DEPARTMENT OF JUSTICE

STATEMENT

OF

CHARLES A. JAMES
ASSISTANT ATTORNEY GENERAL
ANTITRUST DIVISION

BEFORE THE

COMMITTEE ON THE JUDICIARY
U.S. HOUSE OF REPRESENTATIVES

CONCERNING

H.R. 1253, THE FREE MARKET ANTITRUST IMMUNITY REFORM ACT OF 2001

PRESENTED ON

JUNE 5, 2002

Good morning, Mr. Chairman and Members of the Committee. It is a pleasure to appear before this Committee to state the Department of Justice's support of H.R. 1253, a bill that would remove the antitrust exemption for ocean carriers from the Shipping Act of 1984. The bill would phase out the exemption for intercarrier agreements after one year, while not affecting the immunity for marine terminal operators.

The Department of Justice believes that competition under the antitrust laws is the way to provide consumers with the best products and services at the most affordable prices. That is the general rule applicable to virtually every sector of the American economy and has served our Country, its economy and its businesses and consumers extraordinarily well. In certain limited circumstances, more aggressive or less restrictive antitrust rules may be appropriate. We do not believe that the ocean shipping industry exhibits extraordinary characteristics that warrant departure from normal competition policy or the application of the antitrust laws.

Price fixing and other anticompetitive practices by ocean shipping conferences over the years have imposed substantial costs on our economy through higher prices on a wide variety of goods shipped by ocean transportation. In the current era of expanding globalization of trade, in which we are ever more dependent upon an efficient transportation system, it is important that our public policy promote full and open competition.

Brief History of Antitrust Exemptions in Ocean Shipping

Since the Shipping Act, 1916, there has been an exemption, in one form or another, from the antitrust laws for ocean shipping carriers to engage in rate discussions and price-fixing agreements. Congress has revisited the issue at various times over the years, but thus far has not yet enabled the competition generally applicable to the rest of the economy to apply to ocean shipping. It is time to do so now.

While outlawing certain specified monopolistic conference practices, the 1916 Act expressly conferred an exemption from the antitrust laws for conference agreements on shipping rates, pooling arrangements, and shipping route allocations, as long as those agreements were first submitted to and approved by the newly created U.S. Shipping Board (the body that eventually became the Federal Maritime Commission).

Following enactment of the 1916 Act, conferences began making extensive use of "dual rate" contracts to bind shippers to the conferences and stave off non-conference carrier competition. These dual-rate contracts, also referred to as "loyalty contracts," offered discounted rates to shippers who agreed to use only conference carriers. The Supreme Court ruled in Federal Maritime Board v. Isbrandtsen Co., 356 U.S. 481 (1958), that dual rate contracts violated the Act.

In the wake of the Isbrandtsen decision, Congress amended the 1916 Act in 1961 to permit dual-rate contracts, though limiting the permissible discount to 15 percent. At the same time, Congress also amended the Act to require the filing of tariffs, transferred the Board's authority to an independent Federal Maritime Commission, and gave the Commission the power to disapprove agreements between and among carriers that were "contrary to the public interest."

In 1984, Congress substantially rewrote the 1916 Act. The Shipping Act of 1984 broadened the antitrust exemption for carrier agreements and streamlined the regulatory process for those carrier agreements. The exemption from the antitrust laws was expanded to cover not only agreements that had gone into effect under the Act, but also activities, "whether permitted under or prohibited by this Act," if they were undertaken "with a reasonable basis to conclude" that they were pursuant to an effective agreement. The antitrust exemption was further expanded

to cover intermodal through rates incorporating rail, truck, and ocean legs. The 1984 Act abolished the Commission's public interest standard for reviewing carrier agreements. A carrier agreement would no longer require Commission "approval," but would go into effect -- and thereby become immunized from the antitrust laws -- 45 days after filing or submission of any additional information requested by the Commission. As a result of the 1984 Act, once an agreement has been filed, the only way it can be challenged**,** as anticompetitive**,** is if the Commission seeks to have a court enjoin the agreement on grounds that it is "likely, by a reduction in competition, to produce an unreasonable reduction in transportation service or an unreasonable increase in transportation cost." (To the best of our knowledge, the Commission has never filed such a challenge.) The 1984 Act otherwise retained the common carrier provisions of the 1916 Act, as amended in 1961, under which the conferences were required to file published tariffs with the Commission, as well as the list of specified prohibited acts. The Act provided for the use of service contracts in limited circumstances.

Next came the Ocean Shipping Reform Act of 1998. The 1998 Act took some notable competitive steps, but it stopped short in some important respects. On the procompetitive side, the 1998 Act guarantees that conference members can take "independent action" on service contracts–that is, can negotiate service contracts with a shipper at rates that differ from the conference tariff -- and thereby compete for large volumes of business by offering discounted rates. The 1998 Act improves on the 1984 Act not only by requiring shipping conferences to permit individually negotiated service contracts, but also by helping protect carriers from anticompetitive pressure from the conferences by prohibiting the conferences from requiring

carriers to disclose the rates in those service contracts and by eliminating the requirement that the negotiated rate be made available to all similarly situated shippers.

However, the 1998 Act also allows conference members to adopt so-called "voluntary" guidelines regarding individual service contracts, which a conference can use, along with its already significant influence over its members, to signal them as to expected behavior. At a minimum, this can be used to discourage vigorous competition with respect to individual service contracts.

These and other provisions of the 1998 Act perpetuate the conference system, either by facilitating intercarrier agreements that would be unlawful in the absence of an exemption or by restricting the ways in which conference members can meaningfully compete on an individual basis for the business of large and small shippers alike. The conference system could not exist in the absence of an antitrust exemption.

Such an exemption no longer makes sense, especially at a time when countries all over the world are turning to competition, rather than antitrust exemptions and regulation, as the best hope for economic prosperity.

There are No Good Rationales for the Antitrust Exemption

We know the benefits of competition: low prices, innovative service, and efficient operations. Yet shippers -- and consumers -- have been denied the full benefits of competition because carriers have been able to persuade policy makers over the years that the ocean shipping industry has certain characteristics that make it necessary to protect carriers from competition.

Supporters of the antitrust exemption for ocean carriers have been reciting essentially the same rationales from the beginning. The rationales tend to fall into two categories: those based

on the economics of shipping and those based on the international nature of the business. Whatever may have been the force of those rationales at the time the exemption was first enacted in 1916, they have become increasingly dubious in the years since, and are particularly so in the current economic and legal environment. They do not justify a departure from the competitive principles that other industries throughout our country -- and much of the world -- have come to live by.

A consistent theme of those supporting an antitrust exemption, rather than competition, has been that carriers need protection from the consequences of "too much" competition. Absent an exemption to allow collective decisionmaking by carriers, the fear expressed has been that carriers would engage in rate wars that might result in certain carriers being unable to cover their capital costs, which would ultimately drive these inefficient carriers out of the market.

In other words, carriers should be exempt from the antitrust laws because, absent the ability to collude, shipping costs would be lower. In our view, this is a seriously flawed public policy. As the General Accounting Office stated in a 1982 report to Congress, a primary objective of shipping conferences "is to increase the profits realized by their members as a group." This is why cartels form. But simply because competitors desire to collude in order to inflate their joint profits does not mean that it is good public policy to allow them to do so. In fact, the contrary is true.

Furthermore, this rationale is difficult to accept, even on its own terms. Arguments based upon concerns about "ruinous" or "destructive" competition are often made, but are virtually never substantiated. Congress has heard them many times before, often with respect to transportation industries such as railroads, airlines, and motor carriers. At one time or another,

each of those industries was subject to pervasive federal regulation and enjoyed a broad exemption from the antitrust laws. Over time, however, each of them has been substantially deregulated and the applicable antitrust exemption has been curtailed or eliminated, with the result that competition has increased for shippers and consumers, and without the horrible consequences predicted by industry. In fact, economists have often found that a "regulated" cartel yields the worst of both worlds: high prices and low profitability, as companies over-invest in capacity and lose the incentive to innovate and operate efficiently. Certainly, the ocean shipping exemption has not saved U.S. carriers.

Another rationale for the exemption has been that the international character of ocean shipping somehow made it inappropriate to subject the industry to the antitrust laws. The notion has been that it would be unfair to apply U.S. antitrust laws just to U.S. carriers, but that attempting to apply them to foreign carriers as well would provoke our trading partners. Whatever may have been the validity of such a concern many decades ago, it has no continuing validity today. There has been no doubt for many years that U.S. antitrust laws can properly be applied to foreign persons engaged in commerce with the U.S. and that the transportation of freight between the U.S. and a foreign country falls well within that principle. Thus, foreign carriers serving the U.S., no less than U.S. carriers serving the U.S., are subject to our antitrust laws with respect to those activities. Furthermore, in the intervening years, foreign governments have made a pronounced shift to embrace free-market competition and to adopt and apply antitrust laws. Indeed, it is ironic to note that the most significant recent antitrust enforcement action with respect to ocean shipping in U.S.-Europe trades was taken by the European Commission a few years ago, when it imposed fines on U.S. and foreign carriers operating

between the United States and Europe after determining that they had exceeded the scope of the applicable European exemption. This puts to rest any contention that it would be inappropriate, as a matter of fairness or comity, for the United States to apply its antitrust laws to carriers operating to or from the U.S.

Perhaps a final rationale -- and one that reflects both the economics and the international character of shipping -- is that some foreign countries subsidize their state-controlled carriers and operate them for reasons other than profit. This was a significant concern to U.S.-flag carriers in the 1970s, but Congress has already dealt with that. The Shipping Act of 1984 gave the Commission power to disapprove rates of such carriers that were below a just and reasonable level.

In our view, the case for a broad exemption from the antitrust laws has never been a strong one and is especially weak today. Congress has acted decisively over the past 25 years to deregulate other transportation industries -- railroads, airlines, and motor carriers -- and the predictions that ruinous competition would harm carriers and consumers alike never came to pass. The case for continuation of the antitrust exemption for ocean carriers is no stronger. Indeed, at a time when the U.S. model of deregulation -- coupled with appropriate antitrust enforcement -- is winning converts around the world, the antitrust exemption for ocean shipping is badly out of step with the times.

Conclusion

Mr. Chairman, the 1998 Act took an important but limited step forward toward more competition in ocean shipping. The Department of Justice believes that the proposed legislation would firmly establish competition as the touchstone for this important industry. We believe that

the ocean shipping marketplace can benefit, no less than other industries, from healthy competitive market forces safeguarded by appropriate antitrust enforcement.

The Department of Justice urges Congress to enact your legislation and allow competition to flourish in ocean shipping -- subject only to our antitrust laws. A competitive marketplace protected by the antitrust laws will do more than the most carefully constructed regulatory scheme to allow competitive forces in the ocean shipping industry to benefit consumers, shippers, the economy, and ultimately the ocean shipping industry itself.