forum/_forum_grad/00000019.htm)]

<sup>6</sup> MARAD ‘99, available at [<http://www.dot.marad.gov/>]

<sup>7</sup> “Shifting Focus,” *Journal of Commerce*, Jan. 21, 2000.

## Groups Opposing the Jones Act

Opponents of the Jones Act view the law as a “high-cost, low-selection” policy that is not fulfilling its national defense purpose.<sup>8</sup> Instead of fostering a robust maritime industry, critics claim the Jones Act is working against the national security interest. By raising the price of domestic waterborne transport, they say it encourages transport by railroad or pipeline, thus decreasing the demand for domestic ship construction. Critics claim that the protection afforded by the Act has allowed U.S. shipyards to fall behind the rest of the world in efficient and innovative building methods.

**Bulk Shippers.** In general, bulk shippers are more likely to be affected by the Jones Act because their commodities have a lower value per unit cost which means the transport costs are a much higher portion of the total cost to the end user. U.S. agricultural producers are leading opponents of the Jones Act. The American Farm Bureau Federation believes that the Jones Act stands in the way of shipping feed grains economically from the Great Lakes to Southeastern U.S. ports. It contends that livestock producers in the Southeast import feed from foreign suppliers rather than buy from U.S. suppliers in the Midwest because international ocean rates are lower than domestic rates.<sup>9</sup> However, an economic study sponsored by farm groups concluded that improvements in transportation infrastructure in Brazil and Argentina and lower production costs in those countries were a more significant factor than the Jones Act in explaining the foreign sourcing of feedstuffs.<sup>10</sup>

Other bulk shippers opposed to the Jones Act include scrap metal and road salt shippers. At a 1996 congressional hearing, a representative of the Steel Manufacturers Association complained of not being able to utilize domestically produced scrap metal because domestic waterborne transport made it prohibitively expensive. Instead, scrap metal found a foreign market and was being exported to Turkey. At this same hearing, a representative of the road salt industry complained that mid-Atlantic states were importing road salt from Chile and Mexico rather than buying from mines in Ohio and Louisiana. Importing salt was cheaper than buying domestically due to the difference in transport costs.<sup>11</sup>

**Consumers in Hawaii, Alaska, and Puerto Rico.** In addition to bulk shippers, consumers in Alaska, Hawaii, and Puerto Rico also claim they are negatively affected by the Jones Act. A 1988 GAO report found that the Jones Act was costing Alaskan families between \$1,921 and \$4,821 annually for increased prices paid on goods shipped from the mainland.<sup>12</sup> A Hawaii state representative asserted that “Hawaii

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<sup>8</sup> “Spotlight focuses again on the Jones Act,” *Journal of Commerce*, Mar. 16, 2000.

<sup>9</sup> “Jones Act Reform,” available at [<http://www.fb.org>].

<sup>10</sup> *Southeast US Feedstuff Imports: Causal Factors and Recommended Response*, Promar International, March 2003.

<sup>11</sup> U.S. House of Representatives, Subcommittee on Coast Guard and Maritime Transportation, Hearing on *The Impact of U.S. Coastwise Trade Laws on the Transportation System in the United States*, June 12, 1996.

<sup>12</sup> “The Jones Act, Impact on Alaska Transportation and U.S. Military Sealift Capability,” (continued...)

residents pay an additional \$1 billion per year in higher prices because of the Jones Act. This amounts to approximately \$3,000 for every household in Hawaii.”<sup>13</sup> A representative of business interests in Puerto Rico argued that their producers were placed at a disadvantage with respect to producers in Mexico because the cabotage laws raised shipping costs between the United States and Puerto Rico.<sup>14</sup>

These groups claim that they are in fact subsidizing the Jones Act fleet through the higher rates they must pay. They argue that since maintaining a Jones Act fleet is largely for national defense purposes, the Nation as a whole should share the cost rather than the burden falling on just a few. These groups recommend that a domestic fleet be subsidized directly by the Department of Defense (DOD).

## Groups Supporting the Jones Act

**Pro-defense Groups.** The strongest argument proponents of the Jones Act have to counter high cost accusations is its strategic defense necessity - the unstated role of the merchant marine as America’s “fourth arm of defense.” Recent Presidents, Democrat and Republican, have supported the Jones Act. Although in peacetime the Jones Act may be viewed by many as an anachronism, in wartime, shipbuilding and a merchant marine are viewed as vital to national security. Defense groups argue that the maritime community represents a highly skilled work force and a physical establishment that can not be quickly replaced once it is lost. They assert that the national security importance of the Jones Act goes beyond the simple “bean counting” of deep-sea vessels. The most valuable national security component that the Jones Act provides, they contend, is a domestic shipbuilding and repair base.

**Maritime Unions.** Maritime unions point to the 124,000 jobs the Jones Act creates for the U.S. economy. These jobs are said to pay annually \$1.1 billion in federal taxes and \$272 million in state taxes. Domestic carriers that participate in the Jones Act trade claim that they pay \$300 million in federal and \$55 million in state taxes on their corporate profits.<sup>15</sup> Maritime unions also argue that the Jones Act ensures a level playing field among domestic carriers. If carriers are all U.S. owned, they all will be subject to the same laws and regulations. All domestic carriers pay U.S. taxes, adhere to U.S. labor laws - including minimum wage and other requirements, and follow Coast Guard safety, and environmental regulations. If foreign carriers were allowed in the domestic trades, they would have an unfair advantage because they would be free from these extra costs that U.S. regulations impose on domestic transport.

**U.S. Shipyards.** Domestic shipyards contend that there are “fair trade” issues involved in U.S. shipbuilding. Many nations subsidize their shipyards either directly or

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<sup>12</sup> (...continued)

General Accounting Office, September 1988, RCED-98-96R.

<sup>13</sup> Ward, Gene. “View Point: To Fix Economy, Junk the Jones Act,” *Honolulu Star-Bulletin*, Dec. 5, 1997. Available at [<http://starbulletin.com/97/12/05/editorial/viewpointf.html>].

<sup>14</sup> Testimony of Rafael Cebollero, U.S. House, Subcommittee on Coast Guard and Maritime Transportation, Hearing on *The Impact of U.S. Coastwise Trade Laws*, June 12, 1996.

<sup>15</sup> These statistics are available from [<http://www.marad.dot.gov/>].

indirectly. Recently, South Korea has drawn much criticism from the European Union for its alleged subsidy practices. South Korea recently emerged as the largest shipbuilding nation, a title Japan had held for 44 years. The EU is claiming that South Korean yards are “dumping” their ships on the market at prices below cost. South Korea claims its advantage is a result of cheap labor costs and the weakness of its currency. Although the U.S. does not currently provide direct subsidy for commercial shipbuilding,<sup>16</sup> it does provide a loan guarantee program that insures 87.5% of the financing for new ship construction.<sup>17</sup> The U.S. shipbuilding community contends the Jones Act is needed to counteract the subsidy policies of other nations.

## **An Assessment of the Jones Act**

Economic studies have consistently found an aggregate economic cost of the Jones Act. For instance, a recent U.S. International Trade Commission economic study found that repealing the Jones Act would have a annual positive welfare effect on the overall U.S. economy of \$656 million.<sup>18</sup> Although this and other studies make an economic case for repeal of the Act, the Act provides a significant degree of protection for U.S. shipyards, domestic carriers, and American merchant sailors. Additionally, the national security implications of the Jones Act are difficult to measure but are considered by many observers as positive for the Nation.

Like U.S. trade policy in other goods or services, the Jones Act is highly controversial because there are definite winners and losers. The potential losses from lifting the shipping restrictions, such as jobs in shipyards and the merchant marine, are highly visible and concentrated, while the potential gains, such as lower consumer prices, are largely invisible and widely dispersed. It is worth noting that some of the largest shipyards in the country are the largest employers in the states where they are located. On the other hand, only a tiny fraction of American consumers are probably aware of the Jones Act or that it affects the prices they pay for goods. Shippers and residents of Hawaii and other insular possessions are most directly affected in terms of the cost of the Jones Act.

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<sup>16</sup> Direct subsidies ended in 1982 when funding of the Construction Differential Subsidy (CDS) was terminated.

<sup>17</sup> The Maritime Guaranteed Loan (Title XI) Program which is administered by MARAD.

<sup>18</sup> *The Economic Effects of Significant U.S. Import Restraints*, Third Update, June 2002.