PUBLICATION

Customs Reverses Course on Proposed Change to Jones Act Interpretation

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The “Jones Act,” enacted in 1920 as section 27 of the Merchant Marine Act, is the principal law governing wholly domestic shipping to and from American “ports” and “coastwise points,” commonly known in the maritime industry as “cabotage” or “coastwise trade.” The Jones Act supports the important purposes of national defense and the development of domestic and foreign commerce by requiring a U.S.-flagged merchant marine fleet – built, owned and crewed by American citizens – that is sufficient to maintain the flow of waterborne commerce, domestic and international, and able to support the U.S. military in times of war or national emergency.

While the Jones Act's central dictates may appear straightforward on their face, a clear application and interpretation of the statute has remained elusive since enactment. Particularly in recent decades, many questions of key importance to the maritime industry have arisen, including (1) what constitutes a U.S. “port” or “coastwise point;” (2) what is “merchandise” that must be carried between U.S. ports or points on U.S. vessels; and (3) in what instances are vessels “wholly owned by citizens of the United States.” In large measure, the governmental entities charged with enforcing and administering the Jones Act must resolve these questions, including the U.S. Maritime Administration (MARAD), U.S. Customs and Border Protection (CBP or Customs) and the U.S. Coast Guard.

One key issue that Baker Donelson maritime attorneys continue to monitor closely is a proposed rule change introduced by CBP that if implemented will significantly affect the rights of non-U.S. vessels to transport construction materials from American ports to offshore oil and gas well sites, principally in the Gulf of Mexico. Although controversy surrounding the proposed rule change led CBP to withdraw it pending further study, it is expected that Customs will reintroduce a proposed rule change in the near future. This article examines the significance of the proposed changes to U.S. Coastwise law, why they were controversial and what may lie ahead for water-borne transportation between U.S. ports and offshore installations.

It has long been established that the Jones Act's dictates apply to many of the structures commonly used in off-shore resource exploration operations, provided those structures are secured to or submerged onto the seabed of the Outer Continental Shelf (OCS). In this circumstance, the structures attached to the OCS, which include mobile drilling rigs, drilling platforms, artificial islands and anchored warehouse vessels, constitute “points in the United States to which the coastwise laws apply,” barring foreign-built vessels from conducting any coastwise trade with these structures. But in a seminal 1976 ruling, Customs concluded that, with respect to vessels that provide diving operation support to offshore oil and gas production structures, “the use of a vessel in laying pipe is not a use in the coastwise trade of the United States” because “the pipe is not landed but only *paid* out in the course of the pipelaying operation.”

Through other rulings, Customs has also recognized an important distinction between “merchandise,” which can only be carried between U.S. coastwise points by a coastwise-qualified vessel, and “vessel equipment,” which can be carried between coastwise points by foreign vessels, broadly characterizing “vessel equipment,” as examples, to encompass items carried “in furtherance of the primary mission of the vessel,” “in furtherance of the operation of the vessel” or “essential to the mission of the vessel.” To constitute “equipment,” Customs has not required that an article be necessary to the navigation, operation and maintenance of the vessel, or to the comfort and safety of the individuals aboard the vessel. Examples of articles found to constitute

“equipment” include “rope, sail, table linens, bedding, china, table silverware, cutlery, bolts and nuts.” Applying the distinction made, several Customs rulings have reasoned that items that are “paid out” and not “unladen” are vessel equipment. In other words, Customs has historically held that the paying out of pipe, cable, flowlines and umbilicals is permissible because these items are “vessel equipment” carried in furtherance of the vessel's mission, such that there is no “landing of merchandise” and therefore, no engagement in coastwise trade.

What CBP's proposed change means for offshore oil and gas operations. On July 17, 2009, CBP published a notice in which it proposed modifying its position on what constitutes “merchandise” and non-merchandise “vessel equipment” for purposes of the Jones Act. In that notice, CBP was critical of many of its own prior rulings, finding that certain key parts of seminal rulings had been ignored in later determinations, or taken out of context. For example, CBP posited that the initial requirement that carriage of pipeline materials must be “incidental to the pipe-laying function” of a vessel had been ignored in later rulings allowing non-U.S. vessel carriage of materials to be installed on previously laid or installed pipelines. Thus, CBP suggested that unless its installation was part of the original pipeline laying or “paying out” process, carriage of underwater equipment for installation on a well or related structure on the OCS by a non-U.S. vessel would be a violation of the Jones Act, potentially carrying a severe penalty, including seizure of the cargo or a fine equivalent to its value or the freight for its carriage, whichever is greater.

CBP also criticized prior rulings that characterized items as “vessel equipment” (not merchandise) even if they were not necessary to the vessel's navigation, operation or maintenance, or to the safety and comfort of the persons aboard the vessel. For example, a 2003 CBP ruling found that non-coastwise qualified liftboats could transport compressors, generators, pumps and pre-fabricated structural components from a U.S. port to a coastwise point on the OCS without violating the coastwise laws since such equipment was “fundamental to the mission of the vessel” to support oil and gas well drilling, construction and repair. According to the notice, such rulings took concepts in earlier rulings out of context, and violated the intent of the Jones Act. CBP suggested that such equipment, characterized in some rulings as “vessel equipment” that could be carried by non-U.S. vessels, were in fact “merchandise” that must be carried by Jones Act-qualified vessels.

Reaction to CBP's proposed change. The proposed change, if implemented, would invariably have a significant economic impact on the maritime industry, favorable to U.S. vessels and adverse to foreign-built vessels. In light of this significance, numerous interested parties and industry groups responded to CBP's requested comments on its proposed re-interpretation of the Jones Act in relation to offshore oilfield operations.

The Offshore Marine Service Association (OMSA) came out in favor of the proposed changes: Ken Wells, OMSA's president, noted, “With this proposal, CBP is saying that there is a hard line between transportation and installation. Foreign boats may be able to install oilfield equipment, but only U.S. boats can carry it offshore. . . .The problem is that for many years, CBP rulings had allowed foreign vessels to carry cargo to subsea oil and gas locations as long as that vessel also installed it.”

Foreign vessel owners, unsurprisingly, opposed CBP's proposal. The International Marine Contractor Association (IMCA) claimed it would shut down offshore projects due to a lack of coastwise qualified vessels and trained personnel to take over work now being performed by foreign-flagged vessels. OMSA responded that American vessels were in fact available, and that the CBP proposal would protect existing U.S. jobs. OMSA urged offshore oil and gas companies to support the CBP proposal, saying that opposing the CBP initiative was tantamount to saying, “We don't want Americans to work in offshore energy at a time when we are arguing that expansion would create jobs.”

Withdrawal of ruling and the future. The proposed changes proved controversial, evidenced by the extent of comments received, ultimately leading to their recent withdrawal by Customs, effective October 1, 2009,

pending further study. As part of its withdrawal, Customs indicated that it would publish a new notice “in the near future.” Because CBP is again expected to receive comments on its future proposed revision, persons interested in a proposed change would be wise to carefully review any upcoming proposed change.

Related movements are also underway seeking legislative support for increased “short sea” domestic shipping to reduce highway congestion, cut diesel exhaust and lessen wear and tear on our bridges and highways. Some have advocated for relaxing the Jones Act to support this effort, and vigorous debate continues. In his campaign for President, Barrack Obama expressed strong support for the Jones Act, calling into question the potential viability of an effort to limit the Jones Act's applicability. As to future changes to the Jones Act, whether by a Customs ruling or by legislation, one thing is certain: any changes will meet immediate scrutiny and vigorous debate among the many parties interested in the development of U.S. oil and gas reserves, domestic short sea shipping and a strong U.S. Coastwise fleet. Baker Donelson's marine and energy attorneys are closely monitoring significant Jones Act rulings and changes, and will keep readers informed of future events.