



September 1<sup>st</sup>, 2016

Senator Orrin G. Hatch, Chairman  
Senator Bill Nelson  
Senator Robert Menéndez  
Senator Marco Rubio  
Representative Nydia Velázquez  
Representative Sean Duffy  
Representative Tom MacArthur  
Representative Pedro Pierluisi

The Congressional Task Force on Economic Growth in Puerto Rico  
Vía email: [prtaskforce@mail.house.gov](mailto:prtaskforce@mail.house.gov)

Dear Chairman Hatch and Members of the Congressional Task Force:

On behalf of the Puerto Rico Food Marketing, Industry and Distribution Chamber (MIDA), we are responding to Section 409 of PROMESA which requests this task force to evaluate: “(1) *impediments in current Federal law and programs to economic growth in Puerto Rico including equitable access to Federal health care programs; (2) recommended changes to Federal law and programs that, if adopted, would serve to spur sustainable long-term economic growth, job creation, reduce child poverty, and attract investment in Puerto Rico; (3) ...*” Puerto Rico is suffering a transportation crisis caused by several federal laws, **including the Jones Act of 1920**. Resolving this situation is among the few concrete actions Congress can take that will help the Island be competitive in the long term while not increasing the federal deficit.

MIDA represents the chain of food distribution and retail in Puerto Rico, which imports most of our food items from the US, including agricultural products and food brands. This means that the cost of maritime transportation is vital for the price and availability of food in the Island but also affects US farmers and companies that export to Puerto Rico. Furthermore, local food production is highly dependent on imports of feed, pesticides and other raw materials.

Therefore the importance of a competitive maritime transportation system not only affects the prices of imports but it also affects our food security, our ability to produce locally and ultimately affects our competitiveness in all areas of production. For example, food items are 23% more expensive than the average in the US., according to the Council for Community and Economic Research (C2ER).

The cost of transportation, as well as the higher costs of utilities and labor in the Island, have a greater impact in the competitiveness of local businesses and industries that have limited net margins as opposed to industries such as the pharmaceutical industry. Thus, when considering options to the economic crisis in the Island, the Task Force needs to consider giving Puerto Rico the tools to compete by our own devices in the long term and differentiate them from other equally beneficial and necessary measures that could be taken away by future Congressional actions. We need both.

## Why change the Jones Act now?

The Jones Act of 1920 requires all maritime trade between US ports to be done by ships that are US flagged, US manned, US owned and US built. Even though the Jones Act has been around for 100 years, its impact has recently become intolerable for Puerto Rico. For most of those hundred years, the Jones Act was applied parallel to tariff regulations in ocean transport which prevented commercial abuse. The Interstate Commerce Commission (ICC) and the Federal Maritime Commission (FMC) had regulatory oversight over Jones Act carriers. Tariffs had to be public and "reasonable" and those agencies passed judgment and had public hearings. In 1995, during the deregulation process of all transport in the US, this oversight was eliminated with the ICC Termination Act of 1995. The basic premise was that competition was a better regulator than the government. Unfortunately, there can be little competition under the Jones Act because of the barriers to entry, particularly the lack of US built ships for rent or purchase and the cost of constructing new ones, which can be between three and six times more than an internationally build ship.<sup>1</sup> Nonetheless, in 1996 Congress created a new agency, the Surface Transportation Board (STB), as a substitute for the ICC, 40 U.S.C.A. 13521 (1996), and its main focus is railroad transportation and not ocean transportation. For reasons unknown, Congress maintained the FMC but transferred its oversight over Domestic Offshore Carriers or Jones Act Carriers to the STB. The result was that Jones Act Carriers are now under an agency focused mainly on railroads that has done no oversight or analysis of ocean cargo services since its inception.

Probably the most important aspect of these changes is that Jones Act carriers are not required to file any data on private contracts which in the case of the PR trade account for over 85% of movements. This means there are no direct statistics on the actual costs of transportation from the US to PR even though studies have estimated it to be significant.<sup>2</sup> This information is extremely important to an island that depends on this mode of transportation. In contrast, the FMC oversight of international carriers does require the filing of service contracts for oversight purposes. There is no reasonable explanation for this difference.

**As a consequence, the prevailing law (the Jones Act) imposes a legally mandated cartel on the Island and as it would be expected of an oligopoly that has no oversight.** Indeed, the carriers began fixing prices and were **convicted for Antitrust violations** with plea agreements as recent as 2012. (USDCPR – Case No. 3:11-cr-00511-DRD and 3:12-cr-00590-DRD) These cases against the companies were followed by criminal cases against their executives, private class actions and independent law suits which cost the Puerto Rico economy millions of dollars in excess shipping charges precisely during the beginning of its current economic depression. It is unclear if prices were adjusted after these cases were settled, but what is clear is that the DOT or the STB, the agencies that should oversee the market, have not taken any specific actions or acknowledgement that there is clearly a problem in the Puerto Rican ocean trade.

Also during the early 90s, the US began signing free trade agreements with other nations in the region such as with México, Central America and the Dominican Republic, providing access thru customs for their products and vice versa. As a consequence PR lost the important competitive advantage of being inside the US customs system. In terms of transportation, those nations not only have the liberated customs access and some have direct land access, but they also don't have to use the more expensive US merchant maritime in their trade thus exacerbating the existing competitive disadvantages to Puerto Rico.

---

<sup>1</sup> [https://www.marad.dot.gov/wp-content/uploads/pdf/Comparison\\_of\\_US\\_and\\_Foreign\\_Flag\\_Operating\\_Costs.pdf](https://www.marad.dot.gov/wp-content/uploads/pdf/Comparison_of_US_and_Foreign_Flag_Operating_Costs.pdf) at page 50.

<sup>2</sup> For instance, in 2012 the Federal Reserve Board of New York found that, while it cost \$3,063 to ship a container of food and commercial goods from the US mainland to Puerto Rico, it cost only \$1,504 and \$1,687 to ship the same container to the Dominican Republic and Jamaica, respectively – that's approximately 50% less for the same shipment to neighboring islands.

<https://www.newyorkfed.org/medialibrary/media/regional/PuertoRico/report.pdf>

Furthermore, in January 2015 the largest carrier serving the Island, Horizon Lines, left the market. Horizon had 30% of the market and it was the only carrier operating ships, not barges, from the 3 main connecting ports to PR - NJ, Jacksonville and Houston. This created a huge logistical problem for the Island that has yet to be resolved. **There are now 2 companies with over 80% of the US-PR market.** They are geographically concentrating cargo movements in the port of Jacksonville and the once important northeast route is being served only by barges, not ships, and by only one company. Barges take more than twice the time to make the trip as ships and are thus not ideal for transporting perishables. It is important to consider this also hurts US suppliers that now only have limited barge service from the northeast and only a twice a month service from Houston.

**Therefore, the Jones Act imposes not only significant direct costs on imported products and raw materials but also indirect costs caused by the lack of competition and the abuse of market power of the two main carriers.** What's more, the concentration of 85% of cargo movements between the US and PR in only one port is obligating US shippers to PR to incur in costly land transportation, an important factor that needs to be added to the equation.

Clearly, this has been an enormous contributor in the current economic depression of the Island and is a colossal impediment to future growth that this task force needs to address.

### **It's about costs but also lack of competition**

There are two basic concepts are involved in the analysis of the transportation problems of Puerto Rico -- the importance of maritime transportation for an island and the importance of competition as the ideal means to achieve efficient and cost effective services and products in any market.

Because the Jones Act of 1920 requires all maritime trade between US ports to be done by ships that are US flagged, US manned, US owned and US built, international trade has not been affected. This may explain why most US states are not even aware of its existence or simply feel it is of no consequence. The initial objective of this Act was to guarantee the US with a merchant marine in case of emergencies and war. But it has failed because the US Merchant Marine has never been lower in numbers after almost a 100 years of the supposed protections of the Jones Act and other laws with similar purposes. The main reason is that higher operating costs and ship construction costs make the US flagged vessels less competitive than carriers using international flags.

The Maritime Administration (MARAD) did a study on 2011 confirming US ship owners and operators prefer to register under international flags because they are 2.7 times less expensive and shipbuilding three times cheaper.<sup>3</sup> In fact, it was US carriers that founded most of those foreign "registries of convenience" because they do not want to use the US flag unless they are forced to, have guaranteed cargo, or have a "closed market" as is the case of Puerto Rico, Alaska and Hawaii. Of those, Puerto Rico is by far the poorest and the largest market, therefore it is disproportionately hit by the added costs. It is also the only US territory where the Jones Act fully applies.

In this respect, it is important to highlight the hypocrisy of the US carriers that defend the Jones Act when they themselves do not operate under the US flag when serving international markets. This is even more obvious in the case of the carriers serving Puerto Rico, because they service all our neighbors in the Caribbean and

---

<sup>3</sup> COMPARISON OF U.S. AND FOREIGN-FLAG OPERATING COSTS, MARAD Sept. 2011. [https://www.marad.dot.gov/wp-content/uploads/pdf/Comparison\\_of\\_US\\_and\\_Foreign\\_Flag\\_Operating\\_Costs.pdf](https://www.marad.dot.gov/wp-content/uploads/pdf/Comparison_of_US_and_Foreign_Flag_Operating_Costs.pdf)

Central America with internationally flagged ships, sometimes from the same ports that they service Puerto Rico. It also rejects their theory that they can't compete without the Jones Act and that port employees could be at risk if the Jones Act was amended.

### **Alternatives to end the cartel regime and allow competition**

1. **Exclude PR from the Jones Act** – *All other US territories are totally or partially excluded, even our neighbors the US Virgin Islands.* In fact, the carriers that currently serve PR also operate throughout the Caribbean and Central America with ships registered internationally. This fact reduces the likelihood that Jacksonville port employees would be impacted since the same companies can serve the Puerto Rico market without the Jones Act as they are already doing in the region. If anything, port employees may benefit from more cargo being moved and the entrance of new competitors.
2. **Temporary complete exemption** - It will allow for new competitors and increased service while providing Congress the data to evaluate a permanent exemption. It could even be considered for certain routes, such as the northeast that currently has no ship providing service. This was proposed by the Federal Reserve Bank of NY in 2012 for a 5 year term.<sup>4</sup> But the temporary status could deter any significant investment and new entries.
3. **Give PR a partial exemption of the US built requirement** – Even partial exemption limited to the US built requirement would provide great relief to PR. This was also proposed by the NYFED in 2014 in an update to the 2012 report.<sup>5</sup> It should also be supported by labor groups since the carriers would still have to be US owned ships and the crew would have to be of US citizens. US shipbuilders should not be significantly impacted since the current carriers that would conceivably order new ships have already done so and based on past experience no new ships will be ordered for 40 years.
4. **Regulation** - In addition to the above, the feasibility of regulation has to be considered. The US cannot allow a cartel, whose members have been convicted of price fixing, to control an essential service to an island without some reasonable controls, especially when it is in deep economic and fiscal trouble. For example the FMC, which regulated Jones Act carriers until 1996, regulates international ocean transportation more effectively than the STB oversees the Jones Act trade. In essence, basic economic principles establish that when faced with excessive market concentration governments need to either break the excessive concentration or provide strong oversight.

In fact, the alternative of regulation is supported by the transportation policy set forth in section 13101(a)(1)&(4) of the ICCTA, 49 U.S.C.A. (1996), referring to its statutory goals “to promote safe, adequate, economical, and efficient transportation; to encourage the establishment and maintenance of reasonable rates for transportation, without unreasonable discrimination or unfair or destructive competitive practices;...(and) to **encourage and promote price competition** in the noncontiguous domestic trade.”

Following these goals, Congress, in apparent premonition of the risks, directed the Department of Transportation in 1996 to do a study of:

- 1) Carrier competition in both regulated and unregulated portions of those trades;
- 2) Rate structure in those trades;
- 3) The impact of tariff filing on carrier pricing;

---

<sup>4</sup> Id <https://www.newyorkfed.org/medialibrary/media/regional/PuertoRico/report.pdf>

<sup>5</sup> <https://www.newyorkfed.org/medialibrary/media/outreach-and-education/puerto-rico/2014/Puerto-Rico-Report-2014.pdf>

- 4) The problems of parallel pricing and its impact on competition in the domestic trades;
- 5) The impact of domestic cargo pricing of foreign cargo services;
- 6) **Whether additional protections are needed to protect shippers from abuse of market power; and**
- 7) The extent to which statutory or regulatory changes should be made to further the transportation policy of section 13101 of title 49, USC.

Unfortunately, in compliance with this mandate, the DOT did a report in March 1997 titled “Competition in the Noncontiguous Domestic Maritime Trades” that relied on information submitted by interested parties with little independent or government data. In the area of competition, it acknowledged the markets were very concentrated but it argued that the entrance and exits of competitors in the previous years meant that carriers could not unreasonably raise prices or others could enter the market. (Proven wrong by the antitrust cases) It concluded that even though shippers argued there was parallel pricing between carriers, they found no clear evidence. (Again proven wrong by the price fixing cases). They also concluded that while the public comments provided suggestions for additional protection, no respondent provided clear evidence to justify further investigation by the DOT. (Also proven wrong by the price fixing cases)

In 2006 the DOT with the Maritime Administration (MARAD) published another report with the same title. Surprisingly, it admits that such powerful agencies didn’t have data on the subject so they relied on a study by a private firm, Reeves and Associates, prepared for the Maritime Cabotage Task Force, a group that defends the Jones Act carriers. This admission seriously undermines its credibility.

In any case, after 2006 the competitive and economic situations of Puerto Rico have changed dramatically and what the DOT said would not happen became a reality; the principal carriers were convicted for price fixing. In addition, the largest market under the Jones Act has further concentrated and although antitrust laws have been useful, they are inadequate because they presume an open market. Finally, the Puerto Rico economy is collapsing unlike any other jurisdiction subject to the Jones Act. Thus the mandate of Congress for “protecting shippers from abuse of market power” and the promotion of price competition have not been adequately fulfilled and need to be revisited.

Specific areas of possible regulation:

- a. Provide solutions to unacceptable market concentrations such as;
  - a. Waivers to the Jones Act necessary to attract new competitors;
  - b. Control of tariffs and service contracts until healthy competition exists;
  - c. Provide authority to break those with extreme market power into smaller competitors.
- b. Make the filing of private service contracts mandatory on the STB or move the Domestic Carriers back to the jurisdiction of the FMC where they do have to be filed. This will provide the agency with the required data to actually fulfill its statutory goals.
- c. Provide the agency in charge, STB or FMC, with a specific mandate of publishing independent and reliable statistics on actual transportation costs in the domestic ocean trades. This will provide transparency to the market and allow shippers to better negotiate their rates.
- d. Provide the agency with greater oversight capability to protect shippers. For example: establish priorities of cargo during an emergency or mandate the report of lack of cargo space on ships; mandate weekly reports of cargo left in port due to lack of space. This would also help in determining if the level of available service is adequate for the demand.
- e. Make the agency responsible for promoting competition in the trade and provide guidelines of an unacceptable market concentration. (Antitrust regulations have developed criteria) As

demonstrated in the DOT studies, this is not possible without reliable data so this recommendation relies on the previous.

- f. Reduce the zone of rate freedom that currently allows annual rate increases of 7.5% to less than 3%. The 1997 report by the DOT recommended this. In any case, the agency needs to be actively evaluating the reasonableness of changes. Also, the definition of “rate” needs to include “tie in” or related services, fees, or charges such as the bunker surcharge, demurrage, chassis use, etc.
- g. Allow shippers to negotiate collectively with ocean carriers over rates and conditions of service. (Recommended by the DOT in the 1997 study)
- h. Define and prohibit certain practices. Provide shippers the tools and protection to enforce and request relief to the agency.
- i. Urgently request the STB a report on what it has done to comply with its statutory goals “to promote safe, adequate, economical, and efficient transportation; to encourage the establishment and maintenance of reasonable rates for transportation, without unreasonable discrimination or unfair or destructive competitive practices;...(and) to **encourage and promote price competition** in the noncontiguous domestic trade.”
- j. Request truly impartial new study on the competitive situation of the markets, barriers to entry, and to provide additional solutions. This study needs to be made by the Federal Trade Commission or the Antitrust Division of the Department of Justice, as the GAO and the DOT have failed to see the main problem, lack of competition. (There are examples of congressionally approved languages requiring this type of studies on Section 407 of the Interstate Commerce Commission Termination Act of 1995 but even better language was included in 49 U.S. Code § 10706 - Rate agreements: exemption from antitrust laws, because it specifically assigns the responsibility to the Federal Trade Commission)

In summary, the lack of competition on domestic ocean trade is not new and it has proven to be a greater problem than ever before, particularly in light of the antitrust convictions of the carriers serving Puerto Rico and the further concentration caused by the closing in 2015 of one of the largest carriers serving the Island. The Jones Act is but one aspect of this problem of competition and market concentration, but is the first issue that should be addressed. **Most importantly, it can be addressed without any cost to the Federal government.**

### **Other proposals that can help bring growth**

The economic problems of the Island are complex so a comprehensive approach is needed. We argue that the task force should give priority to those proposals that provide the Island with competitive tools to promote new investments and employment, such as Jones Act relief, but there are other proposals that can help.

Continuing with the matter of cabotage laws, there is an equivalent for air transportation that limits international air carriers from transporting cargo or passengers between two US airports. We favor the proposal to consider excepting Puerto Rico as it was done with Alaska because it is consistent with promoting free trade. Nonetheless, we have to clarify that most cargo movements are done by sea and that air cabotage laws do not require airplanes to be US built as is the case with the Jones Act so this proposal would be a complement, not a substitute, to Jones Act relief.

As mentioned before, the tax break proposal that is being put forward by our sister organization, The Puerto Rico Manufacturers Association (PRMA), needs to be seriously considered. It is clear that the current

economic crisis was greatly accelerated, if not caused, by the repeal of the tax benefits of Section 936 of the US Internal Revenue Code.

We would also urge the task force to consider the areas of labor and energy costs. Related to the labor costs is the welfare system that currently is dissuading people to work and can be reformed in order for it to become an incentive to work by subsidizing employment. Likewise, Congress should look at providing a payroll tax holiday, similar to that approved recently to help the struggling US economy, which would have an immediate effect on the economy and possibly help generate employment.

MIDA stands ready to brief you and your staff on these important issues at your convenience. Please let us know if we can provide any additional information.

Cordially,



Manuel Reyes, Esq.  
Executive Director  
Puerto Rico Food Marketing, Industry and Distribution Chamber (MIDA)  
Tel. (787) 792-7575  
[mreyes@midapr.com](mailto:mreyes@midapr.com)  
90 Carr. 165 STE #501  
Guaynabo, PR, 00968-8058