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Executive Summary

ASDIRS

SEALIFT PROCUREMENT AND NATIONAL SECURITY

(SPANS) STUDY

[redacted]

EXECUTIVE SUMMARY

AUGUST 2, 1972

[redacted]

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3949
Executive
Summary
ASDIRS

OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE
WASHINGTON, D. C. 20301

SYSTEMS ANALYSIS

MEMORANDUM FOR DISTRIBUTION LIST

SUBJECT: Sealift Procurement and National Security (SPANS) Study

On May 8, 1971, the Deputy Secretary of Defense directed that an extensive examination of Department of Defense sealift procurement, requirements, and capabilities be undertaken. He requested that the Maritime Administration in the Department of Commerce, the Federal Maritime Commission, and the Office of Management and Budget participate in this study. This interagency effort was guided by a Senior Advisory Group (listed on the following page) representing participating offices and was aided by an Industry Advisory Committee of senior officials from ten U.S. shipping companies. The entire study was approved by this Senior Advisory Group and forwarded on August 2, 1972 to the Deputy Secretary of Defense for his decisions regarding implementation of the study recommendations.

John D. Christie
Principal Deputy Assistant
Secretary of Defense
Chairman, SPANS Study

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SEALIFT PROCUREMENT AND NATIONAL SECURITY

(SPANS) STUDY

EXECUTIVE SUMMARY

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(U) Introduction

The Sealift Procurement and National Security (SPANS) Study addresses three basic issues:

(1) the financial impact on the general cargo shipping companies of the U.S. Merchant Marine of the competitive negotiated procurement system currently used by the Department of Defense (DoD) to procure peacetime shipping services for less-than-full shipload lots of cargo and the desirability to DoD to modify the current system or to adopt a new procurement system;

(2) the adequacy of shipping assets currently or potentially available to DoD to fulfill all sealift needs for the major (mobilization) and minor (non-mobilization) contingencies for which DoD has been directed to be prepared and the identification of the most effective programs which could offset any shortfall;

(3) the economic desirability, based upon improving the efficiency of peacetime cargo movement operations, of replacing currently government-owned or chartered vessels through the acquisition of new vessels for the Military Sealift Command (MSC) controlled fleet.

The SPANS Study has four parts: Parts I and IV address the first issue and Parts II and III address the second and the third. Both Parts I and II provided basic research and analysis for Parts III and IV which include recommended courses of action for DoD.

(U) I. Part I (Understanding the Current Systems)

Part I-A describes the past and present systems used by the DoD to procure commercial shipping service, both berth-line and chartering. Particular emphasis is placed upon describing the present berth-line system of competitive, negotiated procurement and outlining specific policy and procedural issues related to DoD sealift procurement.

Part I-B is a cost-based analysis of carrier-supplied data for CY 1969 and CY 1970 to determine whether DoD general cargo was being carried at compensatory rates. This financial analysis revealed that considering the entire scope of DoD procurement of commercial sealift, DoD cargo was compensatory (gross profit was approximately 15% of revenue). However, a significant amount of Department of Defense cargo was carried, particularly during CY 1970, at rates which were non-compensatory. This occurred almost exclusively where there was a substantial infusion of new technology, which resulted in overcapacity. The following can probably be reasonably inferred from the analysis of Part I-B:

(a) When overcapacity exists and when a competitive DoD procurement system exists which includes the possibility of one operator carrying a predominant share of the cargo, the conditions are ripe for incremental bidding and serious industry financial problems.

(b) Rates for DoD cargoes which were compensatory and also included a fair rate of return would probably aid in the preservation of the U.S.-flag Merchant Marine.

(U) II. Part II (The Future Size, Composition, and Productivity of the U.S. Merchant Marine and Forecasts of U.S. Waterborne Trade)

The purpose of this Part was to develop a basis for evaluating the wartime general cargo shipping capability which U.S.-flag commercial assets can provide to DoD. This was accomplished by projecting the size, composition, and productivity of the general cargo fleet to FY 76. Two basic approaches were used for these projections. The first involved the application of ship-life rules* to the present general cargo fleet to determine the number likely to remain in the operation in 1976. This provided two fleets: One of these, designated the Pessimistic Fleet (309 ships), included only ships remaining under ship-life rules plus ships under construction or under firm construction contract in early 1972. The second, called the Programmed Fleet (326 ships), included in addition 17 general cargo vessels tentatively planned for construction under the President's Maritime Program.

The second approach involved explicit estimation of probable future cargo generation rates** and of the numbers and types of U.S.-flag vessels that could be supported in efficient operation under two assumptions regarding the rate at which U.S.-flag carriers may penetrate the world shipping market. Of the two fleets projected under this approach, the first, designated the Excursion Fleet (292 ships), reflects the assumed continuation of current rates of market penetration. The second, called the Economic Fleet (331 ships), assumed a limited increase in the U.S.-flag penetration rate as a result of accelerated government/industry cargo promotion programs.

The four fleet projections resulting from these two approaches provide a range of possible merchant fleets for examination. Of these the Economic Fleet would be the most capable, followed by the Excursion Fleet, the Programmed Fleet, and the Pessimistic Fleet, in that order.

The Economic Fleet represents, for SPANS Study purposes, an approximation to the upper limit of U.S.-flag general cargo capability that may reasonably be expected to be generated as of 1976 by market forces and the government support provided by the President's Maritime Program. Participants in the SPANS Study concur in the desirability of moving as far as possible within the limits of the President's Maritime Program to strengthen the U.S. commercial sealift fleet. In the interest of conservatism, however, the Pessimistic Fleet has been used as the base fleet in most of the analyses undertaken in Part III of the SPANS Study.

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*Under ship-life rules, it is assumed that ships are retired 25 years after construction or 15 years after major modification.

**Part II-A provides a projection of DoD general cargo tonnage for FY 72-FY 76 by amount, commodity, and area of the world. The first several sections of Part II-B project the other government cargo and commercial cargo for the same periods.

(S) III. PART III (Defense Implications)

(U) Part III evaluates the capability of the United States to fulfill its wartime deployment requirements and associated shipping requirements with the sealift resources expected to be available in FY 76. It also examines alternative increments of capability that may be provided by different DoD and/or Maritime Administration (MARAD) programs. The summary presented below is followed by conclusions and recommendations.

(S) A. Summary

(U) Both major and minor contingencies have been considered, with primary focus on major potential contingencies which would involve the requisitioning of commercial sealift resources. The deployment of military unit equipment and the movement of resupply in selected major contingencies have been analyzed with the assistance of a computerized transportation model which represents marshalling and cycling (including onload, offload, etc.) of airlift and sealift resources, with emphasis on the latter. The effects of submarine action in NATO contingencies are explicitly represented in terms of ship and materiel losses. Ship loss levels are based on the results of a Navy antisubmarine warfare study designated NARAC-G.

(U) Basic shipping issues considered in the analysis include the use of containerships for moving unit equipment (i.e., the initial equipment for the combat and support forces) as well as resupply, the likelihood of port denial, and potential requirements for emergency port facilities. Other significant issues include possible requirements for Multi-Purpose Ships (MPS) and/or Multi-Mission Ships (MMS) and the potential need for, and availability of, NATO-flag shipping assistance.

(S) Contingencies involving ship requisitioning which have been analyzed include actions in Northeast Asia (NEA), Southeast Asia (SEA), and NATO Europe. Under DoD planning guidance (Defense Policy and Planning Guidance (DPPG), 9 March 1972), 1976 contingencies envisioned in NEA and SEA would not tax U.S. sealift resources expected to be available. Emphasis has therefore been placed on Europe, where force requirements would be significantly larger and where submarine action may have a considerable effect.

(S) Two different NATO contingencies are considered. One of these, designated NATO First, is assumed to occur during an otherwise peaceful period; military mobilization is initiated on the NATO M-Day in this case. In the second case, the NATO contingency is assumed to occur 12 months after the start of a SEA contingency involving full U.S. military mobilization (NATO after SEA). In the first case the maximum U.S. force that could be in Europe by D+90 would include only 15 Army divisions (includes 4 1/3 in place on M-Day and 2 2/3 with prepositioned equipment) with support, plus two Marine Amphibious Forces and appropriate USAF and Naval forces. This limit reflects the force levels projected in the Five Year Defense Plan (FYDP) (13 active Army divisions) and the time requirement for mobilization of Army reserve divisions (14 weeks). In the case of NATO after SEA, the early mobilization of reserve forces would make it possible to have 16 1/3 Army divisions in Europe by about D+90. This matches the deployment objective assumed in the Joint Strategic Objectives Plan (JSOP) FY 74-81.

(S) For both NATO First and NATO after SEA, SPANS has examined, alternatively, the effects of assumed warning periods of 23 days and 10 days (i.e., the time between U.S. mobilization and the start of the conflict). The assumption of 23 days' warning is prescribed for planning purposes in the DPPG, which is binding on SPANS. The assumption of 10 days' warning was employed in JSOP 74-81.

(U) With respect to minor contingencies not involving ship requisitioning, SPANS employed a JCS study (JCS 1454/144-5, 15 October 1971) which postulated notional contingencies (in areas 4000 nautical miles or 11,000 nautical miles from the Continental United States) involving several different U.S. force levels. SPANS conclusions and recommendations with respect to minor contingencies reflect transportation requirements for two and four Army brigades plus appropriate support.

(U) The implications of a variety of assumptions are examined in Part III. In all areas where there are critical differences regarding specific areas of uncertainty, assumptions commonly employed by the Services and the Organization of the Joint Chiefs of Staff have been fully reflected in the analyses and conclusions along with the implications of divergent assumptions, and the origins of specific assumptions are clearly identified.*

(U) The Part III conclusions and recommendations presented below reflect the assumed employment of the Pessimistic Fleet plus the National Defense Reserve Fleet (NDRF), with 130 ships. The conclusions and recommendations are not generally sensitive to the substitution of the alternative projected fleets (e.g., Economic) for the Pessimistic Fleet. (In the few cases where conclusions would be affected by such substitution this is explicitly noted.) Similarly, the subtraction of the NDRF has no effect on the listed conclusions, although it does increase calculated shortfalls under assumed conditions of attrition. The 130 ships of the NDRF are presently scheduled by MARAD for retention at least through the end of FY 77. There is evidence that the condition of these ships is somewhat better than the condition of NDRF ships at the start of the Vietnam buildup.

(U) Finally, it is assumed in SPANS that there is a requirement for an MSC controlled fleet. Some conclusions and recommendations are concerned directly or indirectly with its future size and/or composition, but the basic requirement for a controlled fleet of some form has not been questioned.

(U) *The Army, Navy, and OJCS representatives on the SPANS Senior Advisory Group are concerned that the SPANS Study could be interpreted improperly for future policy decisions, which could reflect an overly optimistic estimate of available sealift capability. These decisions could be based on such assumptions as automatic availability of NATO shipping, utilization in 1976 and beyond of 130 NDRF ships which in 1972 average 27 years of age, the untested concept of containerization of unit equipment, and reliance on emergency container off-loading equipment which may not be available.

(S) B. Conclusions

(S) 1. Worldwide U.S. requirements for sealift capability as of 1976 would be somewhat larger in the event of a NATO contingency starting 12 months after the beginning of a SEA war which was the occasion for full military mobilization (NATO after SEA) than in the case of a NATO contingency occurring during an otherwise peaceful period (NATO First).

(S) 2. Under the assumption that mobilization day (M-Day) would precede the start of hostilities (D-Day) by 23 days (D=M+23, an assumption which is stipulated in the Defense Policy and Planning Guidance), projected U.S. sealift capability would be more than adequate with zero attrition to meet the worldwide U.S. material movement requirements considered in SPANS in either the NATO First or the NATO after SEA contingency.

(S) 3. Under the assumption employed in JSOP 74-81 that D=M+10, and with zero attrition, there would be 5 to 7 day delivery slippages beyond the deployment objectives considered in SPANS as of D+30 in the NATO First case and as of D+30, 60, and 90 in the NATO after SEA case, with the Pessimistic Fleet plus NDRF. The slippages as of D+60 and D+90 would not be encountered with the alternative fleets (plus NDRF) projected in SPANS, but the slippages as of D+30 are inherent in SPANS assumptions regarding time requirements for preparation for overseas movement (POM), for travel to ports, and for marry-up and inland movement overseas. They could not be eliminated under these assumptions by alternative fleets or by sealift augmentation programs considered in SPANS.

(S) 4. Under the SPANS assumptions of "high" sealift attrition (185 dry cargo ships sunk in 90 days) or "alternative" attrition (120 sunk), materiel losses would be very large in a NATO First or in a NATO after SEA contingency, and delivery shortfalls would be significant, (particularly if D=M+10). This would be true with any of the U.S.-flag fleets projected in SPANS (and with or without the NDRF), but the shortfalls would be smallest with the Economic Fleet.

(U) 5. Assuming that containerships were restricted to the delivery of resupply, sealift attrition would have a much more pronounced effect on unit equipment deliveries than on resupply deliveries.

(U) 6. Under attrition conditions, a measurable improvement in unit equipment deliveries could be achieved by using containerships to deliver some unit equipment. An improvement of similar magnitude would be provided by a 10-ship MPS (or 11 MMS) program but at considerably greater peacetime cost.*

(U) *The representative of the U.S. Air Force on the Senior Advisory Group notes that the only remedies considered for enhancement of wartime deployment capabilities under conditions of sealift attrition were sealift options. He believes that requirements can only be evaluated in consideration of other options, to include increased airlift and increased prepositioning of unit equipment and supplies.

(S) 7. With any of the four U.S.-flag fleets projected for 1976 in SPANS the deployment shortfalls that could occur with sealift attrition are so great (20 to 40 percent) that a large number of additional ships would be required to provide significant improvements in deliveries. Among potential sources of augmentation shipping, only the NATO-flag fleet would be adequate to produce a significant reduction in these delivery shortfalls: 198 NATO-flag ships (out of a NATO total of about 2700 deep draft general cargo vessels) could greatly reduce estimated shortfalls as of D+90. (In the case where D=M+23, objectives in gross tonnage could be met with the use of such NATO shipping.) Timely NATO-flag shipping assistance is not assured under current NATO policy. However, it is reasonable to expect that this assistance would be provided: high assurance of its availability could be provided through bilateral agreements with individual NATO countries.*

(S) 8. It is more probable that port capacity adequate for U.S. military needs would be available in Europe than that it would not. However, this availability is not fully assured. (The availability of French ports, as specified in the DPPG would probably assure the availability of adequate capacity.)

(U) 9. Emergency provision for the offloading of containerships would be essential in the early stages of a NATO war with sealift attrition in the event that port use were denied because there is no alternative to the use of containerships to meet resupply requirements in this case.

(U) 10. One and possibly two MMS ships (barge carriers) could be operated efficiently in the MSC controlled fleet in peacetime in the 1976 time frame without preempting DoD cargo normally moved by berth lines. Four MMS ships could be operated efficiently, but this would involve preemption of berth cargo.

(U) 11. There is no need to acquire additional controlled fleet vessels in advance of a contingency in order to assure their availability to fulfill non-mobilization contingency requirements. However, appropriate steps should be taken to assure the contingency availability of modern ships configured to meet specialized military shipping needs, with particular attention to heavy lift needs and to requirements for movement of non-self-deployable aircraft.

(S) 12. A 10-ship MPS (or 11 MMS) increment would provide measureable benefits in NATO deployments under attrition conditions in terms of total deliveries and in terms of offloading capability if ports were denied. However, the delivery benefit would be small relative to potential shortfalls (which could be ameliorated significantly only by NATO-flag shipping) and the offloading benefit would be small relative to emergency offloading capabilities which would be mandatory in any event if port use were denied.

(U) *The representative of the U.S. Air Force on the Senior Advisory Group notes that the only remedies considered for enhancement of wartime deployment capabilities under conditions of sealift attrition were sealift options. He believes that requirements can only be evaluated in consideration of other options, to include increased airlift and increased prepositioning of unit equipment and supplies.

(U) 13. There is no apparent requirement for MPS or MMS ships in the MSC controlled fleet to meet U.S. sealift requirements either in the NATO contingencies examined in SPANS or in small contingencies which do not involve mobilization. (This conclusion does not address the desirability of MMS ships which might be operated efficiently in peacetime in the MSC controlled fleet.)*

(U) 14. Shipping that is required in the MSC controlled fleet should be modernized. However, new ship construction is not required for the replacement of overage vessels in the general cargo portion of an MSC controlled fleet sized to meet peacetime DoD needs for controlled shipping after the Vietnam drawdown (presumably FY 74 and thereafter). The number of general cargo ships of post 1960 construction which are potentially available for charter would be adequate to meet this replacement requirement.

(S) C. Recommendations

(S) 1. Negotiations should be initiated immediately to develop bilateral agreements with European NATO countries providing for early shipping assistance to the United States in the event of a NATO contingency. (The NATO Planning Board for Ocean Shipping (PBOS) has recognized the desirability of such shipping assistance and in May 1972 announced its intention to conduct a study during the ensuing year of the possibility of providing it through NATO agencies. PBOS has also agreed that the negotiation of bilateral agreements would be useful. Action on this matter has been directed by OSD.)

(U) 2. Study and test of emergency offloading facilities for nonself-sustaining containerships should be pursued vigorously by DoD agencies in a coordinated effort.

(U) 3. Equipment and procedures for the movement of unit equipment on containerships should be fully developed and tested as soon as possible.

(U) 4. A two-stage commercial sealift augmentation program involving a total of 43 ships in the first stage and 74 in the second should be developed, and guidance, negotiations and/or incentives should be employed by DoD to achieve commitments to the Sealift Readiness Program of ships suitable to meet specialized military needs under availability schedules consonant with contingency necessity. In addition, programs that would lessen the financial risk to Sealift Readiness Program participants should be investigated.

(U) 5. Acquisition of one or two barge carrying ships for the peacetime controlled fleet would be appropriate and should be undertaken. Acquisition of more than two of these ships in a larger MPS/MMS program should not be undertaken at this time, but the requirement for such a program should be reexamined if the actions recommended above should prove unproductive.

(S) *The JCS, Army, and Navy members of the Senior Advisory Group believe that, based on JSOP 74-81, a 10-ship MPS/MMS program is required to support a NATO contingency. These agencies also believe that the capability represented in the MPS would also be desirable in small contingencies in other areas.

(U) 6. Existing ships built since 1960 should not be placed in the National Defense Reserve Fleet (NDRF) while the Military Sealift Command (MSC) is operating overage vessels in the controlled fleet. Once the overage ships have been retired, however, relatively new used ships should be acquired for the NDRF if they would otherwise be scrapped or sold to foreign operators.

(U) 7. The U.S. commercial sealift fleet should be strengthened to the extent possible within the limits of the President's Maritime Program.

(U) 8. Appropriate steps should be taken, to include initiation of special legislation if necessary, to assure the timely availability of U.S. owned total container and barge systems for military use in major contingencies that involve the requisitioning of containerships and barge carriers. In addition to ships, barges and containers, total systems are construed as encompassing systems needed for handling and inland movement and for the control of container and barge movements.

(U) IV. Part IV (Alternative Procurement Systems)

Part IV examines alternative procurement systems which might fulfill the following goals:

(1) Preservation of a viable U.S.-flag fleet for use during peacetime and during either limited or full-scale contingencies as a necessary deployment and resupply adjunct to DoD forces.

(2) Procurement of peacetime military sealift at lowest cost consistent with the other goals of SPANS.

(3) Provision of an opportunity for the industry to earn a reasonable rate of return for services rendered.

(4) Provision of equal opportunities to all carriers who choose to participate in the DoD sealift program.

The summary presented below is followed by recommendations.

A. Summary

All of the alternatives presented represent either further restriction of price competition or development of totally new systems for establishing rates within the maritime industry. Described briefly below are the various alternatives which were studied.

1. Competitive Procurement

a. RFP 700. RFP 700 incorporates the most substantial changes to date including provisions known as the "MAX-MIN system." These modifications involve a "quasi-allocation" system which intentionally limits competition. The specific intent of the modifications was twofold. First, they were intended to ensure that the carriers bid rates would be based on the anticipation of providing substantial service. The MIN (minimum carriage)

provisions are designed to curtail submission of "paper rates" and the practice of "skimming." Second, the MAX (maximum carriage) provisions are intended to spread the DoD cargo and thus limit the carrier's incentive to bid on an all-or-nothing basis as had occurred under the previous pecking order system.

b. Minor Modifications. Modifications to competitive procurement which have minimal constraining effect upon competitively bid prices and which generally involve the administrative aspects of government procedures, terms of service, or penalties include:

(1) Elimination of the best and final offers where possible under ASPR;

(2) Modification of the RFP time cycle -- possibilities range from decreasing the cycle to 30 days to increasing it to one year;

(3) Expansion of the rate review effort by the Military Sealift Command (MSC) and the Federal Maritime Commission (FMC) by --

(a) simply allowing more time in the cycle for this purpose;

(b) provision of auditable, certified, cost data to the FMC to facilitate review of carrier's rates on an as required (per rate) basis;

(c) utilizing Military Standard Transportation and Movement Procedures (MILSTAMP) data for compliance with the 1904 Act;

(4) Stiffer penalties for violation of the terms of the solicitation.

c. Major Modifications. Modifications which involve augmented cost reporting and review processes or major constraints on competition include:

(1) Establishment of dollar limits on rates to restrict the range of possible rate proposals.

(a) Utilization of an unpublished floor or band by MSC/FMC as a basis for rejecting rates which appear to be prejudicial or detrimental to the DoD mobilization base or to commerce (the floor would be based on a known governmental policy);

(b) Establishment of a more restrictive floor than in (a) above. This floor would go beyond protecting against destructively low rates and would be aimed at insuring that carriers receive enough revenue to cover all operating cash flow costs; e.g., the carriers would not be allowed to bid rates which would absolutely preclude replacement of assets;

(2) Allocation Systems -- Two forms of allocation systems are explored, each of which utilizes a bid rate as one of several inputs in the distribution of cargo among carriers;

(3) Rates to be set in response to short run factors of supply and demand. Under this approach, an individual carrier might adjust his rates at any time he chose. This would be similar to the procedure employed by the Interstate Commerce Commission in regulating inland rates for the trucking industry;

(4) Utilization of commercial conference rates for comparable cargoes less a discount for DoD.

2. Cost-Based Rates

a. Limited System -- A cost-based system which involved some cost reporting, but not for all operations and not necessarily for all carriers involved in the carriage of DoD cargo.

(1) Limitation of cost reporting to only major MSC route indices.

(2) Utilization of an abbreviated "invoice system" which utilizes a standard cost per measurement-ton-mile for at sea costs, direct port costs, a surcharge for overhead and indirect costs, and flow through of the direct cargo handling costs.

b. Simplified Cost-Based System -- Extensive cost reporting for virtually all operators wo carry DoD cargo on the major DoD trade routes. Competitive influences are considered in establishing rates; the accounting and reporting system requirements could be simplified vis-a-vis a cost reimbursement system, with the utilization of more averages, approximations, and other methods of simplification.

B. Recommendations

There has been consensus on the need for some change based on the undesirable impact of some aspects of competitive negotiated procurement on the long-term interests of both the U.S. maritime industry and the Department of Defense. In consonance with the goals of the SPANS Study, significant changes have already been made to the competitive system as incorporated in RFP 700. The outcome, however, is by no means assured as the system is still primarily price competitive.

Recognizing that the changes to RFP 700 as well as future possible changes to competitive procurement may in the long run prove insufficient to achieve the goals established in SPANS, but also recognizing that not all participants in SPANS agree that immediate adoption of a cost-based rate making system is warranted, the recommendations below represent a compromise and a phased response based upon proven need.

It is therefore recommended that:

1. DoD continue the changes developed for RFP 700, which are intended to preserve usable assets for DoD peacetime and contingency requirements.

2. The FMC, with the assistance of MSC, augment their review of competitive rates. In the discharge of their regulatory responsibilities, the FMC will take action against rates which are detrimental to commerce in accordance with the provisions of the Shipping Act of 1916, as amended. It is recommended that the FMC establish the definition of "detrimental to commerce," in specific accounting terms based upon the recommendations developed in the SPANS Study. The recommended SPANS definition is that of operating cash-flow costs (included on Page 4 of Part IV of the SPANS Study) which will allow bids below fully allocated costs. The FMC, with the assistance of the other agencies participating in SPANS, will establish a "spot" cost reporting system similar to that described in Section III.B.2. and Section IV.B.2. of this study. This reporting system would be based upon the terminology contained in FMC General Order 11 as revised and as modified by the relevant portions of the ASPR cost principles so that those costs or services applicable to defense cargoes can be identified. All rates will be subject to an initial review by FMC. After the rates are accepted by MSC and prior to the effective date of the rates, if FMC determines that a particular rate should be subject to challenge as potentially detrimental to commerce in accordance with the above definition, FMC will require submission by the carrier of necessary cost information. After the rates are accepted by MSC and prior to the effective date of the rates, the FMC will initiate appropriate action under the Shipping Act of 1916, which may result in the FMC ordering a carrier to strike any rate which the FMC considers detrimental to commerce. When the FMC strikes a rate, its review will include designation of what would have been the lowest acceptable rate for the particular carrier, route index, commodity and time period under review. If an order to strike from the tariff is issued, from the date that such an order becomes final, the affected carrier(s) will be considered not to have received an award for the cited commodity and route index. If the rate guide has been published, the affected rate will be deleted. The carrier(s) will not be utilized during the remainder of the cycle except as necessary when capability from carriers receiving awards is not available to meet the requirement.* (See Footnote on Page 13.)

3. The need for further changes to the DoD sealift procurement system will depend upon the effectiveness of modifications already made (RFP 700) and any modifications subsequently deemed necessary. If existing or previous changes have been inadequate, then the case will exist for further change to competitive procurement or adoption of a cost-based system. Should further changes be necessary, the full range of options presented herein, including further modification of competitive procurement as well as consideration of a cost-based rate making system, will be considered in determining the next most appropriate change. Adoption of a cost-based rate making system at any time will be based upon: (a) demonstrated need based upon the insufficiency of past modifications of the DoD procurement system and (b) successful completion of a feasibility study which would include resolution of all policy issues contained in Part IV of SPANS, specific consideration of DoD peculiar costs and services, and an objective evaluation of the administrative feasibility of such a system. A cost-based rate making system will be initiated after all agencies involved are satisfied that the preconditions above have been reasonably met and after all agencies agree that alternative forms of competitive procurement either have failed or will fail to meet the SPANS goals.

4. Based upon the premise that the following steps are inherently beneficial to the industry, and in order to facilitate the possible future adoption of a cost-based rate making system, it is also recommended that MARAD and FMC develop a standardized EDP-based industry cost accounting system which could be tailored to the needs of individual companies, yet which would represent as much commonality as is possible within the industry. Since completion of this effort is necessary prior to adoption of any cost-based system, should a cost-based system be required in the future, the most time-consuming initial steps will have been completed.

It is hoped that the development of this accounting system will facilitate the FMC's rate review role as described in Recommendation 2.

5. The Industry Advisory Committee on Maritime Policy** should be periodically informed of progress concerning these recommendations and this group should make recommendations to its chairman, the ASD(I&L), concerning the adoption of successive procurement changes as described above. The group is only an advisory group to the Department of Defense; it is not intended as a review group, a quasi-judicial group, or a parent organization for on-going sealift studies.*** (See Footnotes on Page 13.)

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*The following language is recommended for inclusion in MSC's future RFPs: "Respondents to this RFP are advised that the Federal Maritime Commission will review their submissions and may on its authority disapprove rates which in its judgment are detrimental to commerce of the United States and in violation of the Shipping Act of 1916, as amended. In making this determination, the Federal Maritime Commission may require that respondents submit cost information in accordance with its Bulletin No. _____. Respondents are on notice that it is in their interest to maintain their records in such a manner that will facilitate a timely and accurate response to an order of the Federal Maritime Commission for the production of the aforementioned cost information. Respondents are further on notice that for the purposes of this RFP, the Federal Maritime Commission has defined its standard of rates which are detrimental to the commerce of the United States in its Bulletin No. _____."

**This group has been formally chartered under DoD regulations and consists of the following members: The ASD(I&L), the PDASD(SA), ASN(I&L) and ASA(I&L), Assistant Secretary of Commerce(MA), Chairman FMC and Industry Representatives.

***The following pertains to the entire set of recommendations: The recommendations presented in Part IV of the SPANS Study are the result of considerable negotiation among all parties involved. In these negotiations, express consideration was made of the views of the SPANS Industry Advisory Committee. The recommendations represent considerable compromise on the part of everyone and are necessarily general in nature.

The details of the augmented review procedures (Recommendation 2) will be developed primarily by the FMC, with the assistance of the other agencies. It is recognized by all parties that review under the Shipping Act of 1916 is solely the responsibility of the FMC and that adjudication of issues arising thereunder could eventually be necessary. However, since all parties to the SPANS Study are also interested parties to the FMC review, it was in the spirit of cooperation that the SPANS Interagency Working Group developed suggested accounting definitions and procedures to aid the FMC in its difficult regulatory task.

It is also recognized by all parties that the DoD, and specifically the MSC, have no regulatory powers and thus cannot be direct participants in the FMC review (except as an intervenor in any regulatory proceedings which may result therefrom). The use of the word "assistance" by the MSC refers to the MSC's making information available to FMC (within the limits of the ASPR and DoD procurement policy) to facilitate the FMC review.

It is the understanding of all parties that the order by FMC to strike or disapprove a rate found to be detrimental to commerce is presumed to be final until such time as it is either temporarily stayed or set aside by competent authority.

The definition of cash flow operating costs is presented in the SPANS Study only as a concept. It is useful as it relates to the FMC's concept of "detrimental to commerce" and to the DoD's concept of preserving a mobility base (ASPR exception 16). The concept will be translated into specific maritime industry accounting terms which recognize the uniqueness of DoD cargoes, i.e., the non-applicability of certain industry cost categories and services. While some members of the DoD staff view this review as an unprecedented establishment of a price floor on a viable competitive system, it should more properly be viewed by DoD as a lawful intervention under FMC's regulatory authority and one which is designed to ensure adequate consideration of the DoD position.

It is agreed by all parties that the FMC will be responsible for the development of the detailed accounting definition of "detrimental to commerce." Aiding the FMC will be OMB, MARAD, DoD (probably OASD(I&L), Defense Contract Audit Agency, and MSC) and the industry.

It is also agreed by all parties that MSC must proceed with is responsibilities to ship DoD cargo under Shipping and Container Agreements. All parties have agreed that possible FMC action will not interfere with the timely execution of these responsibilities and that specifically, the review process will not delay the MSC procurement process. It is also agreed that the FMC bears the responsibility for rejecting any rate in violation of the Shipping Act of 1916, as amended, and that if any rate under FMC challenge has not been lawfully rejected at the time of the effective date of the MSC rate agreements that the MSC has no option but to promulgate and utilize the rate. The FMC's lawful orders regarding rates which are binding on DoD will be followed by MSC.

When a carrier's rate is disapproved by FMC and MSC later finds that it is necessary to utilize the carrier's capacity on the affected route index, there are several alternatives which MSC might pursue in arriving at a rate and conditions for using the carrier. For example, they might use the commercial tariff or negotiate a contract for a specific shipment. The carrier's utilization will be determined by MSC at the time the carrier is required, based on conditions which will serve the best interest of the government.

It is also recognized that in any procedure, certain unforeseen problems could develop. For example, if the FMC strikes a significant number of rates (or conceivably all rates) for a particular route index and commodity, some accommodation will have to be made to ensure the timely movement of DoD cargo. All parties agree that some special administrative procedures will be developed as necessary by the parties involved based on the good judgment and goodwill of these parties.

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