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Abstract

Traditionally, the United States has aspired to the operation of its industries in a system of free enterprise. One of the oldest instances of government intervention in shipping - the cabotage law- was designed to preserve for domestic vessels all trade between domestic points. Recently, however, developments in maritime commerce have led United States courts to an examination of cabotage legislation. The result has noticeably limited the scope of United States coast-wise laws. Specifically, questions have arisen over: 1) the eligibility for coastwise trade of vessels which have been reconstructed from parts of two other ships, 2) the application of cabotage legislation to cargo which returns to the United States after having been processed or refined abroad,6 and 3) the entry into coastwise trade of federally subsidized vessels. After discussing the purpose and scope of the cabotage law, this Note will discuss these issues and their significance in the overall scheme of United States shipping.

THE WEAKENING GRIP OF UNITED STATES CABOTAGE LAW

INTRODUCTION

Traditionally, the United States has aspired to the operation of its industries in a system of free enterprise. Yet today, the United States shipping industry finds itself ensnared in an increasingly intricate set of domestic and international regulations.[1] One of the oldest instances of government intervention in shipping[2]—the cabotage law[3]—was designed to preserve for domestic vessels all trade between domestic points.[4]

Recently, however, developments in maritime commerce have led United States courts to an examination of cabotage legislation. The result has noticeably limited the scope of United States coastwise laws. Specifically, questions have arisen over: 1) the eligibility for coastwise trade of vessels which have been reconstructed from

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1. *See generally* G. JANTSCHER, BREAD UPON THE WATERS: FEDERAL AIDS TO THE MARITIME INDUSTRIES (1975); Hearn, *Cargo Preference and Control*, 2 J. MAR. L. & COM. 481 (1971); Morse, *A Study of American Merchant Marine Legislation*, 25 LAW & CONTEMP. PROB. 57 (1960); James, *Some Current Developments in United States Control of International Shipping*, 7 INT'L LAW. 541 (1973); Note, *Cargo Preference: The United States and the Future Regulation of International Shipping*, 16 VA. J. INT'L L. 865 (1976). For examples of specific United States legislation, see Shipping Act of 1916, 46 U.S.C. §§ 810-842 (1976) (especially § 814, the provision excluding liner conferences from United States antitrust laws, *see* Llorca, *Anti-trust Exemption of Shipping Conferences*, 6 J. MAR. L. & COM. 287 (1975)); Merchant Marine Act of 1936, 46 U.S.C. §§ 1101-1294 (1976) (vessel construction and operating subsidy programs); Merchant Marine Act of 1970, 46 U.S.C. §§ 1151-1155 (1976) (amendments to Merchant Marine Act of 1936, *see* Richardson, *Capital Construction Funds Under the Merchant Marine Act*, 29 TAX L. REV. 751 (1974)).

2. Among the earliest laws passed by Congress was one which placed a discriminatory tax on foreign vessels operating in the coastwise trade. Act of July 20, 1789, ch. 2, 1 Stat. 27.

3. Cabotage is defined as "*coasting-trade* so that it means navigating and trading along the coast between the ports thereof." BLACK'S LAW DICTIONARY 183 (5th ed. 1979) (emphasis in original). A similar cabotage provision restricts the use of foreign aircraft between United States destinations. 49 U.S.C. § 176(c) (1976).

4. The chief legislation in the United States concerning this reservation is 46 U.S.C. § 883 (Supp. III 1979).

parts of two other ships,[5] 2) the application of cabotage legislation to cargo which returns to the United States after having been processed or refined abroad,[6] and 3) the entry into coastwise trade of federally subsidized vessels.[7] After discussing the purpose and scope of the cabotage law, this Note will discuss these issues and their significance in the overall scheme of United States shipping.

I. *NATURE OF CABOTAGE LAW*

The United States Congress has long recognized the need to shield the domestic merchant marine from foreign competition.[8] Originally, in the face of the dominance enjoyed by Britain on the seas, this protection was aimed at simply permitting the United States to develop a merchant marine.[9] More recently, Congress has maintained protectionist legislation because the cost of constructing vessels in United States shipyards and operating them with United States crews is substantially higher than comparative foreign costs.[10] Additionally, the governments of most seafaring nations supply their national merchant marines with generous subsidies.[11] Quite obviously, the United States merchant marine would

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5. Marine Carriers Corp. v. Fowler, 429 F.2d 702 (2d Cir.), *cert. denied*, 400 U.S. 1020 (1970).

6. American Maritime Ass'n v. Blumenthal, 590 F.2d 1156 (D.C. Cir. 1978), *cert. denied*, 441 U.S. 943 (1979).

7. Seatrain Shipbuilding Corp. v. Shell Oil Co., 444 U.S. 572 (1980), *rev'g sub nom.* Alaska Bulk Carriers, Inc. v. Kreps, 595 F.2d 184 (D.C. Cir. 1979).

8. *See, e.g.*, Act of March 1, 1817, ch. 31, § 4, 3 Stat. 351 (outright prohibition of foreign vessels from United States coastwise trade); Act of July 20, 1789, ch. 3, § 3, 1 Stat. 27 (tax on foreign vessels operating in the United States coastwise trade); Act of July 4, 1789, ch. 2, § 5, 1 Stat. 27 (reduction of duty on goods imported on United States owned vessels).

9. G. GILMORE & C. BLACK, THE LAW OF ADMIRALTY 963 (2d ed. 1975).

10. *Id.* at 968-70. Operating costs on United States flag vessels traditionally have been double those of vessels sailing under Liberian or Panamanian registries. B. BOCZEK, FLAGS OF CONVENIENCE 2 n.5 (1962); *see, e.g.*, *Ship Transfers to Foreign Flag: Hearings on S. 1488 Before the Subcomm. on the Merchant Marine & Fisheries of the Senate Comm. on Interstate & Foreign Commerce*, 85th Cong., 1st Sess. 104-05 (1957). *See also* Farrell Lines Inc. v. United States, 499 F.2d 587 (Ct. Cl. 1974). Both the Dept. of Commerce and shipowners have "developed elaborate systems for estimating the foreign cost . . . of a proposed ship. One method . . . is to obtain . . . information on the costs of the myriad components of the ship in the foreign shipbuilding center. From this data they compute a hypothetical low bid for their ship . . . ." Moore-McCormack Lines Inc. v. United States, 413 F.2d 568, 572 (Ct. Cl. 1969).

11. For a review of the maritime subsidies of other nations, as well as those of the United States, see MARITIME ADMINISTRATION, U.S. DEP'T OF COMMERCE, MARITIME SUBSIDIES (1978).

be swept from the seas without some governmental aid designed to reduce this competitive imbalance.

Congress has insisted that a viable merchant marine is a requisite for both commercial and defensive purposes.[12] Consequently, the protective umbrella erected for United States shipping has a dual nature. First, cabotage specifically requires that a vessel be built in a United States shipyard, be owned by United States citizens and be manned by a United States crew in order to gain enrollment,[13] which is the permission to engage in domestic coastwise commerce.[14] Section 27 of the Merchant Marine Act of 1920,[15] known as the Jones Act,[16] provides for the forfeiture of any cargo transported between United States domestic points by unenrolled vessels.[17]

Second, Congress has established several subsidy programs which enable United States flag vessels engaged only in foreign trade to compete effectively with carriers registered abroad.[18] Specifically, the Merchant Marine Act of 1936[19] permitted the government to contribute up to 50% of the construction costs for vessels needed in the United States foreign merchant fleet.[20] The act also requires that those vessels which received such a construction-differential subsidy (CDS) refrain from competing in the United States coastwise trade unless they fall within one of two statutory

12. *See* Merchant Marine Act of 1936, 46 U.S.C. § 1101 (preamble) (1976). The United States seeks to "have a merchant marine of . . . vessels sufficient to carry the greater portion of its commerce and serve as a naval or military auxiliary . . . ." *Id.* *See generally* W. GORTER, UNITED STATES SHIPPING POLICY (1977).

13. 46 U.S.C. §§ 11, 252 (1976). The Commissioner of Customs is responsible for making rulings and regulations on vessel activity in the coastwise trade. *Id.* § 2. Enrollment is not to be confused with registration, which is the documentation required in order to participate in foreign trade under the United States flag. *Id.* § 11.

14. *Id.* § 252.

15. 46 U.S.C. § 883 (Supp. III 1979).

16. *Id.* The "Jones Act" is also a name often ascribed to Section 33 of the Merchant Marine Act of 1920, 46 U.S.C. § 688 (1976) (concerning liability for injuries to seamen). For the purposes of this Note, however, the "Jones Act" refers only to section 27 of the Merchant Marine Act of 1920. For a concise history of section 27, see Lowry, *Jones Act*, 40 ICC PRAC. J. 779 (1973).

17. 46 U.S.C. § 883 (Supp. III 1979).

18. The Merchant Marine Act of 1936, 46 U.S.C. §§ 1101-1294 (1976); *see* notes 91-95 *infra* and accompanying text.

19. 46 U.S.C. §§ 1101-1294 (1976).

20. *Id.* § 1152(b). The considerations which go into determining whether a vessel is needed in the United States foreign merchant fleet are found at 46 U.S.C. § 1171(a)(1) (1976). For an analysis of this section, see 1978 DUKE L. J. 252; 18 VA. J. INT'L L. 359 (1978).

exceptions.[21] In order for a vessel to take advantage of either exception, its owners must make a proportional repayment of the subsidy to the government.[22]

Thus, the United States merchant marine can be divided into two separately protected groups: 1) the "Jones Act Fleet," which enjoys freedom from competition by foreign and government subsidized vessels, while high operating expenses prevent it from soliciting any worldwide trade, and 2) the subsidized foreign trade fleet, which is in a position to compete with foreign vessels, but is statutorily barred from coastwise activities. The necessity of such an arrangement has gone largely undebated,[23] and, in fact, disputes over United States cabotage legislation have only occasionally reached the courts.[24] Largely due to the era of the super-tanker and the opening of the Alaskan oil slopes, however, several major cabotage issues have emerged which have required judicial resolution.[25]

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21. 46 U.S.C. § 1156 (1976). For a discussion of this government subsidy program, see Moore-McCormack Lines, Inc. v. United States, 413 F.2d 568 (Ct. Cl. 1969). For general discussions on the effect of the Merchant Marine Act of 1970, 46 U.S.C. §§ 1151-1155, see Blackwell, *Implementation of the Merchant Marine Act of 1970*, 5 J. MAR. L. & COM. 167 (1974); Bowman, *The Merchant Marine Act of 1970*, 2 J. MAR. L. & COM. 715 (1971).

22. For a description of these exceptions, see note 106 *infra* and accompanying text.

23. Cabotage restriction is a principle generally agreed upon among the world's major maritime powers. 1 L. OPPENHEIM, INTERNATIONAL LAW § 187 (8th ed. 1955). At present, twenty-two seafaring nations have enacted cabotage statutes. These are: Australia, Brazil, Canada, Chile, Colombia, Denmark, Finland, France, the Federal Republic of Germany, Greece, India, Italy, the Republic of Korea, Pakistan, Panama, Peru, the Philippines, Portugal, Spain, Turkey, the United States, and Venezuela. The notable exception is Great Britain. Komarow, *Foreign Cargo Vessels in the Coastwise Oil Trade*, 10 J. MAR. L. & COM. 271, 271 n.2 (1979). For a discussion of coastwise law in relation to German public policy, see Wirth Ltd. v. S/S Acadia Forest, 537 F.2d 1272, 1279-81 (5th Cir. 1976).

24. *See, e.g.*, Central Vt. Transp. Co. v. Durning, 294 U.S. 33 (1935) (denial of coastwise privileges to a vessel owned by a Canadian corporation); Gillentine v. McKeand, 426 F.2d 717 (1st Cir. 1970) (barring renationalized vessels from operating in the coastwise passenger trade); United States v. 1500 Cords, More or Less, Jackpine Pulpwood, 204 F.2d 760 (7th Cir. 1953) (transport of logs by a Canadian tug within a United States harbor did not violate cabotage law); Great Lakes Dredge & Dock Co. v. Ludwig, 486 F. Supp. 1305 (W.D.N.Y. 1980) (dredging activities are not considered coastwise activities); United States v. 12,536 Gross Tons of Whale Oil Ex The Charles Racine, 29 F. Supp. 262 (E.D. Va. 1939) (constantly changing points are not included within the cabotage restriction).

25. *See* notes 5-7 *supra* and accompanying text.

II. *REBUILT VESSELS*

One of the more complex problems arising under cabotage legislation concerns the "jumboizing" of vessels.[26] Such a procedure involves the rebuilding of a ship by connecting components of two or more vessels to create a larger ship. If such a ship then attempts to enter the coastwise trade, the heritage of those components becomes crucially significant. This was at the heart of *Marine Carrier Corp. v. Fowler*,[27] a case in which the owners of the jumboized vessel OBSERVER attempted to gain for it coastwise privileges. The Commisioner of Customs, however, ruled that the OBSERVER was ineligible for enrollment,[28] and the owners' appeal to the Secretary of the Treasury resulted in an affirmation of that ruling.[29] In the resulting court battle the district court held in favor of the OBSERVER;[30] however, the Second Circuit reversed and remanded for further fact finding.[31]

The ancestry of the OBSERVER is quite detailed, yet merits discussion because it makes clear the problem of jumboizing.[32] The tanker WAPELLO, one of the OBSERVER's earliest ancestors, was constructed in a United States shipyard for Panamanian owners in 1953. It was subsequently dismembered, and in a Japanese shipyard its forebody was attached to the stern of the tanker ESSO CHITTAGONG, a United States-built vessel also of Panamanian ownership and registry. The result of the pairing was the Liberian registered SANTA HELENA. That ship was itself dismembered, and its forebody, previously that of the WAPELLO, was attached, in a United States shipyard, to the stern of the enrolled vessel TRUSTCO. The offspring from this coupling was christened the OBSERVER.

As already indicated, in order to enjoy coastwise privileges, a

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26. Shipowners have made "ingenious efforts to rebuild, modernize, and enlarge qualified vessels without losing the favored Jones Act status." Lowry, *supra* note 16, at 784 (footnotes omitted). The difficulty arises in "distinguishing the donor from the donee." Marine Carriers Corp. v. Fowler, 429 F.2d 702, 709 (2d Cir.), *cert. denied*, 400 U.S. 1020 (1970).

27. 429 F.2d 702 (2d Cir.), *cert. denied*, 400 U.S. 1020 (1970).

28. 429 F.2d at 704.

29. *Id.* at 704-05.

30. 305 F. Supp. 984, 989 (S.D.N.Y. 1969).

31. 429 F.2d 702, 710 (2d Cir. 1970).

32. This history of the OBSERVER is a paraphrasing of the district court's own discussion. *See* 305 F. Supp. at 985.

vessel must meet several criteria.[33] It must be of United States construction and ownership. Furthermore, if two vessels were entitled to enrollment, their progeny most certainly would also possess this right.[34] In the case of the OBSERVER, however, debate arose as to whether one parent, the SANTA HELENA, possessed coastwise privileges. Several of the provisos[35] added to the Merchant Marine Act of 1920 caused the status of the WAPELLO, and subsequently that of the OBSERVER, to be disputed.

The first proviso mandates that once a vessel has forfeited its right to engage in coastwise trading by being sold to a foreigner, it may never recapture that privilege. It states:

> [N]o vessel having at any time acquired the lawful right to engage in the coastwise trade, either by virtue of having been built in, or documented under the laws of the United States, and later sold foreign in whole, or in part, or placed under foreign registry, shall hereafter acquire the right to engage in the coastwise trade . . . .[36]

The first question then, becomes whether the WAPELLO ever possessed that coastwise privilege. If it did not, it obviously could never have forfeited it.[37] Both the district and circuit courts saw this initial problem as one of interpretation of the statute's rather ambiguous wording.[38] The Second Circuit noted that "[t]he first

33. *See* notes 13-14 *supra* and accompanying text.

34. 429 F.2d at 705. The court stated that "[t]he TRUSTCO's eligibility for coastwise trade was not subject to question . . . . [i]f the WAPELLO, and *a fortiori* its forebody, were also eligible, it would follow that the OBSERVER . . . was entitled to coastwise trading privileges." *Id.* (emphasis in original).

35. Eight provisos, together with amendments, have been added to the Jones Act. 46 U.S.C. § 883 (Supp. III 1979). These are: Nov. 16, 1979, Pub. L. No. 96-112, § 4, 93 Stat. 848; Oct. 3, 1978, Pub. L. No. 95-410, tit. II, § 213, 92 Stat. 904; Nov. 23, 1971, Pub. L. No. 92-163, § 1, 85 Stat. 486; Aug. 11, 1968, Pub. L. No. 90-474, 82 Stat. 700; Sept. 21, 1965, Pub. L. No. 89-194, 79 Stat. 823; July 5, 1960, Pub. L. No. 86-583, § 1, 74 Stat. 321; July 7, 1958, Pub. L. No. 85-508, § 27(a), 72 Stat. 351; July 14, 1956, Pub. L. No. 714, ch. 600, § 1, 70 Stat. 544; 1950 Reorg. Plan No. 21, §§ 204, 306, eff. May 24, 1950, 15 Fed. Reg. 3178, 64 Stat. 1276, 1277; June 29, 1936, ch. 858, §§ 204, 904, 49 Stat. 1987; July 2, 1935, ch. 355, § 1, 49 Stat. 442; Apr. 11, 1935, ch. 58, 49 Stat. 154; Ex. Ord. No. 6166, § 12, June 10, 1933. For a general discussion of pre-1979 provisos, see Komarow, *supra* note 23, at 276-85; Lowry, *supra* note 16, at 784-89.

36. Act of July 2, 1935, ch. 355, § 1, 49 Stat. 442 (codified at 46 U.S.C. § 883 (Supp. III 1979)).

37. 429 F.2d at 706.

38. 305 F. Supp. at 987; 429 F.2d at 706.

phrase seems to suggest that the proviso applies only to those vessels sold foreign after having acquired the full legal right to engage in the coastwise trade; the second phrase, that it applies to all vessels sold foreign after having been built in the United States."[39]

The district court decided that the first phrase was operative, and thus held that the WAPELLO would have been eligible for domestic trading.[40] Consequently, it ruled that the OBSERVER, the offspring of two legitimate traders, was likewise fit for enrollment.[41]

The Second Circuit rejected this holding and based its decision on the proviso's legislative history. As the court noted, both the Senate and House Committee Reports specifically named two classes of vessels to which the proviso was directed: " '1. Vessels built in or documented under the laws of the United States and later sold to foreign owners,' " and " '2. Vessels built in the United States for foreign countries or foreign purchasers.' "[42] The WAPELLO falls directly into the second category. Such specific legislative intent, coupled with the usual statutory scheme of protectionist legislation,[43] convinced the court that the WAPELLO had indeed surrendered its right to coastwise trade.[44] Thus, in order to reconcile the proviso's conflicting language, the circuit court decided that a vessel built in the United States acquires a right to participate in domestic trade, conditioned upon its ownership by a United States citizen.[45] If, as in the WAPELLO's case, it is sold to a foreigner, even if it was never previously enrolled, the vessel irrevocably loses its coastwise trading privileges.[46]

Having determined the WAPELLO's domestic ineligibility, the Second Circuit had to rule on the rights of a vessel created by

39. 429 F.2d at 706.

40. 305 F. Supp. at 988.

41. *Id.*

42. 429 F.2d at 707, quoting S. REP. NO. 870, 74th Cong., 1st Sess. 2 (1935); H.R. REP. NO. 118, 74th Cong., 1st Sess. 2 (1935).

43. *See generally* Morse, *supra* note 1, at 62.

44. 429 F.2d at 708. The Second Circuit stated:

> In sum, we are of the view that the first proviso to § 27 [of the Merchant Marine Act of 1920] must be interpreted as a coherent whole and that we must give recognition to the expressed intent of Congress, and the purposes of the statutory scheme. Accordingly, we are led to the conclusion that the WAPELLO could not engage in the coastwise trade.

Id.

45. *Id.* at 707.

46. *Id.*

the joining of one eligible and one ineligible tanker. Important to this evaluation was the second proviso to section 27 of the Merchant Marine Act of 1920.[47] It forbids a rebuilt vessel's entry into the coastwise trade unless the entire rebuilding, including construction of any major components of the hull or superstructure, takes place within the United States.[48]

This exception was relevant because the OBSERVER *must* be considered a rebuilt ship rather than a new one.[49] The question remained whether it was a rebuilt SANTA HELENA, which contributed the WAPELLO's forebody to the OBSERVER, or a rebuilt TRUSTCO. If it was a rebuilt SANTA HELENA, the second proviso deprived it of coasting privileges because the SANTA HELENA's own rebuilding had taken place in Japan. Similarly, the first proviso would also deny it enrollment because of the SANTA HELENA's own tainted lineage (the WAPELLO).[50] On the other hand, the OBSERVER would have enjoyed coastwise rights if it was a rebuilt TRUSTCO.[51]

With the central issue now being which ship bequeathed its personality to the OBSERVER, the Second Circuit decided that this is a matter requiring determination at trial.[52] Accordingly, it remanded the case to the district court.[53]

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47. Act of July 14, 1956, Pub. L. No. 714, ch. 600, § 1, 70 Stat. 544, *as amended by* Act of July 5, 1960, Pub. L. No. 86-583, § 1, 74 Stat. 321 (codified at 46 U.S.C. § 883 (Supp. III 1979)). The proviso states:

> [N]o vessel of more than five hundred gross tons which has acquired the lawful right to engage in the coastwise trade, by virtue of having been built in or documented under the laws of the United States, and which has later been rebuilt shall have the right thereafter to engage in the coastwise trade unless the entire rebuilding, including the construction of any major components of the hull or superstructure of the vessel, is effected within the United States, its Territories (not including trust territories), or its possessions . . . .

48. *Id.*

49. The Second Circuit pointed out that the OBSERVER necessarily cannot be defined as a new ship; otherwise, a shipowner could attach the stern of one ineligible ship to the forebody of another, and vice-versa. He would thereby create two "new" ships eligible for the coastwise trade, whereas none had existed before. The result would be in direct conflict with the statutory intent of United States cabotage laws. *See* 429 F.2d at 709.

50. 429 F.2d at 709.

51. *Id.*

52. *Id.* at 710.

53. *Id.* The case was never retried in the district court. Appellant, Marine Carriers, had two vessels which possessed both enrolled and unenrolled parts. One, the SEAFARE, was sold after the Second Circuit decision. The OBSERVER, meanwhile,

The primary significance of *Fowler* is the importance of ancestral purity for jumboized vessels seeking coastwise privileges, and the ease with which the first proviso may strip a vessel of its conditional right to that privilege. Significantly, though, no such condition exists with respect to the second proviso. In other words, although an entire vessel may lose its domestic trading rights, its parts are not similarly barred. Thus, if it was decided that the OBSERVER was a rebuilt TRUSTCO, the fact that its forebody came from the tainted SANTA HELENA in no way flaws its enrollment claim.[54]

The issue remains undecided, however, as to which rebuilt vessel the OBSERVER actually was. Protracted expert testimony will be necessary to determine whether a rebuilt vessel's forebody, which comprises most of its length, or its stern, which is the more valuable part, dominates its heritage.[55] If construction of jumboized super-tankers continues, this is a problem with which courts must ultimately grapple.

III. *ALTERED CARGO AND COASTWISE SHIPPING*

Encompassed within the Jones Act is a prohibition against the transshipment of goods; that is, cargo cannot be shipped from a domestic point to a foreign port, and then fowarded directly back to another domestic point unless vessels on both legs of the journey are enrolled.[56] This prohibition stems from the result in *United States v. 250 Kegs of Nails*,[57] after which Congress added the words, "either directly or via a foreign port,"[58] to the original cabotage statute.[59] In that case, the court strictly applied the statute,[60] which simply banned the shipment of cargo from one domestic point to another on a foreign vessel. Therefore, 250 kegs of nails

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was stranded in the Suez Canal during hostilities between Egypt and Israel in 1970. It was not returned to its owners until a 1976 dredging of the Canal. Marine Carriers, therefore, did not pursue the case as the issue had become moot because of the vessel's damaged condition. Telephone conservation with Robert Corbett, counsel for appellants (Feb. 23, 1981).

54. 429 F.2d at 708 n.5.

55. *Id.* at 710.

56. 46 U.S.C. § 883 (Supp. III 1979).

57. 61 F. 410 (9th Cir. 1894).

58. Act of Feb. 15, 1893, ch. 117, 27 Stat. 455 (current version at 46 U.S.C. § 883 (Supp. III 1979)).

59. Act of March 1, 1817, § 4, 3 Stat. 351, *as amended by* Act of July 18, 1866, § 20, 14 Stat. 182.

60. 61 F. at 411.

which were sent from New York to Antwerp on a Belgian ship, and then were reshipped to California on a British ship, were not subject to forfeiture.[61] The court's emphasis was on the continuity of the voyage, which it saw to be disrupted by the Antwerp stopover.[62] This decision pointed out the ease with which all the carefully constructed protection for the United States Merchant Marine could be circumvented. The new phrase "either directly or via a foreign port," was Congress' answer.[63]

Although the amended statute removed one problem, new questions naturally emerged. Despite *250 Kegs*, the shipper's intent has traditionally been the controlling element in determining whether his cargo was on a continuous voyage.[64] Thus, if he sent goods to a foreign port with the anticipation of reshipping them directly back to the United States, he could be held in violation of coastwise law.[65] Increased Alaskan oil trade has prompted one circuit to reevaluate this test.[66]

In *American Maritime Ass'n v. Blumenthal*[67] the Hess Corporation decided to transport crude oil in foreign flag tankers from Valdez, Alaska to its refinery in the Virgin Islands.[68] The refined products would then be shipped to points on the United States east coast,[69] again in foreign vessels. The problem for the court was determining whether such activity amounted to two distinct voyages, or one voyage subject to the Jones Act.

Both the district and circuit courts concluded that Hess' action was not a Jones Act violation.[70] The district court found that eleven different products result from the refining of crude oil,[71] and this

61. *Id.* at 414.

62. *Id.* at 411.

63. *See* note 56 *supra* and accompanying text.

64. The Bermuda, 70 U.S. (3 Wall.) 514 (1865). *See also* The Peterhoff, 72 U.S. (5 Wall.) 28 (1866).

65. *See* 32 Op. Att'y Gen. 350, 351 (1920). This intent was deemed to be a question of fact. If such intent were attributable to the shipper, his cargo was subject to forfeiture. *Id.* at 362-63.

66. American Maritime Ass'n v. Blumenthal, 590 F.2d 1156, 1164-65 (D.C. Cir. 1978).

67. 590 F.2d 1156 (D.C. Cir. 1978), *aff'g*, 458 F. Supp. 849 (D.D.C. 1977).

68. The Virgin Islands are not embraced within the United States cabotage law. 46 U.S.C. § 877 (1976).

69. 590 F.2d at 1161. At that time, Alaskan oil could not be exported except under certain prescribed circumstances. *Id.* at n.9. *See* Act of June 22, 1977, Pub. L. No. 95-52, § 110 (codified at 50 U.S.C. app. § 2406 (Supp. III 1979)).

70. 458 F. Supp. at 863; 590 F.2d at 1165.

71. 458 F. Supp. at 862. The refining of Alaskan crude oil yields the following

"conclusively demonstrates that the products of the Hess refinery are new and different merchandise from the Alaskan crude oil."[72] Thus, Hess' activities added up to much more than simple transshipment, and the coastwise laws remained undisturbed.[73]

On appeal, the American Maritime Association insisted that continuity within the meaning of the Jones Act was violated, regardless of the change these goods underwent because of Hess' ultimate intent that its fuel products be sent to the United States.[74] Further, it argued that in this particular instance, the goods did not so lose their identity that they qualified as different merchandise.[75] In addressing these two arguments, the District of Columbia Circuit arrived at what could prove to be a troubling conclusion.[76]

The court saw the case as one of strict statutory application,[77] and reduced the problem to the nature of the goods.[78] Since "[n]o merchandise shall be transported . . . between points in the United States . . . in [foreign vessels],"[79] if the merchandise leaving the Virgin Islands was not the same cargo as that which entered, the Jones Act was inapplicable.[80]

The court refused to apply the intent test, and stated that "under the circumstances of this case, we hold that it is not the *intent* of a shipper to send goods to a final destination that governs, but the degree to which the goods are altered *in fact* in the course of commercial dealings."[81] Admittedly, the court restricted its decision to the facts before it; however, if the alteration test is given

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products in per cent volume: No. 6 Oil (55.82); No. 2 Oil (14.50); jet fuel (8.70); gasoline (4.19); premium gasoline (4.19); unleaded gasoline (3.00); toluene (2.23); paraxylene (1.08); benzene (.47); sulfur pellets (.30); xylene (.27). *Id.*

72. *Id.* at 863.
73. *Id.*
74. 590 F.2d at 1164.
75. *Id.* at 1162.
76. *See* notes 81-89 *infra* and accompanying text.
77. 590 F.2d at 1161.
78. *Id.*
79. 46 U.S.C. § 883 (Supp. III 1979).
80. 590 F.2d at 1163.
81. *Id.* at 1164 (emphasis in original). The court also noted that in construing the predecessor statute to the Jones Act, the Ninth Circuit, in *United States v. 250 Kegs of Nails*, 61 F. 410, 412 (9th Cir. 1894), emphasized that the ultimate purpose of the parties meant little if they had actually complied with the letter of the law. 590 F.2d at 1164 n.39. *250 Kegs* would hardly seem a worthwhile case on which to rely since its result immediately prompted an adverse congressional response. *See* notes 57-63 *supra* and accompanying text.

wide utility, an entire array of new problems may unfold within the shipping industry.

Specifically, an alteration rather than an intent test may give shippers unabashed liberty to undertake activity that would attenuate Congress' protectionist shipping policies. Industrialists could conduct all manner of manufacturing, processing, and refining activities at points outside the embrace of cabotage[82] with the view towards gaining the availability of foreign shipping.[83] The court noted that much of the world's economy is based on both United States exports and the vast United States consumer market.[84] Therefore, it would be senseless to prohibit from transport in foreign vessels goods which might originate as United States raw materials, then become processed abroad, and finally go on sale to the United States public.[85] Nevertheless, the bare alteration test seems to dismantle part of Congress' protectionist scheme, and could pave the way to a weakening of the United States merchant marine.

More suitable would be a combined intent/alteration test. Then, for example, if a shipper were sending products abroad for what, under judicial determination, appeared to be no other reason than circumvention of cabotage law, he could be thwarted. A chain of connection test, which would blend features of both the intent and alteration test, is perhaps the best alternative. To illustrate, regard two hypotheticals:

First, a United States mining outfit sells its ore to a Canadian steel manufacturer. In turn, this manufacturer sells its steel to a Japanese auto maker. The company then exports automobiles to the United States for sale. It is clear that the ore has undergone vast changes *and* the original mining firm has lost all control over its ore upon the initial sale. Thus, under this suggested chain of connection test, the autos should not be subject to the Jones Act.

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82. In addition to foreign lands, several United States points enjoy some form of protection from the Jones Act. *See, e.g.*, 46 U.S.C. § 877 (1976) (Virgin Islands); *Id.* § 1664 (Guam, Tutuila, Wake, Midway and Kingman Reef); 48 U.S.C. § 1664 (1976) (American Samoa).

83. Unsubsidized United States shipping costs significantly more than foreign freightage. *See* notes 9-10 *supra* and accompanying text.

84. 590 F.2d at 1168. The court cited appellee's brief in noting that the total value of United States foreign commerce involved in round trip processing and manufacturing was nearly six billion dollars in 1976. *Id.* at n.62.

85. *Id.* at 1168-69.

Second, a United States paper manufacturer harvests a crop of trees, ships them to a plant in Canada where they are processed into an array of paper products, and then controls the return of the goods to the United States for sale. Although a piece of paper is no more a tree than sulfur pellets are crude oil,[86] cabotage restrictions should apply to the paper's entry into the United States. The original manufacturer maintained his connections to and control over the product, and despite its change of character, his ultimate intentions are quite clear. An additional feature of this test might well be a requirement that a certain percentage of the original cargo return to the United States in order for the shipper to be subject to the Jones Act.[87]

This chain of connection analysis would also ease a second problem the circuit court created for itself in *Blumenthal*. As stated, the appellants claimed that the Alaskan crude oil had not undergone sufficient alteration to escape the clutches of cabotage. The court disagreed, though, due to the eleven different products emerging from crude oil. It is unclear, however, where the line is to be drawn in assessing change. The court noted that "the precise point at which a substance subjected to an altering process becomes 'different' eludes simple definition; attempts at a universal description would lead into metaphysical realms which a court should fear to enter."[88] The court nevertheless felt that the case represented a clear choice, so that it could easily determine that Alaskan crude oil had been transformed.[89]

After noting the complexities of the issue, the court's conclusion is somewhat puzzling. For the reasons the court itself acknowledged, simple change of the goods' condition is a wholly unsatisfactory test in gauging the application of coastwise law. Although it has useful elements, the test is best augmented by the traditional notion of intent.

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86. *See* note 71 *supra*.

87. This test is apparently similar to that used by the Attorney General when he ruled that the transportation of fish from an Alaskan port to Vancouver, and then on to United States points was a violation of cabotage law. In this case, the shipper knew that 1) Vancouver was not the product's final destination, and 2) that a certain percentage of the fish would be forwarded to the United States. This ruling was made despite the fact that the fish were stored and dried in a bonded warehouse for four months to a year in Vancouver. 32 Op. Att'y Gen. 350 (1920).

88. 590 F.2d at 1163 n.37.

89. *Id.* at 1162-63.

IV. *SUBSIDIZED VESSELS IN COASTWISE TRADE*

The United States has subsidized the construction of vessels in United States shipyards and the cost of manning those ships with United States crews in order to maintain a competitive merchant marine in foreign commerce.[90] Administered by the Department of Commerce, the Merchant Marine Act of 1936[91] includes in this network of aid operating subsidies;[92] acquisition of new and reconditioned vessels for charter or sale;[93] a loan guarantee program;[94] and the construction-differential subsidy (CDS) program,[95] around which raged a recent storm.[96]

Controversy erupted over the CDS of 27.2 million dollars that the Maritime Subsidy Board[97] approved for Seatrain Shipbuilding.[98] Seatrain, under contract to Polk Tanker Corporation, constructed the 225,000 deadweight ton super-tanker, the STUYVESANT, and, as stipulated in the subsidy agreement, the parties agreed not to enter the vessel into the coastwise trade except as statutorily provided.[99] By the time the vessel was completed in 1977, however, demand for tankers on the world market

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90. 46 U.S.C. §§ 1101-1294 (1976).

91. *Id.* For a short discussion of the available provisions under this act, see Morse, *A Review of the Assistance Provided to the American Merchant Marine Under Statutes of the United States and Their Administration by the Federal Maritime Board and the Maritime Administration, U.S. Department of Commerce*, 18 FED. B. J. 355, 358-59 (1958).

92. 46 U.S.C. §§ 1171-1176 (1976). For a discussion of the government's operating-differential subsidy, see Whitehurst, *The Merchant Marine Act of 1936: An Operational Subsidy in Retrospect*, 8 J. L. & ECON. 223 (1965).

93. 46 U.S.C. §§ 1191-1194 (1976).

94. *Id.* §§ 1271-1280.

95. *Id.* §§ 1151-1156.

96. Seatrain Shipbuilding Corp. v. Shell Oil Co., 444 U.S. 572 (1980), *rev'g sub nom.* Alaska Bulk Carriers, Inc. v. Kreps, 595 F.2d 814 (D.C. Cir. 1979). For a detailed discussion of the Supreme Court's opinion, see Bloom, *Repayment of Construction-Differential Subsidies*, 11 J. MAR. L. & COM. 183 (1980). For an analysis of the D.C. Circuit Court's opinion, see 20 HARV. INT'L L.J. 417 (1979); 4 SUFFOLK TRANSNAT'L L.J. 225 (1980).

97. The Maritime Subsidy Board actually approves all subsidy contracts. 46 C.F.R. §§ 201.1, 251.1 (1980). This Board is a component of the Maritime Administration, which in turn is part of the Department of Commerce.

98. In addition to the CDS program, the Economic Development Administration of the Department of Commerce had advanced to Seatrain five million dollars as a direct loan and had guaranteed 90% of 82 million dollars in loans from other sources to help finance modernization and operation of its Navy Yard facilities and an on the job training program for employees. 595 F.2d at 819-20.

99. *See* note 106 *infra* and accompanying text.

had dramatically declined.[100] Thus, Polk sought to enter the STUYVESANT into the newly opened Alaskan oil trade, which lacked sufficient numbers of tankers because of the Jones Act's prohibition of foreign vessels on domestic routes.[101]

Upon petition by Polk and Seatrain to the Secretary of Commerce, the restriction was lifted because the Secretary felt that: 1) there were no other employment opportunities for the STUYVESANT, 2) the contract which Seatrain had already negotiated for transporting Alaskan oil would strengthen the collateral securing obligations the government had guaranteed, 3) the contract might prevent default on those obligations, and 4) the failure to lift restrictions might jeopardize Seatrain's survival.[102] In exchange, Seatrain had to repay the entire amount of the subsidy, which it was willing to do with twenty-year promissory notes.

United States shipping interests[103] sought to bar this action, claiming the Secretary lacked power to effect such a release. They also claimed that had the Secretary possessed such authority, it was inapplicable in the case of the STUYVESANT.[104] The District of Columbia Circuit and the Supreme Court disagreed sharply in their statutory interpretations of section 506 of the Merchant Marine Act of 1936,[105] with the Supreme Court ultimately deciding that the Secretary possessed such power.[106]

Section 506 provides two explicit exceptions to the coastwise trading ban applicable to subsidized vessels. Congress permitted

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100. This reduction was a direct result of the oil production slowdown undertaken by OPEC. 444 U.S. at 576.

101. 46 U.S.C. § 883 (Supp. III 1979). *See also* MARITIME ASS'N OF THE UNITED STATES, U.S. DEP'T OF COMMERCE, ASSESSMENT OF ALASKAN CRUDE OIL (Aug. 8, 1979) (suggesting an insufficient tanker capacity to handle Alaskan production).

102. Letter of James S. Dawson, Secretary of Maritime Administration, to Polk Tanker Corp. (Aug. 31, 1977). *See* 444 U.S. at 581. In fact, as of this writing, Seatrain Lines, Inc. the parent of Seatrain Shipbuilding, is facing possible bankruptcy and reorganization. It is attempting to remain a viable business by making favorable arrangements with its creditors. Operations have already been suspended, however, at the Brooklyn Navy Yard, the site of the STUYVESANT construction. N.Y. Times, Feb. 10, 1981, at D5, col. 3.

103. The original plaintiffs were Alaskan Bulk Carriers, Inc. and Shell Oil Co., both of which possessed enrolled tankers engaged on Alaskan oil routes. 595 F.2d at 814.

104. 444 U.S. at 579-80.

105. 46 U.S.C. § 1156 (1976).

106. 444 U.S. at 597.

ships to carry domestic cargo on one leg of certain foreign voyages, and permitted vessels to engage in domestic trade for six months or less in any one year upon a finding that such action would be necessary or appropriate to carry out the purposes of the chapter. In order not to prejudice unsubsidized vessels, Congress required that any CDS ship entering domestic trade, under the latter provision, repay that portion of the outstanding subsidy allocable to the vessel's coastwise activities.[107]

The United States Court of Appeals for the District of Columbia Circuit decided that these two specific exceptions framed the limit of the Secretary's power regarding entry of subsidized vessels into the coastal trade. In effect, the court viewed the expansive powers given the Secretary under the rest of the act as immaterial.[108] The court saw that such specificity limited the Secretary's authority to amend construction-differential contracts and his discretion to administer the act.[109]

The Supreme Court overruled this holding. It saw section 506 as a simple mandate that vessels wishing to move in and out of coastwise trading could do so only under the circumstances precisely defined in the act.[110] Thus, the Court reasoned, the statute was addressing only temporary releases.[111] Permanent releases, such as the type sought by the STUYVESANT, are not, therefore, necessarily prohibited by the statute.[112] A permanent release would forever locate a vessel in the "Jones Act Fleet,"[113] thereby permitting it no unfair advantage—such as those possessed by a vessel moving freely between the subsidized and unsubsidized fleets.[114] Where repayment of the subsidy includes an amount equal to capital costs which would have been met had no subsidy been available,[115] a CDS vessel entering the coastal trade enjoys no competitive edge. Consequently, the Supreme Court found

107. 46 U.S.C. § 1156 (1976).

108. Alaska Bulk Carriers, Inc. v. Kreps, 595 F.2d at 836; *see* 46 U.S.C. § 1117 (1976). This section expressly permits the Secretary to make and *amend* CDS contracts.

109. *See* 595 F.2d at 834-35.

110. 444 U.S. at 588.

111. *Id.*

112. *Id.* at 589-90.

113. *See* pt. I *supra.*

114. 444 U.S. at 588-89.

115. The Court noted that the Secretary was intending to apply a reasonable interest rate to the original subsidy amount. This is primarily designed to protect the interests of the unsubsidized fleet. 444 U.S. at 589 n.31.

nothing in section 506 barring a permanent release from a CDS contract.[116]

Both the District of Columbia Circuit and Supreme Court investigated the legislative history of section 506 in arriving at their conflicting conclusions. As originally enacted, the section provided for three releases from subsidy restrictions: 1) incidental tasks in domestic trade requiring a pro rata subsidy repayment, 2) permanent releases requiring full repayment of the amortized portion of the subsidy, and 3) emergency situations requiring no repayment.[117] In 1938, however, section 506 was rewritten into its current form.[118] Two changes were made that resulted in the elimination of the language concerning permanent releases and an alteration in the emergency provision to require a pro rata subsidy repayment. The District of Columbia Circuit concluded that this evidenced Congress' clear intention to remove permanent releases from the list of exceptions.[119] The Supreme Court, however, relying on the amendment's legislative history,[120] believed that Congress was trying only to clarify some ambiguities in the statute, and sought to effect no substantial changes.[121] The Court concluded: "What does seem clear is that [the 1938 amendment] did not represent a considered congressional judgment that the permanent-release/full repayment transaction before us should be prohibited."[122] Thus, subsidized vessels will be permitted into the coastwise trade upon a full subsidy repayment.

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116. *Id.* at 595.

117. Merchant Marine Act of 1936, ch. 858, § 506, 49 Stat. 1999. *Compare* this section and its three explicit exceptions *with* the current version, amended in 1938, 46 U.S.C. § 1156 (1976). *See* note 106 *supra* and accompanying text.

118. 46 U.S.C. § 1156 (1976).

119. 595 F.2d at 829.

120. 444 U.S. at 595-96. The House Report stated that "[n]o fundamental change in the original purpose of this section has been effected." H.R. REP. NO. 2168, 75th Cong., 3d Sess. 21 (1938). The Senate Report identifies the major significance of the changes as making unmistakably clear the owner's obligation to repay his subsidy if he wishes to enter coastwise trade. S. REP. NO. 1618, 75th Cong., 3d Sess. 12-43 (1938).

121. The Court additionally noted that the United States Comptroller General had permitted the GRACE LINE back into the coastwise trade upon full repayment of its subsidy. This vessel had been converted, under subsidy, from a domestic cargo ship into a container vessel equipped for foreign trade. *Id.* at 595. *See* Grace Line Inc., 44 Comp. Gen. 180 (1964). The circuit court had distinguished *Grace Line* from *Seatrain* partially on the grounds that the two subsidies involved were not the same. 595 F.2d at 830. The Supreme Court, however, failed to "see the relevance of this distinction." 444 U.S. at 595 n.40.

122. 444 U.S. at 595.

V. *CONCLUSION*

None of the three decisions examined in this Note modifies Judge Kaufman's well known observation that "the United States treats its coastwise shipping trade as a jealously guarded preserve."[123] Nevertheless, these cases, while hardly revolutionary in and of themselves, when taken together undeniably narrow the grand protectionist design of United States cabotage legislation.

It is now clear that while a renationalized vessel is ineligible for domestic trade, its parts will not necessarily bar a jumboized vessel from coastwise participation. The potential, therefore, exists for a sizeable fleet of partially foreign vessels to ply the domestic trade. Additionally, United States goods processed abroad can be shipped back to domestic points on foreign vessels, regardless of the shipper's intent. As a result, circumvention of cabotage law looms as a distinct possibility. Finally, upon full repayment of its construction subsidy, a vessel is eligible for coastwise trade. The owner of such a vessel is thus afforded the desirable choice of which trade to pursue depending upon market conditions.

Robert W. Gruendel

123. Marine Carriers Corp. v. Fowler, 429 F.2d 702, 703 (2d Cir.), *cert. denied*, 400 U.S. 1020 (1970).