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The OECD Shipbuilding Agreement and Legislation in the 105th Congress

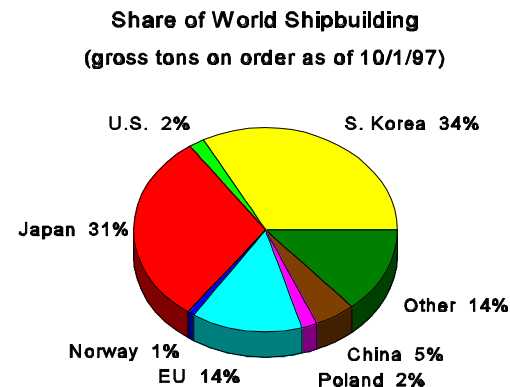
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Summary

In December 1994, the United States, the European Union, Japan, Korea, and Norway signed an agreement on shipbuilding that was negotiated under the Organization for Economic Cooperation and Development (OECD). The agreement prohibits most subsidies for shipbuilding, limits financing assistance, allows actions against injurious pricing, and establishes a dispute resolution process. Although the United States was the lead proponent of the agreement, it is the only signatory that has not ratified the agreement. U.S. maritime industries are split. The largest shipyards oppose the agreement without modifications such as a longer phase-out of the U.S. vessel financing guarantee program. Mid-level shipyards and vessel operators support the agreement, primarily for its provision to end most shipbuilding subsidies. Legislation to approve the agreement and make necessary statutory changes has been introduced in the 105th Congress.

The OECD Shipbuilding Agreement

The “Agreement Respecting Normal Competitive Conditions in the Commercial Shipbuilding and Repair Industry” was negotiated under the auspices of the Organization for Economic Cooperation and Development (OECD). Signatories are the European Union, Japan, Korea, Norway, and the United States, which currently represent about four-fifths of world shipbuilding (see figure). They signed the Agreement in December 1994. The United States is the only signatory that has not ratified the Agreement.



Source: U.S. Maritime Administration.

Negotiation of the Agreement began as a result of action by U.S. shipbuilders. In 1989, the Shipbuilders Council of America, which at the time included the largest U.S. shipyards among its membership, asked the U.S. Trade Representative (USTR) to investigate the subsidy practices of Korea, Japan, Germany, and Norway. The U.S. shipbuilding subsidy program had ended in 1981, commercial orders for large oceangoing vessels had fallen to zero, military programs were being cut back, and foreign subsidies continued. The Shipbuilders Council filed its petition under section 301 of the Trade Act of 1974, as amended, which authorizes remedial action (e.g., raise tariffs) if the Administration concludes that another country is engaged in unfair trade practices. The Shipbuilders Council eventually withdrew its petition with the understanding that the USTR would seek a multilateral end to shipbuilding subsidies through either the OECD or the Uruguay Round of negotiations.

After 5 years of negotiation under OECD auspices, countries concluded an agreement that provides for elimination of noncompetitive support measures, compensatory charges for injurious pricing, and dispute settlement proceedings.

Elimination of Noncompetitive Measures. With some exceptions, the Agreement requires the elimination of subsidies (e.g., grants, tax credits, loan guarantees on preferential terms) for vessel construction and repair. It allows exceptions for ongoing restructuring programs in Korea and in Belgium, Portugal, and Spain.¹ The Agreement states that domestic build/repair or domestic content requirements, including regulations such as cargo reservation programs linked with domestic shipbuilding, would have to be eliminated.

The United States alone reserved the right to retain domestic build requirements for coastwise shipping. The foremost coastwise law is the “Jones Act” (Merchant Marine Act of 1920), which requires that goods transported between points in the United States be on U.S.-built ships documented under U.S. law (U.S.-flagged) and owned by U.S. citizens. The Agreement requires the United States to report on vessels contracted for coastwise transport. Other Agreement countries may be permitted to take action against U.S. shipyards that build coastwise vessels if such construction undermines the balance of rights and obligations reached under the Agreement. During the first three years of the Agreement, a finding that actual or expected deliveries of coastwise vessels will exceed 200,000 gross tons per year is required before responsive action may be considered.²

Injurious Pricing. This section of the Agreement is consistent with U.S. antidumping law. An Agreement country may impose an injurious pricing charge on a foreign shipbuilder if the Agreement country finds the foreign shipbuilder sold a vessel at

¹ The restructuring assistance to Belgium, Portugal, and Spain includes but is not limited to assistance for social measures such as worker adjustment and to assistance for costs incurred before signing of the Agreement but not yet paid due to budgetary problems. The Agreement specifies amounts, deadlines, and purposes of assistance under this exception.

² In the Agreement, the United States estimates that average deliveries of coastwise vessels subject to the Agreement will not exceed 200,000 gross tons per year. U.S. negotiators affirm that past deliveries of such vessels never reached this level. Opponents of the Agreement warn that the level could be exceeded and countermeasures could apply.

less than fair value to a buyer in the country and the sale injured or threatened to injure a shipbuilder in the country. The foreign shipbuilder has 180 days to pay the charge.

Under a third-country provision, a shipbuilder in a third Agreement country can seek action if it has been injured or threatened with injury by the sale of a vessel at less than fair value to a buyer in another Agreement country. In this case, the country of the injured shipbuilder would approach the country of the buyer about imposing an injurious pricing charge on the builder of the delivered vessel.

Dispute Proceedings. The Agreement provides for dispute proceedings when there is a complaint about actions covered by the Agreement, e.g., a support program or injurious pricing. A party may request consultations about a complaint. If a solution is not found through consultations, a party can ask for a decision by a dispute panel. The panel's decision is binding unless all of the Agreement countries reject it.

Other Provisions of the Agreement. The Agreement covers seagoing vessels of at least 100 gross tons and excludes military and military reserve vessels and modifications for military purposes. It states that such vessels and modifications should not be disguised commercial construction. It excludes fishing vessels for the building country's fishing fleet.

The Agreement requires close monitoring of support measures. Each party must report on prices and credit terms for ships sold and on proposed assistance to the shipbuilding industry. They must provide extensive data such as ownership, financial statements, and capital contribution for shipyards building larger vessels.

The date for entry into force was January 1, 1996; however, the Agreement provided that if one or more of the signatories had not ratified it by then, the date for entry into force was 30 days after the last country's ratification.

Legislation in the 105th Congress³

Legislation to implement the OECD Shipbuilding Agreement was considered but not enacted during the 104th Congress (1995-1996).⁴ New implementing legislation is being considered during the 105th Congress. Legislation includes changes to U.S. law that are necessary to implement the Agreement. It also includes provisions that are related to shipbuilding but are not necessary under the Agreement.

Legislative Provisions to Implement the OECD Agreement. Current U.S. antidumping law does not cover unfair pricing for trade in vessels because of the unusual nature of this trade. Implementing legislation proposes to add a new title to U.S. trade law to cover unfair pricing in shipbuilding. Some provisions of the new title provide that when a U.S. buyer purchases an unfairly priced vessel, an injured industry can petition an

³ For information on current legislation on the OECD shipbuilding Agreement, see CRS Issue Brief 98007. *The OECD Shipbuilding Agreement and Implementing Legislation*, by (name redacted).

⁴ See CRS Report 96-775 E. *The OECD Shipyard Agreement: Background and Status*, by Kenneth R. DeJarnette.

investigation by the U.S. Trade Representative. The new title would authorize the imposition of an unfair pricing fee if there is a negative finding against the shipbuilder.

Implementing legislation also would eliminate domestic-build or domestic-content requirements in U.S. law that are not allowed under the Agreement. Among the U.S. programs that would be amended to meet this obligation are: (1) the current duty levied on repairs of U.S.-flag vessels in a foreign shipyard; (2) tax deferral on deposits by U.S. operators into funds for construction of U.S.-built ships; and (3) cargo preference programs that favor U.S.-built ships. Proposed legislation would give the same treatment to ships built in any of the signatory countries.

The Agreement calls for an end to subsidies in the form of loan guarantees on preferential terms. One such loan guarantee program is the Title XI maritime program, which provides for a government guarantee of debt obligations by U.S. or foreign shipowners for the construction of eligible vessels in U.S. shipyards. To implement commitments reached under the OECD, legislation would have to amend the Title XI program. Many experts estimate that the Title XI guarantee program will become less attractive and offer reduced support to U.S. shipbuilding as a consequence.

Legislative Provisions Related to the Shipbuilding Agreement. Among other provisions that might be included in implementing legislation is a proposal to allow more time for shipbuilders to adjust to the change in the Title XI guarantee program. Large shipbuilders had been dependent on military orders through the 1980s, but these orders fell, and builders turned to commercial orders supported by the Title XI program. The large shipbuilders have argued for a longer phase-out for the Title XI program than the OECD Agreement allows. Questions that might be considered during debate on the legislation include how long a phase-out period is optimal for U.S. shipbuilders, and the consequences of a phase-out period that differs from that in the Agreement.

Some opponents of the OECD Agreement have argued that the definition of “military vessels” should be a national, not international, decision. Supporters of the Agreement respond that each signatory country cannot decide on its own which vessels will fall under the Agreement and which will not, otherwise the Agreement will fail. Some legislative proposals would authorize U.S. officials, in particular the Secretary of Defense, to decide which vessels will be defined as “military” and therefore be exempt from the shipbuilding Agreement. Other proposals seek to more clearly define “military vessels” by statute.

A third issue that might be addressed in other legislative provisions is the level of protection for U.S. shipyards that build vessels for coastwise trade (trade between U.S. ports, or “Jones Act” trade). Coastwise trade is now reserved for U.S.-built vessels. The Agreement allows other signatories to take action against U.S. shipyards that build Jones Act vessels, but only if certain conditions are met. Proposals for legislation address whether coastwise trade should be more strongly protected, and whether the United States should continue to participate in the Agreement if another country eventually takes punitive action.

Analysis

The most serious opposition to the OECD Agreement and the implementing bill comes from major U.S. shipyards. The six largest U.S. shipbuilders withdrew from the

Shipbuilders Council and are now represented by the American Shipbuilding Association. Their position is that the Agreement does not end subsidies because foreign shipbuilders can continue to receive aid through restructuring provisions and other “loopholes.” The large shipyards oppose any change to the Title XI program because they say that the program is the reason U.S. shipyards are again building large commercial vessels. They insist that if Title XI benefits must be given up, a long transition should apply. The major shipbuilders argue that the injurious pricing mechanism will be ineffective because the strongest protections apply only when a U.S. buyer makes the purchase, but U.S. buyers represent a small share of vessel purchases worldwide. (To the extent that shipyards in other signatory countries are hurt by a purchase, they can seek an injurious pricing charge through the third-country provisions.) They argue that Jones Act vessels and military reserve vessels are not adequately protected, and point out that some major shipbuilding nations, for example, China, are not parties to the Agreement and can continue to subsidize their yards.

Second-tier shipyards, represented by the Shipbuilders Council, and ship operators support the OECD Agreement and implementing bill. They argue that the United States will not return to construction subsidies, so the best way to help U.S. shipyards is to agree on a set of rules where other countries limit their subsidies. The mid-sized yards say that Title XI helps U.S. shipbuilders now because other countries agreed to freeze support when they signed the Agreement, but once the other countries decide that the Agreement is not going into force, they will subsidize again and wipe out any benefit from Title XI. Supporters of the Agreement also argue that any expectation of negotiating another agreement is unrealistic because it took 5 years to reach this deal and the United States is not in a strong negotiating position because it already unilaterally ended its own subsidy program.

The Agreement’s requirement to reduce subsidies for shipbuilding represents a potentially large benefit to the U.S. domestic industry, since the United States has no subsidy program and other countries do. The Title XI program has been crucial for some ship orders and some shipyards, especially the largest shipyards, which have depended on Title XI guarantees in the face of severe cutbacks in military shipbuilding. The importance of Title XI to the entire U.S. shipbuilding industry and naval defense base might be weighed against possible opportunities rising from the subsidy restrictions. The Agreement allows U.S. coastwise trade to continue to be protected, but permits countermeasures if all signatories decide U.S. construction of coastwise vessels disrupts other signatories’ markets. Although it is not clear how the Agreement might affect the defense fleet, it is unlikely the United States would stay in a commercial agreement that it perceives jeopardizes its national defense.

Some opponents have called for renegotiation of the Agreement to obtain better terms for the U.S. industry. U.S. negotiators could attempt to reach agreement on new terms, but other countries have indicated unwillingness to participate in a renegotiation and even so would expect U.S. concessions if the terms were changed. Countries might question the mandate of U.S. negotiators without some assurance that an agreement will be approved back home. Fast-track procedures would assure a congressional vote and would not allow for amendments to an implementing bill, but these procedures do not apply to the shipbuilding Agreement. The Agreement’s original date for entry into force has passed, and signatory countries have begun to subsidize their shipyards again. A

congressional vote on the Agreement will decide whether the United States agrees to those rules to govern shipbuilding.

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