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FEDERAL MARITIME COMMISSION

46 CFR Parts 571 and 572

[DOCKET NO. 93-23]

ADVANCE NOTICE OF PROPOSED RULEMAKING
CONCERNING SECTION 6(g) OF
THE SHIPPING ACT OF 1984

AGENCY: Federal Maritime Commission.

ACTION: Advance Notice of Proposed Rulemaking.

SUMMARY: The Federal Maritime Commission is considering whether it should issue regulations or guidelines that would describe the Commission's enforcement policy with respect to section 6(g) of the Shipping Act of 1984, which authorizes the Commission to seek an injunction against substantially anticompetitive agreements. This Advance Notice of Proposed Rulemaking recounts the background and legislative history of section 6(g), describes the Commission's procedures for evaluating and monitoring agreements, sets forth a possible section 6(g) guideline, and seeks comment on whether published guidelines would be useful and appropriate and, if so, what form they should take.

DATES: Comments due on or before (insert date 60 days after publication in the Federal Register).

ADDRESS: Send comments (original and 20 copies) to:

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SUPPLEMENTARY INFORMATION:

The Federal Maritime Commission ("Commission" or "FMC") is considering the advisability of promulgating some form of public statement that would describe the Commission's analytic framework for determining whether an agreement filed pursuant to the Shipping Act of 1984 ("1984 Act") should be made the subject of an injunctive action under the standards of section 6(g) of that Act, i.e., whether the agreement, by a reduction in competition, is likely to produce or has produced "an unreasonable reduction in transportation service or an unreasonable increase in transportation cost." 46 U.S.C. app. 1705(g).

To date, statements by the Commission and opportunity for public comment regarding the section 6(g) general standard and the extent of the Commission's powers under it have been limited.[1]

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[1] On February 12, 1992, the Advisory Commission on Conferences in Ocean Shipping ("ACCOS") held a public session to consider alternative antitrust standards. The FMC's staff briefed ACCOS on the Commission's section 6(g) review and monitoring procedures and their underlying rationale. However, ACCOS's final report did not comment on the FMC's interpretation of section 6(g). (See Report of the Advisory Commission on Conferences in Ocean Shipping, April 1992, p. 82.)

This Advance Notice of Proposed Rulemaking is intended both to provide a vehicle for increasing public awareness regarding the FMC's regulation of agreements under the 1984 Act, and to provide a means for input from shippers, carriers, government agencies and other interested persons on whether, in what form, and with what degree of specificity, publication of section 6(g) methodological guidelines would be helpful to the ocean transportation industry and the shipping public. The Notice recounts the background and legislative history of section 6(g) and describes the Commission's procedures for evaluating and monitoring agreements. It then sets forth a possible section 6(g) guideline and solicits comments on the guideline's contents and format.

Commenters may also suggest, if they wish, possible alternative methods of providing public guidance with regard to section 6(g). Such alternatives could include instituting a rulemaking such as that undertaken in FMC Docket No. 78-46, Financial Reports of Common Carriers by Water in the Domestic Offshore Trades, in which the Commission established its methodology for determining what constitutes a reasonable rate of return in the domestic offshore trades; publishing a set of specific guidelines similar in format to the Horizontal Merger Guidelines issued jointly by the Department of Justice and the Federal Trade Commission; or issuing a general statement of policy in the Commission's regulations under 46 CFR Part 571, Interpretations and Statements of Policy.

A. The Section 6(g) Standard

1. Background

Section 15 of the former Shipping Act, 1916 ("1916 Act"), required carriers to secure Commission approval for any agreement governing rates, conditions of service, or similar matters, before such an agreement could become effective. Under standards set forth in section 15, the Commission was permitted to disapprove, cancel, or modify any agreement which it found to be unjustly discriminatory or unfair, or to operate to the detriment of the commerce of the United States, or to be contrary to the public interest, or to be in violation of the Act. 46 U.S.C. 814 (1982).

The Commission, with Supreme Court approval, took the position that agreements to set rates, pool revenues, restrict capacity, or to engage in other activities that normally would be contrary to the antitrust laws were presumed to be contrary to the public interest, and would be approved only if they were shown to be "required by a serious transportation need, necessary to secure important public benefits or in furtherance of a valid regulatory purpose of the Shipping Act." FMC v. Svenska Amerika Linien, 390 U.S. 238, 243 (1968). The burden of making this showing was placed upon the carrier proponents of an agreement, on the theory that information regarding the operation and probable future impact of an agreement "[a]lmost uniformly . . . is in the hands of those seeking approval . . . and it is incumbent upon those in possession of such information to come forward with it." Mediterranean Pools Investigation, 9 F.M.C. 264, 290 (1966). Under these procedures,

the implementation of agreements was often delayed for considerable amounts of time, especially if formal protests were made. See Marine Space Enclosures, Inc. v. FMC, 420 F.2d 577 (D.C. Cir. 1969) (requiring that the Commission hold a hearing where a protest raising substantial issues had been filed). In many cases, protests were filed by other carriers, who effectively delayed or blocked the approval of their competitors' business plans.

The 1984 Act removed the Commission's broad discretion to disapprove agreements. Instead, under section 6(c), properly filed agreements generally become effective automatically after forty-five days. 46 U.S.C. app. 1705(c). To balance this liberalized approach to agreement review, the 1984 Act sets forth an extensive list of prohibited acts, barring many anticompetitive practices which previously had been challenged under the general standards of section 15. This shift in regulatory approach reflects a decision by Congress "to strike the overall balance between competition and cooperation in specific provisions of the act," rather than to vest in the Commission broad discretion to approve agreements. H.R. Rep. No. 600, 98th Cong, 2d Sess. 34 (1984) ("Conference Report"). Section 10(c) of the 1984 Act prohibits conferences and groups of carriers from engaging in, inter alia, boycotts, predatory practices, unreasonable refusals to deal, and allocation of shippers among specific carriers. 46 U.S.C. app. 1709(c). Section 10(b) bars carriers from engaging in a variety of unfair practices, such as granting secret kickbacks to shippers, retaliating against

a shipper who has patronized another carrier, and refusing to negotiate with a shippers' association. Id. 1709(b).

Further procompetitive provisions of the 1984 Act are set forth in section 5(b), 46 U.S.C. app. 1704(b), which includes a list of terms which must be incorporated in every conference agreement. For example, conferences must allow, on equal terms and conditions, open admission (and readmission) for any carrier willing to serve a particular trade, and must permit any member to withdraw without penalty. Especially noteworthy is the requirement that all conference agreements must clearly state that any member line may take "independent action" on any rate or service item required to be filed in a tariff with the Commission; that is, any member line may opt to set an individual rate below (or above) the conference rate. The conference is required to publish the independent action rate in its conference tariff upon ten days' notice. In addition, the 1984 Act authorized carriers and conferences to enter into service contracts with shippers covering cargo volume, rates and service.[2]

In addition to its authority to enforce the specific prohibitions and mandatory provisions in the 1984 Act, the Commission also has the power, under section 6(g), to seek an injunction in federal district court against an agreement which is

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[2] Congress did not, however, extend the independent action requirement to conference member lines' ability to enter into service contracts with shippers. As part of the overall compromise underlying the 1984 Act, section 4(a)(7) expressly authorizes conferences to "regulate or prohibit" members' use of service contracts. 46 U.S.C. app. 1703(a)(7).

"likely, by a reduction in competition, to produce an unreasonable reduction in transportation service or an unreasonable increase in transportation cost." This is the only way the Commission can prevent the operation of an agreement, either before or after it first goes into effect. Unlike the former agreement review process under the 1916 Act, the Commission carries the burden in an injunctive suit of showing that an agreement fails to meet the section 6(g) standard.

Although the language of section 6(g) is relatively brief and non-specific, the accompanying legislative history makes clear that the statute is not a mandate for the Commission to apply a broad "public interest" standard to maritime agreements. Instead, the Conference Report sets forth in uncommon detail the nature of the section 6(g) standard and the appropriate analysis to be performed pursuant to it. The Report also states unequivocally that it is intended to govern the interpretation of section 6(g). Conference Report at 32. The relevant section of the Conference Report (pages 31-37) is appended to this Notice for convenient public reference.

2. The Conference Report

The analysis prescribed by Congress has two distinct requirements -- a substantial reduction in competition, and an unreasonable increase in transportation cost or an unreasonable decrease in transportation service.

The Report gives specific instructions to the FMC regarding substantial reductions in competition. The Commission is directed not to place undue emphasis on the market share of the parties.

While the Commission can use market share analysis, it may be neither determinative nor necessary. This directive contrasts with traditional antitrust analysis, which posits that high levels of market concentration lead to significant market power. For example, Congress noted that although a conference may have a significant market share, its market power may be mitigated by the 1984 Act's mandatory independent action and open membership provisions. Further, the Report contemplates that some agreements might include all the carriers in the trade (i.e., 100 percent market share), without transgressing the overall purposes of the 1984 Act:

> In some forms of concerted activity, participation by all or virtually all the members of a trade is necessary if the agreement is to have the desired effect on problems of overcapacity or rate instability.

Conference Report at 34. Regarding the relevant competitive market, the Commission is instructed to consider an agreement's impact on shippers not only in the terms of competition between carriers in the subject trade, but also in terms of other competitive means of transport.[3]

Congress further stated that a substantial reduction in competition is a necessary but not a sufficient condition for the FMC to seek injunctive relief. Such relief may be obtained only if an unreasonable increase in transportation cost or an unreasonable reduction in service to shippers would likely result from the

[3] Suggested competitive alternatives may include alternative liner routings, and service provided by bulk carriers, charter operators or air freight carriers.

substantial reduction in competition. This unreasonableness requirement contains two distinct aspects -- a finding of unreasonable harm to shippers and a balancing of that harm against the agreement's benefits to the industry.

Again, the Conference Report sets forth specific requirements for both aspects. The harm to shippers must be unreasonable "in a commercial context." Conference Report at 35. The likely changes in cost and service must be derived from the agreement, and be "material and meaningful." Id. Congress did not further define these concepts. It stated, however, that the Commission may not determine that rate increases are per se impermissible, since such actions "may be necessary to achieve other benefits of the Act," id., such as allowing carriers "room to develop new and innovative cooperative ventures for dealing with changing technologies and customer needs," id. at 32-33, while still realizing a "reasonable return" on their investment. Id. at 34. Also, when determining unreasonableness, the FMC is barred from resorting to the public utility ratemaking analysis it applies to the domestic offshore trades.

The second aspect of the unreasonableness requirement involves determining whether the negative impact upon shippers may be offset by the benefits of an agreement. With respect to conferences, Congress stated:

> . . . the competitive harm ensuing from conferences, already diminished by the statutory limitations on conference activity, can and often will be offset by significant benefits of such activity.

Conference Report at 36.

Congress enumerated a number of benefits for Commission consideration: a conference's ability to address the problems of overcapacity and rate instability, an agreement's impact on foreign policy and international comity, U.S.-flag participation in a trade where restrictive cargo preference practices exist which would otherwise limit or prohibit their participation, and efficiency-creating aspects of agreements (e.g., cost reduction, economies of scale, and technological innovation).

Additionally, the Commission is not to "wear blinders" in its analysis under the general standard by ignoring other reasonable and commercially proven alternatives which may create less competitive harm with most or all of the essential benefits. Conference Report at 36. While the Commission may consider such alternatives and seek to enjoin an agreement if it knows of a less damaging arrangement, Congress did not wish a return to the "public interest" standard where proponents are compelled to show that no less anticompetitive alternatives are available. In general, the Commission is to discharge its responsibilities under section 6(g) "in light of the historic [sic] international acceptance of carrier conference agreements"[4] and with a view to the "long-term interests of carriers and shippers." Id. at 33.

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[4] The Report points out that "the major economic allies of the United States continue to tolerate or even support conference and other cooperative carrier activity, in many cases in a measure far stronger than our laws have tolerated." Conference Report at 33. For example, the Treaty of Rome extends a blanket exemption from its competition rules for liner conferences, without any equivalent to the 1984 Act's provision for independent action.

B. The Commission's Agreement Review Program Under Section 6(g)

Bearing in mind the new responsibilities and limitations imposed by section 6(g) and the other provisions of the 1984 Act, the Commission has developed and refined its processes for evaluating and monitoring agreements. When an agreement is filed, it is immediately reviewed by attorneys in the Commission's Office of General Counsel and by transportation analysts and economists in the Bureau of Trade Monitoring and Analysis. These offices scrutinize agreements to insure that they contain the mandatory provisions set forth in the 1984 Act, and to determine whether they run afoul of the prohibited acts sections or the general standard of section 6(g). Some types of agreements are also subject to specific informational requirements; rate-fixing, revenue pooling, joint service and consortium agreements are required to submit an Information Form, which provides cargo carryings and market share information for the past year and identifies competitors and the nature and extent of that competition. Agreements that contain the authority to alter service are required to provide specific information on changed port calls or reduced sailings.

Because the Commission's responsibility under section 6(g) does not end with the initial filing of an agreement, the FMC maintains an extensive program of ongoing information collection and trade monitoring. Depending on each agreement's anticompetitive potential, monitoring is performed on either a periodic or a continuous basis. Most effective agreements are required to file reports, including Minutes of Meetings, Shippers'

Request and Complaint Reports, Consultation Reports, and, if applicable, descriptions of space chartering activity. Also, the Commission's monitoring group routinely prepares economic reports on trade-wide and agreement-wide bases, as well as individual economic profiles on ocean carriers.

Both of these agreement oversight functions -- pre-implementation review and post-implementation monitoring -- are performed pursuant to the section 6(g) standard, as discussed below.

1. Substantial reduction in competition

In assessing whether or not an agreement substantially reduces competition, the Commission must first identify the relevant market. In the case of pre-implementation review of an agreement, the Commission generally will consider the relevant market to be defined by the scope of the agreement. However, if elements of the agreement suggest its major impact will be on a particular country, port range, or commodity group, the definition of relevant market can be adjusted accordingly. The market definition also could be adjusted in a case where a specific class of shippers appeared to be without alternative service options.

Once the appropriate market is defined, such factors as chronic overcapacity, barriers to entry or exit, pre- and post-implementation market concentration, recent rate and service trends, and foreseeable impacts of specific agreement activities will be considered in the Commission's analysis. Factors such as the type of the agreement (for example, pooling, conference,

discussion) or its organizational structure (for example, inclusion of both conference members and non-conference carriers in a discussion agreement) also may be significant. Further, the statutory provision for independent action on tariff rates must be taken into account, because it fosters intra-agreement competition. The same would be true if the agreement allows for service contracts, and especially if it allows for independent action on service contracts.

In the case of post-implementation analysis of an agreement, market definition will depend on the identity of the class of any shippers allegedly harmed by the agreement. Thus, the relevant market definition may be either narrower or broader in terms of geographic scope or commodities than the scope of the agreement. Once the relevant market is defined, the Commission can then examine the evidence concerning capacity utilization, barriers to entry and exit, market concentration, independent action, etc., to determine if a substantial reduction in competition has occurred as a result of the agreement's actions.

2. Material and meaningful shipper harm

As regards harm to shippers, the adjectives "material" and "meaningful" are qualitative rather than quantitative terms. Therefore, judgments about what constitutes meaningful and material harm must be made in the context of the specific injury being alleged.[5] However, the Conference Report notes that increases in

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[5] Indeed, as previously discussed, the Conference Report specified that harm to shippers is "to be understood in a commercial context."

rates or decreases in frequency or variety of service cannot be viewed as _per se_ violations of the section 6(g) standard. Conference Report at 35.[6]

In the case of pre-implementation review of agreements, there can be no evidence of actual shipper harm. Consequently, any Commission effort to enjoin an agreement prior to its implementation necessarily would involve an estimate of that agreement's likely economic impact. Such estimates ordinarily must be made without knowledge of what rate increases the parties to the agreement intend to enact. Furthermore, the 1984 Act's provision for independent action undercuts the application of simple market concentration assumptions (_i.e._, high concentration equals effective market power).

On the other hand, post-implementation monitoring offers the possibility of obtaining empirical evidence of anticompetitive behavior, and thus a greater likelihood of being able to demonstrate material and meaningful harm to some identifiable class of shippers. The extent of actual rate increases or service reductions can be calculated, as well as the effects of those increases or reductions on particular groups of shippers.

It should be noted that, in order for the Commission to convince a federal district court that an agreement should be enjoined because it has caused material and meaningful harm to

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[6] In addition, the Commission no longer has authority to review the level of specific rates. The 1984 Act repealed section 18(b)(5) of the 1916 Act, which empowered the FMC to disapprove any rates found to be "so unreasonably high or low as to be detrimental to the commerce of the United States." 46 U.S.C. 817(b)(5) (1982).

shippers, active and voluntary shipper assistance almost certainly would be necessary. Information concerning such relevant factors as the extent of individual shippers' rate increases or service reductions, percentage increases in product costs, revenue losses, lost orders, lost market share, employment cutbacks, reduced investments, etc., is not otherwise available to the Commission. Unless shippers were able and willing to provide such information and to provide testimony in court if necessary, any injunctive suit by the Commission would likely be unsuccessful.

3. Experience under the section 6(g) standard since 1984

To date, the Commission has not been presented with a situation which met Congress's standard for seeking an injunction under section 6(g). The chronic condition of excess capacity in many of the U.S. liner trades, and economic recessions in the United States, Japan and Western Europe, have placed pressure on carriers to keep rates and services at competitive levels. Moreover, the procompetitive provisions of the 1984 Act, especially the right to take independent action on tariff rates, have fostered competition among agreement parties and served to discourage unreasonable rate increases and service reductions. It has become apparent that, while the reforms of the 1984 Act greatly accelerated the effectiveness of ocean carrier agreements, they also substantially weakened the power of traditional conferences to maintain rate increases or other conference-wide pricing

decisions.[7] In some cases, potentially problematic agreement provisions have been addressed through negotiation, or corrected after the Commission formally requested additional information or took other action. In particular, the Commission has not been presented with financial data or other substantial evidence from shippers or shippers' groups documenting actual "material and meaningful" harm from any agreement, which is an essential

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[7] In an effort to find a new way to stabilize rates, carriers in two major trades formed agreements with "capacity management programs." The Transpacific Stabilization Agreement ("TSA") is a cooperative working arrangement among thirteen carriers in the inbound trade from the Far East to the United States, which permits the carriers to withhold up to eighteen percent of their collective container capacity from the market, but has no binding ratemaking authority. The Trans-Atlantic Agreement ("TAA") is a conference with binding ratemaking authority among certain members and voluntary ratemaking authority applicable to others, and allows the fifteen members of the agreement to withhold up to twenty-five percent of their collective capacity in the inbound trade from North Europe to the United States.

Agreements that authorize capacity management programs raise significant regulatory concerns, because they potentially can create an artificial shortage of container space by reducing supply to a level below demand, which, in turn, may result in unreasonable rate increases. In addition, both TSA and TAA operate with substantial market shares in their respective trades.

When TSA and TAA were filed, the Commission formally requested historical and forecasted data on the parties' vessel deployment, cargo demand, and capacity utilization in the affected trades. From its analyses, the Commission concluded that neither of the Agreements' proposed capacity management programs should unduly impact on the supply of container space. However, because of the Agreements' importance, the Commission has continually monitored their impact on their respective trades using, among other resources, informational reports on the parties' rate activities, services, and capacity utilization. Thus far, the Agreements have not caused any shortage of vessel space; on the contrary, under both Agreements, there remained a significant margin between vessel space supply and cargo demand, even after the artificial reduction of supply effected by the capacity management programs. This has kept the TSA and TAA carriers under significant price and service pressures, and stimulates intra-conference competition.

prerequisite for the final step in the section 6(g) analysis, i.e., a weighing of the agreement's economic costs against its benefits.

4. Analysis of Economic Costs and Benefits

If the Commission should encounter an agreement where there is evidence meeting Congress's requirement of material and meaningful harm to shippers, it would then be necessary to perform the final step in the section 6(g) analysis prior to seeking a court injunction. Convincing evidence of agreement-generated shipper harm, even substantial harm, is not sufficient to warrant Commission action under section 6(g). The Conference Report specifies that "the negative impact upon shippers may be offset by the benefits of the agreement." Conference Report at 35. Therefore, it would be necessary for the Commission to identify any such benefits, and to establish an appropriate process for weighing the benefits of the agreement against its costs before seeking an injunction.

The first task would be made somewhat easier by the fact that the Conference Report identifies, in general terms, some of the benefits that Congress wants the Commission to consider. These include, but need not be limited to, reducing overcapacity and improving rate stability, creating economic efficiencies (e.g., reducing costs, attaining economies of scale, promoting technological innovation), insuring that U.S. lines can compete with state-sponsored and controlled carriers, and assisting in the achievement of foreign policy goals and the maintenance of international comity.

The second step -- comparison of the benefits purportedly flowing from an agreement with the demonstrable shipper harm that results from it -- is analogous to the standard formerly applied to agreements under section 15 of the 1916 Act, which compared anticompetitive impact with public interest benefits. Actual reduction of overcapacity and identifiable technical and operational efficiencies that depend on cooperative action among agreement members should be relatively amenable to quantification. Evaluation of benefits of a less concrete nature (e.g., international comity), or those attributed to some future period (e.g., long-term price and service stability) would be necessarily more subjective, but, again, would not represent a new task for the Commission. Under section 15, the issue of whether to approve an agreement was often resolved on the basis of anticipated benefits, e.g., Agreement No. 57-96, Pacific Westbound Conference Extension of Authority for Intermodal Services, 19 F.M.C. 291, 301-304 (1976), or international comity, e.g., Agreement No. 9932 -- Equal Access to Government-Controlled Cargo and Interim Cooperative Working Arrangement, 16 F.M.C. 293, 306 (1973). It should be noted, however, that to conduct an adequate analysis, the Commission would need specific information from the carriers, some of a proprietary nature. For example, information on carrier revenues, fixed and variable input costs, cost reduction and efficiency enhancement measures, anticipated rate levels and revenues, and projections on future cargo levels likely would be required.

Once all the relevant information had been obtained, the Commission could then conduct its analysis of the agreement's economic costs and benefits. In general terms, one way of conducting such an analysis would involve the following steps:

1. Identify the affected parties.

2. Identify the short-term and long-term costs of the agreement to each of the affected parties.

3. Identify the short-term and long-term benefits of the agreement to each of the affected parties.

4. Value the costs and benefits monetarily, where possible, and identify all non-quantifiable costs and benefits.

5. Discount all identified and valued costs and benefits occurring at different times at the appropriate discount rate.

6. Aggregate the present-valued costs and benefits.

7. Perform a sensitivity analysis[8] on the major costs and benefits (especially any that are unquantifiable or uncertain).

8. If the present-valued net benefits of the agreement are positive (i.e., if benefits outweigh costs), determine if there are any "reasonable and commercially proven alternative arrangements" that would achieve similar benefits at a lower net cost.

Technical issues such as the appropriate discount rates, inflation assumptions, multiplier effects, etc., could be handled,

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[8] Sensitivity analysis involves changing the parameters of a decision problem and studying how this affects the outcome. It is particularly associated with cost-benefit analysis, where the most common form is the use of alternative discount rates.

to the degree possible, in accord with the provisions in the Office of Management and Budget's benefit/cost analysis guidelines.[9]

C. Request for Comment

Interested members of the public, including carriers, shippers and governmental bodies, are invited to comment on the draft Section 6(g) Guideline set forth below. As previously stated, commenters may also suggest alternative methods of providing guidance with regard to section 6(g).

GUIDELINE

Upon filing with the Commission, an agreement and its information form will be subject to pre-implementation review to determine whether or not it should be made the subject of an injunctive action under the standards of section 6(g) of the 1984 Act. In addition, the agreement will be subject to on-going monitoring. The following guidelines outline the present pre- and post-implementation 6(g) review processes.

Pre-implementation 6(g) Review

A. The Commission will define the relevant market to be used in evaluating the agreement. Normally, at the pre-implementation review stage, that market will be determined by the geographical scope of the agreement and will be limited to the liner shipping industry. However, in some cases the market may be defined by country, port range, commodity group, or class of shipper most likely to be affected.

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[9] Office of Management and Budget Circular No. A-94 Revised, (Transmittal Memorandum No. 64), October 29, 1992.

B. The Commission will assess the agreement's likely economic impact on the market. Consideration will be given to available vessel capacity in the market, barriers to entry or exit, pre- and post-implementation market concentration, the effect of mandatory IA provisions and other prescribed procompetitive requirements, recent rate and service trends, type of agreement involved (for example, pooling, conference, discussion), organizational structure of the agreement, and any foreseeable impacts of proposed agreement activities such as a capacity management program.

C. If the Commission determines that further information or clarification is needed to properly evaluate whether the agreement is likely to violate the section 6(g) standard, it may seek additional information from the filing party pursuant to section 6(d) of the 1984 Act.

D. In the event that the Commission determines that the agreement is likely, by a reduction in competition, to unreasonably increase transportation costs or decrease transportation service, it will inform the filing party of its objections. If those objections cannot be redressed by negotiation, the Commission may then seek an injunction in federal district court as provided in section 6(h) of the 1984 Act.

Post-implementation Agreement Monitoring

A. The Commission will define the relevant market to be used in monitoring the agreement. In the absence of specific shipper allegations of harm, the market will be defined in the same

manner as for a pre-implementation review. If the Commission has received credible allegations of material and meaningful harm owing to activities undertaken by agreement members pursuant to the terms of the agreement, consideration will be given to the particulars of the allegations in defining the scope of the market.

B. The Commission will determine if the agreement has resulted in a reduction in competition that has increased transportation costs or decreased transportation service as applied to either (a) the market as a whole, or (b) specific groups of shippers alleging material and meaningful harm. In the case of a post-implementation review, consideration will be given to the actual behavior (for example, increases in transportation costs, decreases in transportation service, capacity limitations, etc.) of member lines under the agreement in addition to the elements considered in a pre-implementation review.

C. The Commission will determine whether evidence is available of material and meaningful harm to a specific class of shippers and the credibility and utility of such evidence for seeking injunctive action under section 6(g). Such evidence, which would by its nature have to be provided by shippers alleging harm, would include data on individual rate increases or service decreases, increases in product costs, revenue losses, lost orders, lost market share, employment cutbacks, reduced

investments, etc., that are attributable to transportation cost increases or service decreases.

D. Should the Commission determine that the agreement has resulted in a reduction in competition leading to an increase in rates or decrease in service, and that, as a consequence, a specific group of shippers has suffered meaningful and material harm, it will undertake an economic analysis to determine if the short and/or long-term benefits of the agreement outweigh the harm to shippers. Where possible, benefits will be expressed in monetary terms. Such analysis will give consideration to any subsidization that may exist, that is, where the rates charged shippers under the agreement do not cover the carrier-parties' variable costs.

E. Any economic analysis of costs and benefits would require specific information from the carriers which is not available from other sources. To obtain such information, the Commission may direct the carriers involved in the trade -- possibly including carriers who are not members of the agreement -- to provide the information pursuant to section 15 of the 1984 Act.

F. Based on all available information, and following the general method outlined in the Advanced Notice, the Commission will decide whether to bring suit in the United States District Court for the District of Columbia to enjoin the operation of the agreement.

By the Commission.

Joseph C. Polking
Secretary

APPENDIX

(CONFERENCE REPORT)

(31) SECTION 6(g) AND (h)

A. Background--Differing approaches in House and Senate bills

The new general standard in section 6(g) represents a compromise of approaches taken in the Senate and House Bills.

The provision would authorize the Federal Maritime Commission to seek injunctive relief against agreements that it determines do not meet the standard set forth in the subsection. This flexible standard permits the Commission to seek an injunction even when an agreement would not violate any of the prohibited acts set forth elsewhere in the bill.

The Senate bill contained no general standard. It did not authorize Commission disapproval of agreements except for violation of specified requirements (the Commission could also authorize special investigations of, but not immediately disapprove, certain pooling agreements). The Senate approach reflected a view that review of agreements under the general standard of the present Shipping Act, including the "public interest" test, places too much weight on antitrust principles and that the present standard is too vague to provide clear guidance to the regulated industry as to the extent of permissible activities. Believing that this vagueness and overemphasis on competition has not well served the public because it has denied carriers serving the U.S. foreign commerce opportunities to cooperate, rationalize services, and achieve rate stability, the Senate excluded a general standard from its bill.

The House bill, on the other hand, included a provision authorizing the Commission to intercede against substantially anticompetitive agreements, even if these agreements would not violate any specific prohibitions of the bill. The House provision grew out of the Judiciary Committee's conviction that it is impossible to draft a sufficiently comprehensive list of specific prohibited acts to cover all potentially injurious anticompetitive behavior: such behavior would, under the House approach, be weighed against beneficial effects under a flexible general standard. Problems with uncertainty and delay would be addressed through a streamlined review process that set shorter time limits for Commission action than those prescribed in the Senate bill. And the House bill placed the burden on the Commission to establish that an agreement would result in (32) a harmful reduction in competition before it could enjoin the operation of an agreement.

Because of the strong views on the general standard, the conferees opted for a compromise provision differing in approach from either the House or Senate bills. Specifically, the Senate conferees agree to recede from the language of subsections 12(c)(8) and 13(d) of S. 47 and the House conferees agree to recede from the language of subsection 5(g) of the House amendment. The conferees intend that this report shall govern interpretation of the new section 6(g).

B. <u>Nature of the compromise general standard</u>

The new section 6(g) allows the Commission to seek an injunction if it determines that an agreement "is likely, by a

reduction in competition, to produce an unreasonable reduction in transportation services or an unreasonable increase in transportation cost." The compromise accedes to the House position insofar as it would establish a flexible general standard to be applied by the regulatory agency with expertise in this industry. This standard provides a basis for Commission review of agreements other than for contravention of specific statutory proscriptions and recognizes that a substantial reduction in competition can, under certain circumstances, trigger Commission intercession to prevent agreements from becoming effective or remaining in effect. On the other hand, the standard in the Conference Bill responds to the Senate concern that the "public interest" test in the present law is vague and unworkable in its automatic application of certain antitrust principles to ocean shipping. The new standard removes any per se condemnation of concerted conduct such as might be applied under the antitrust laws. Consequently, the standard establishes a threshold for prompt approval of most generally accepted joint conduct in ocean shipping. Other significant changes from the public interest standard of the present law includes section 6(h), placing the burden of proof on the Commission in any application of the general standard.

The compromise will place in the hands of the Federal Maritime Commission, the expert agency charged by the Congress with regulating this industry, sole responsibility for enforcing the general standard. Although the Department of Justice will continue to represent the FMC in most other respects, the Commission is

granted authority to represent itself in district court actions to seek an injunction. The expertise of the FMC in regulating this industry, the agency's experience in applying the standard, and the likely need for prompt action to stop threatening conduct, warrant a limited exception to the principle of centralized government litigation authority. In this case, the limited grant of litigation authority is to an independent agency, created by Congress with considerable autonomy from the Executive Branch. As new and evolving forms of cooperative conduct develop, the conferees believe that the Commission, rather than the antitrust agencies or the courts in the first instance, is in the best position to assess an agreement's benefits and detriments in light of the objectives of this Act.

The general standard leaves the carriers room to develop new and innovative cooperative ventures for dealing with rapidly (33) changing technologies and customer needs. At the same time, it grants to the Commission the necessary authority to act to stop schemes that go beyond what is necessary to obtain such benefits and cause substantial anticompetitive effects.

The flexibility in the compromise provision eliminates the need for a longer list of possibly overreaching prohibitions. The conferees agree that selective provisions limiting joint ventures or pooling agreements might discourage arrangements that often enhance the quality, frequency, or efficiency of transportation services. These agreements, just as any others, should be permitted unless the FMC demonstrates that they are likely to cause

concrete competitive harm evidenced in unreasonable and detrimental changes to transportation costs or services.

The language of this subsection must be interpreted in light of the historic international acceptance of carrier conference agreements. Conferences have been recognized in our laws at least since the Shipping Act of 1916. This legislation does place substantial limitations on that conference activity, including provisions that require open membership, a right of independent action on 10 days' notice for each member, and a substantial list of protective prohibitions, including a ban on boycotts, fighting ships, or other concerted practices designed to deny entry or drive existing competitors from the market. This legislation also prohibits the use of loyalty contracts not in conformity with the antitrust laws. But while limiting certain possible excesses of concerted activity, the compromise general standard clears the way for the conferences to perform concerted activities that serve the long-term interests of ocean carriers and shippers.

Economists and transportation experts differ as to whether conferences are the best means of attaining a modern and efficient transportation system and, if so, how conferences should be structured. After weighing these concerns, the conferees have approved a bill that, subject to the constraints already mentioned, permits the reasonable use of conferences and other concerted activity to address structural and competitive problems, such as severe rate instability and overcapacity that have long plagued this industry. Underlying this determination is also a realization

that the major economic allies of the United States continue to tolerate or even support conference and other cooperative carrier activity, in many cases in a measure far stronger than our laws have tolerated. Any major change in regulatory policy, although not precluded by these differences in approach, should be taken with a sensitivity to interests of friendly nations, and, insofar as possible, in tandem with them.

C. Analysis under the general standard

A critical factor enabling the Conferees to agree on a more narrowly drawn general standard is the inclusion in this bill of numerous other provisions which address the nation's interest in competition in the ocean common carrier industry. For example, prohibited acts in the Shipping Act of 1984 will continue the protections of the present law against predation and unreasonable refusals to deal. Even more importantly, the bill includes other specific and (34) major procompetitive reforms that will affect the operation of ocean carriers and conferences--notably a strong requirement of independent action with a limited notice period and the elimination of conference authority to offer loyalty contracts (unless their use would not violate the antitrust laws). With these reforms and other provisions in the bill, the Conferees have determined that carrier agreements generally will serve this nation's interest in international liner shipping. Thus, the Conferees determined to strike the overall balance between competition and cooperation in specific provisions of the act and

to allow for disapproval of agreements only under the carefully drawn circumstances set forth in subsection 6(g).

The new standard will permit conference agreements and amendments (including those providing intermodal ratemaking authority) to be reviewed promptly. Except in cases raising substantial issues under the standard, such agreements will enter into effect routinely, without the need for submitting additional information under section 6(d). Intermodal rate agreements have been used effectively throughout the world and are an important tool permitting the conferences to offer a through-rate, preferred by many shippers over segmented, port-to-port rates. Although some conferences serving U.S. trades have implemented intermodal rate agreements, the authority for such agreements is disputed. The Act recognizes that intermodal ratemaking authority is an important tool for the conferences to remain viable: no special stigma should attach to such agreements under the general standard.

The general standard also permits agreements providing for rationalization of services to be reviewed promptly and, except in cases raising substantial issues under the standard, to enter into effect routinely. Through these agreements, overcapacity (i.e., economic waste) can be reduced and efficiency enhanced, thereby better enabling carriers to respond with reasonable rates that afford them a reasonable return.

As suggested by the title of subsection (g), a likely reduction in competition should be substantial before triggering Commission intercession under the general standard. Unless the

competitive threat is substantial, any reduction in service or increase in cost would not be unreasonable, as required by the general standard. The Commission should not, in any event, expend its limited resources to pursue insubstantial reductions.

The market share of parties participating in concerted action is a touchstone for traditional antitrust analysis. This form of analysis, although helpful in determining whether an agreement is likely to cause a substantial reduction in competition, is only one factor in the Commission's decision calculus. Its significance will depend on the circumstances. In the case of conference agreements, including those with intermodal ratemaking authority, the conferees believe that potential reductions in competition will be at least partially offset by a member carrier's right of independent action and ability to enter and leave the conference freely. In some forms of concerted action, participation by all or virtually all of the members of a trade is necessary if the agreement is to have the desired effect on problems of overcapacity or rate instability. Thus, although a market share analysis is available to the Commission, in many (35) cases, depending on the circumstances, its outcome will not be determinative or necessary for application of the general standard.

In applying the general standard, the Commission also must consider whether the relevant competitive market includes more than just ocean common carriers providing direct service in a trade. The conferees intend that the Commission, in carrying its burden under the general standard, consider the impact on shippers of an

agreement not only in view of competition between ocean common carriers providing direct service in a trade, but also in view of other competitive means of transport. In some cases, alternative liner routings, bulk carriers, charter operators, or air freight carriers may provide competitive alternatives to the direct service provided by ocean common carriers. In considering these alternatives, the Commission may gather relevant information from shippers, other carriers, and third parties. And although the Commission may use its information powers to request market information from the proponents of an agreement, such information must be relevant and readily available to the proponents.

Even if an agreement is likely to cause the requisite reduction in competition, the Commission can obtain injunctive relief only if the likely net result will be an unreasonable increase in costs to shippers, or an unreasonable reduction in the frequency or quality of service available to shippers. There are two distinct aspects to this requirement.

The first is whether the harm to shippers is unreasonable. The term "unreasonable" is to be understood in a commercial context. Unreasonableness refers to the cost of transportation to the shipper or the availability or quality of service to the shipper. The likely change in costs or services must arise from the agreement and be material and meaningful. The Commission may not determine that rate increases or service reductions are "per se" impermissible results of agreements. Rate increases or decreases in the frequency or variety of service may be necessary

to achieve other benefits of the Act. The determination whether an agreement is likely to produce "an unreasonable increase in the price of transportation" does not authorize the FMC to engage in the type of ratemaking analysis undertaken by regulators of public utilities or as applied in the domestic offshore trades.

A second aspect of the unreasonableness requirement is that the negative impact upon shippers may be offset by the benefits of an agreement. For example, the competitive harm ensuing from conferences, already diminished by the statutory limitations on conference activity, can and often will be offset by the significant benefits of such activity. The privately-owned ocean common carriers that service U.S. foreign commerce are likely to be subjected to increasing competition from state-subsidized and controlled carriers. A conference's ability to address problems of overcapacity and rate instability is an important benefit that the Commission must weigh.

Another possible benefit to be considered by the Commission is the impact of an agreement on U.S. foreign policy and international comity. The Conferees agree that the United States should act with sensitivity to the interests of its trading partners when administering shipping regulation. One possible problem area arises (36) from cargo reservation schemes in the laws or trading practices of some foreign nations. There are important policy considerations that have led the United States to oppose some cargo reservation schemes. The Conferees understand that these considerations may lead our Government to continue this opposition

in many cases. At the same time, the Conferees recognize that some U.S.-flag carriers, through no fault of their own and despite such government opposition, may be confronted with a cargo reservation scheme that will exclude them from a trade entirely, or so limit their access to certain cargo as to make service of the trade commercially unattractive, unless they participate in a revenue or cargo sharing agreement with the carriers of such nations that preserves the right of the U.S.-flag parties to the agreement to compete for reserved cargo. Under such circumstances, the Conferees consider it a clear benefit to allow U.S.-flag carrier participation in the trade. Although the Commission might generally not approve such restrictive arrangements, the Commission, after giving due consideration to the maritime and trade policy views of the United States, may conclude that approval is necessary in order to maintain a viable U.S.-flag service, as it has in the past in similar circumstances.

Another important potential benefit to be considered is any efficiency-creating aspects of an agreement. Agreements involving significant carrier integration are, if properly limited to achieve such important benefits, to be favorably considered by the Commission and the courts. Joint ventures and other cooperative agreements can enable carriers to raise necessary capital, attain economies of scale, and rationalize their services. Pooling arrangements can also offer significant benefits in reducing excess capacity and promoting efficiency.

In assessing the benefits of any of these agreements, however, the Commission need not wear blinders. If, in applying its expertise, the Commission establishes that reasonable and commercially proven alternative arrangements will provide most or all of the essential benefits without the same anticompetitive impact, it may weigh this fact in its decision calculus. The conferees agree, however, that this standard does not represent a return to existing law, under which proponents may have been compelled to show that no less anticompetitive alternative was available to obtain the benefits of the Act.

The Conferees intend that ocean carriers be free to structure their own affairs, except when such structuring violates specific statutory provisions or the new, more narrowly drawn, general standard. Even when an agreement raises potential issues under the general standard, the Conferees believe that the procedural framework for application of that standard will give carriers maximum flexibility. Carriers will be able to obtain a prompt ruling from the Commission under the new provisions for expedited review. If the Commission objects to an agreement under the general standard, the filing party may withdraw it, modify it, or force the Commission to make its showing in court. Even after such a court proceeding is initiated, the filing party retains the option of withdrawing or settling the matter with the Commission.

(37) In sum, the general rules of operation and approval of agreements have been developed by the Congress with full awareness of the realities of international ocean carriage; a general

standard has been retained to provide the necessary flexibility to deal with the unusual or severe cases not addressed by other prohibitions in the Act.