BEFORE THE
UNITED STATES COAST GUARD

In the Matter of	)	
Great Lakes Pilotage Rates:	)	USCG Docket ID: 2015-0497
2016 Annual Review and Changes to Methodology	)	

COMMENTS ON GREAT LAKES PILOTAGE RATES - 2016 ANNUAL REVIEW AND CHANGES TO METHODOLOGY NOTICE OF PROPOSED RULEMAKING

The American Great Lakes Ports Association, Canadian Shipowners Association, Canfornav Inc., Fednav International Ltd., Polish Steamship Company, Shipping Federation of Canada, Spliethoff Transport B.V., United States Great Lakes Shipping Association, and Wagenborg Shipping (collectively, the "Commenters") appreciate the opportunity to comment on the United States Coast Guard's ("USCG") Notice of Proposed Rulemaking (NPRM) on the Great Lakes Pilotage Rates - 2016 Annual Review and Changes to Methodology. *See* 80 Fed. Reg. 54,484 (Sept. 10, 2015).

The governing statute for this exercise requires USCG to give "consideration to the public interest and the costs of providing the [pilotage] services." 46 U.S.C. § 9303(f). The NPRM is patently inadequate with regard to this statutory requirement. Pilotage rates for the Great Lakes have for some time been a matter of great concern to shipping interests. U.S. pilotage costs in the Great Lakes, although subject to USCG regulation, have risen 114 percent over the last 10 years. Much of this increase has occurred in the last two navigation seasons. Pilotage is now one of the largest single cost items for foreign-flag vessels that enter the St. Lawrence Seaway/Great Lakes system. Competent pilotage in adequate supply is a goal that is shared by pilots, shipowners, ports, and other shoreside economic interests in the United States and Canada. However, an empirical case can be made that capability, capacity and costs are not in reasonable balance under existing USCG rate-setting methodology. The 51 percent revenue increase (as estimated by USCG) that will result from this NPRM, if carried forward to a final rate, will erode the competitive position of the Great Lakes Seaway navigation system and betray USCG's goal of providing safe, reliable, and efficient pilotage service. The Commenters therefore respectfully suggest that USCG withdraw this NPRM, even if to do so requires a minimum one-year extension of the existing methodology. Such an extension will enable the USCG to better identify approaches that will meet, as law requires, not only the financial aspirations of pilots, but the overall economic interests of all participants in this vital sector of the United States and Canada's maritime economy.

As noted above, the USCG exercises delegated authority to ". . . prescribe by regulation rates and charges for pilotage services, *giving consideration to the public interest and the costs of providing the services*." 46 U.S.C. §9303(f) (emphasis added). Congress also granted broad authority to prescribe regulations governing the "operation and administration" of approved pilotage pools, to "prescribe a uniform system of accounts," to "perform audits and inspections" and to "require coordination on a reciprocal basis" with Canadian pilotage organizations. 46 U.S.C. § 9304. A major defect in the NPRM and in the overall administration of these statutory authorities by the USCG is that these authorities have not been adequately deployed to ensure rate payers that the rate-setting process is using reliable data either for past periods or as the basis of projected pilot revenue requirements. In most government rate-setting environments, rate payers can expect that the regulated utilities are subject to a uniform system of accounting, that the regulated entities' financial submissions are routinely audited and verified by the rate-setting body, that the rate-setting agency maintains accurate, current operational data to enable past periods to be checked against projections for those periods, and a "truing up" or refund mechanism to compensate rate payers when disparities between projections and actual data for a given period yield excess revenue collections. These features do not exist in the current system administered by USCG, despite considerable statutory power available to USCG to impose these mechanisms.

The result is an unacceptably incomplete ratemaking environment in which, unlike other state or federal agencies that set rates for important services, USCG sets rates based on unreliable inputs that yield the kinds of enormous rate increases that are proposed in this NPRM. These increases are all the more damaging given the lack of a year-to-year revision mechanism to compensate rate payers for overcharges once actual data are available to test against projections. Because Commenters are here urging that the NPRM be withdrawn to enable USCG to address numerous defects in its cost and revenue projections, we also urge that USCG review rate-setting processes of other agencies and departments in order to adopt some kind of best practices guidelines to govern future rate decisions.

We recognize that USCG has been tasked with a difficult assignment in setting pilotage rates for the Great Lakes, and, by extension, affecting the economics of international shipping for all operators and related shoreside entities who serve the St. Lawrence Seaway and U.S. and Canadian Great Lakes region. We respectfully submit however, that the overriding flaws of the NPRM include a failure to require and compile sufficient and reliable economic data to enable USCG to identify accurately the cost, economic, financial, and service impacts of the Proposed Methodology on ratepayers, and a general failure to assess the sustainability of the proposed methodology over a multi-year period. The NPRM, as drafted, is arbitrary, capricious, unsupported by substantial evidence, and otherwise not in accordance with law. *See* 5 U.S.C. § 701 *et seq*.

I. COMMENTING PARTIES

The following organizations join in this comment:

American Great Lakes Ports Association ("AGLPA"), founded in 1977, is an organization representing the interests of commercial ports and port users on the United States side of the Great Lakes. AGLPA member ports are served by ocean-going vessel operators subject to Great Lakes pilotage regulations. Great Lakes ports are dependent on waterborne commerce and are therefore stakeholders of a safe, efficient, reliable and cost effective pilotage system.

The Canadian Shipowners Association (CSA) represent Canadian domestic ship owners operating in the Great Lakes, St Lawrence River, Eastern Canada and the Arctic With 86 vessel, the Canadian fleet carries approximates 60 million tons of cargo annually, which represents over 80 percent of the tonnage of the St Lawrence Seaway. Approximately half of the tonnage is between Canada and United States.

Shipping Federation of Canada ("SFC") is a trade association that represents and promotes the interests of the owners, operators and agents of ships involved in international trade, including the St. Lawrence and Great Lakes Seaway. The Federation has over 70 member companies from the United States and Canada, representing over 250 ocean shipping companies.

United States Great Lakes Shipping Association ("USGLSA") is a trade organization formed in 1956, consisting of vessel agent members located at major ports throughout the U.S. Great Lakes. USGLSA agents service the international flag vessel fleet entering the Great Lakes and calling at U.S. Great Lakes ports. The owners/operators of these vessels are the commercial maritime entities that employ Great Lakes pilotage services and as such, the matter of safe, reliable and economic pilotage is a vital concern to both USGLSA and the entities which they serve.

Canfornav Inc., Fednav International Ltd., Polish Steamship Company, Spliethoff Transport B.V., and Wagenborg Shipping also join in these comments.

II. BACKGROUND

The Great Lakes Pilotage Act of 1960, 46 U.S.C. Ch. 93 (the "Act"), requires certain U.S. and foreign vessels to use U.S. or Canadian pilots while transiting the waters of the St. Lawrence Seaway and the Great Lakes system. *See* 46 U.S.C. § 9302(a)(1). In 1996, USCG issued Appendices A, B, and C to 46 C.F.R. parts 403 and 404 to provide methodologies for use in establishing pilotage rates. *See* Great Lakes Pilotage Rate Methodology, 61 Fed. Reg. 21,081-01 (May 9, 1996) (*codified at* 46 CFR pts. 403, 404). After these three methodologies were added, although USCG relied on the Appendix A methodology to set rates, it did not set rates on an annual basis until 2006 when 46 U.S.C. § 9303 was amended to require that USCG "establish new pilotage rates by March 1 of each year. . . ." USCG has not made any material changes to its ratemaking methodology since 2006.

Appendix A is a legislative rule that USCG adopted after notice and comment. *See* 60 Fed. Reg. 18,370 (Apr. 11, 1995), *redesignated at* 61 Fed. Reg. 32,655 (June 25, 1996), *further redesignated by* USCG-1998-3976, 63 Fed. Reg. 35,139 (June 29, 1998). As set forth in the current Appendix A methodology (the "Current Methodology"), to determine the relevant pilotage rates, the Director must:

> (1) Collect financial information from the three pilot associations to project the total authorized operating expenses for each association;
>
> (2) Project the target pilot compensation based on the targeted rate of pilot compensation and the number of pilots needed in each district;

(3) Project revenue using the current pilotage rates;

(4) Determine each pilot association's investment base and an appropriate return on this investment base for each association;

(5) Determine each association's projected net income by subtracting projected expenses, which include pilot compensation, from each association's projected revenue;

(6) Compare the projected net income with the targeted return on the investment base for each association; and

(7) If there is a significant difference between the projected rate of return and the targeted rate of return on the investment base, the Director will adjusts the rates for pilotage services appropriately.

See Lake Pilots Ass'n, Inc. v. U.S. Coast Guard, 257 F. Supp. 2d 148, 152 (D.D.C. 2003) (internal citations omitted); *see also* 46 C.F.R. Pt. 404, App. A. After this process is completed, the Director initiates a rulemaking by publishing a NPRM and invites comments from the public, including from pilot and shipping interests groups. After public comments have been reviewed and necessary adjustments, if any, are made, a Final Rule is published establishing the new rates. However, if there is not a significant difference between the projected and targeted rate of return on the investment base, the Director leaves the pilotage rates unchanged. *See id.*

USCG has faced legal challenges to its Current Methodology and its ratemaking decisions. In *Lake Pilots Association*, a district court concluded that the 2001 Final Rule was arbitrary and capricious because USCG used compensation rates derived from a ship operating company, as opposed to reliance on union contracts, to determine compensation rates. *See* 257 F. Supp. 2d at 167. The court also found it arbitrary and capricious for USCG to categorically exclude cash assets from the pilot associations' investment base. *See id.* at 172-73. USCG faced a more recent challenge in *St. Lawrence Seaway Pilots Association Inc., et al. v. U.S. Coast Guard*, when pilot associations successfully challenged the 2014 Appendix A Final Rule with respect to target compensation. 85 F. Supp. 3d 197 (D.D.C. 2015). The district court found, among other things, that USCG's actions were arbitrary and capricious because the agency failed to provide any "rational justification for its decision to continue using data *the source of which* affirmatively stated was inaccurate[.]" *See id.* at 206 (emphasis in original).

On September 10, 2015 USCG issued the present NPRM. *See* Great Lakes Pilotage Rates - 2016 Annual Review and Changes to Methodology, 80 Fed. Reg. 54,484 (Sept. 10, 2015) (the "Proposed Methodology"). USCG issued the Proposed Methodology to address "certain methodology issues" that "both pilots and industry" have identified as issues that "significantly distort ratemaking calculations." *Id.* USCG also recites that the Proposed Methodology is being considered because USCG claims that it no longer has access to maritime union-supplied benchmark data previously used to determine pilot compensation. *See* 80 Fed. Reg. 54,484. Under the Proposed Methodology the Director must:

> (1) Review and recognize previous operating expenses based on audits of records provided by the pilot associations;
>
> (2) Project each association's future operating expenses, adjusting for inflation or deflation;
>
> (3) Project the number of pilots needed based on each area's peak pilotage demand data and the pilot work cycle;
>
> (4) Set target pilot compensation using a compensation benchmark;
>
> (5) Project each association's return on investment by adding the projected adjusted operating expenses and the total target pilot compensation and multiplying by the preceding year's average annual rate of return for new issues of high grade corporate securities;
>
> (6) Calculate each association's needed revenue by adding the projected adjusted operating expenses, the total target pilot compensation, and the projected return on investment;
>
> (7) Calculate initial base rates based on the preceding steps; and

> (8) Adjust the initial base rates if necessary and reasonable to do so for supportable circumstances, and set final rates.

See 80 Fed. Reg. 54,484.

III. STANDARD OF REVIEW

Federal courts have judicial authority to review USCG's ratemaking methodology determination under the Administrative Procedures Act ("APA"). Under the APA, there is a strong presumption of reviewability of agency action. *See Abbott Labs. v. Gardner*, 387 U.S. 136, 140 (1967). The court has the authority to "hold unlawful and set aside agency action, findings, and conclusions found to be":

> (A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; (B) contrary to constitutional right, power, privilege, or immunity; (C) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; (D) without observance of procedure required by law; (E) unsupported by substantial evidence . . .; or (F) unwarranted by the facts to the extent that the facts are subject to a trial *de novo* by the reviewing courts.

5 U.S.C. § 706 (2).

USCG's Proposed Methodology is considered a legislative regulation. *See Am. Pilots Ass'n, Inc.*, 631 F. Supp. at 830 ("Where Congress delegates the interpretation of the statute explicitly, regulations adopted by the agency interpreting the statute's terms have legislative effect.") (internal citation omitted); *see also Chevron v. Natural Res. Def. Council*, 467 U.S. 837, 844 (1984). While reviewing courts are frequently described as requiring deference to agencies in areas of "special competence," the district court in *St. Lawrence Seaway Pilots* recognized that the USCG's particular expertise lies in the area of maritime safety. *See St. Lawrence Seaway Pilots Ass'n, Inc.* 85 F. Supp. 3d at 204, fn. 9. The process of administrative ratemaking is far afield of USCG's primary missions and not an area in which significant judicial deference can be expected. *See id.*

IV. COMMENTS

A. The Proposed Methodology is inconsistent with USCG's delegated statutory authority.

The APA requires that all "agency action, findings and conclusions of law" must be within the agency's "statutory jurisdiction, authority, or limitations, or short of statutory right." 5 U.S.C. § 706 (2)(C). Indeed, "Congress has been willing to delegate its legislative powers broadly – and courts have upheld such delegation – because there is court review to assure that the agency exercises the delegated power within statutory limits. . ." *Ethyl Corp. v. E.P.A.*, 541 F.2d 1, 68 (D.C. Cir. 1976).

USCG received broad ratemaking authority through a series of delegations of authority. First, Congress delegated authority to the Secretary of Transportation.[1] The Secretary also established regulations that require USCG to "prescribe regulation rates and charges for pilotage services, *giving consideration to the public interest and the costs of providing the services.*" 46 U.S.C. § 9303 (emphasis added). Next, the Secretary delegated authority to the Commandant of USCG pursuant to 46 U.S.C. § 2104, who in turn delegated his authority to the Director of the Great Lakes Pilotage Office in the implementing regulations found at 46 C.F.R. Parts 401–404.

USCG must conform to the standards which accompanied the delegation of the power to prescribe rates. *See Farmers Union Cent. Exc., Inc. v. F.E.R.C.*, 734 F.2d 1486 (D.C. Cir. 1984). Pursuant to its authority as delegated from Congress, USCG is required to explain how a change in the regulation is "necessary to the provision of pilotage services." *Lake Pilots Ass'n, Inc.*, 257 F. Supp. 2d at 174 (finding the USCG must exclude cash expenses when not necessary for pilotage operations). USCG must also prescribe rates that consider the "public interest and the costs of providing services." 46 U.S.C. § 9303. The public interests includes provisions for safe,

[1] Now the Department of Homeland Security.

efficient, and reliable pilotage service on the Great Lakes. Equally important to the public interest, however, is a sustainable, economically sound rate structure that does not simply lock in avoidable pilotage costs. *See Lake Pilots Ass'n, Inc.*, 257 F. Supp. 2d at 152 (finding that the public interest includes "lower shipping costs"). As overseers of a regulated monopoly, USCG oversight and regulation is required to protect consumers and create space for economic efficiencies. *See Verizon Commc'ns, Inc. v. F.C.C.*, 535 U.S. 467, 543 (2002) (stating general principal that "[a]n agency engaged in traditional ratemaking will seek to protect consumers by mandating low prices as the end result").

In administrative ratemaking an inquiry into actual costs is generally considered "the most useful and reliable starting point for rate regulation." *Farmers*, 437 F.2d at 1502. Non-cost factors may be allowed in setting a rate, but "each deviation from cost-based pricing [must be] found . . . to be consistent with the [agency's statutory] responsibility." *See Mobil Oil Corp. v. FPC*, 417 U.S. 283, 308 (1974). Courts allow an agency to rely on non-cost factors to set rates primarily in recognition of the need to stimulate additional capacity. *See Farmers*, 437 F.2d at 1503. However, the agency must "forecast or otherwise estimate the dimensions of the need for additional capacity" and "attempt to calibrate the relationship between increased rates" and the desired result. *Id.*

If USCG contemplates increasing rates, "it must see to it that the increase is in fact needed, and is not more than is needed, for the purpose. Further than this we think the [agency] cannot go without additional authority from Congress." *City of Detroit v. FPC*, 230 F.2d 810, 817 (D.C. Cir 1995). Agency decisionmaking must be more than "reasoned" in light of the record. It must also be true to the congressional mandate from which it derives authority. Therefore, a reviewing court must be satisfied that the agency's reasons and actions "do not deviate from or ignore the ascertainable legislative intent." *Ethyl Corp.,* 541 F.2d at 36; *see* 5 U.S.C. § 706(2)(C) ("The reviewing court shall . . . hold unlawful and set aside agency action . . . in excess of statutory jurisdiction, authority, or limitations."). Beyond that, however, the court is not at liberty to substitute its own judgment in the place of the agencies'.

The NPRM fails to consider whether several elements of the Proposed Methodology are necessary. It also fails to consider the public interest in maintaining reasonable costs and whether the significant cost increases under the Proposed Methodology are excessive. Specifically, USCG fails to meet its delegated responsibility to consider these factors with respect to the use of weighting factors, the peak-demand staffing model, hourly rates during detention periods, the mandatory change point at Iroquois Lock, the elimination of rates based on distance, and American Pilots Association dues.

1. USCG fails to consider the weighting factor in setting pilotage rates.

The NPRM neglects to account for extreme differences in rates charged as a result of the weighting factor that is applied to pilot fees. Pilotage charges are calculated by multiplying the hourly rate by the hours that the registered pilot is on the bridge or available to the master of the vessel. This value is then multiplied by a weighting factor. Under 46 C.F.R. § 401.400 the weighting factor, which is based on the size of the ship, ranges from 1.0 to 1.45. *Id.*

The NPRM does not reflect application of the weighting factor in setting rates. It therefore overestimates the rates needed to ensure adequate pilotage revenues. The NPRM conducts its multi-step analysis to set pilotage rates to meet a target revenue figure given the expected demand in the upcoming year. This means that pilot charges should be set such that if the upcoming year's actual traffic is equal to the expected demand, the actual revenues received from the pilotage rate will equal the target revenue. However, actual pilotage charges include a weighting factor multiplier and additional charges (e.g. docking fees). Therefore, assuming actual traffic is equal to expected demand, pilot associations receive revenue above and beyond the target revenue amount. For example, if the average weighting factor for all vessel traffic in the 2016 season was 1.25,[2] this would mean that pilot associations will receive pilotage rates sufficient to reach the $18.6 M 2016 target revenue, plus an additional 25 percent in weighting factor revenue, plus any additional amount charged to vessel operators. The NPRM did not consider the additional revenue that pilot associations receive as a result of the application of weighting factors when it set pilotage rates to meet the target revenue amount of $18.6 M. Therefore, the NPRM overestimated the necessary rate for pilotage services. This represents a prime example of the NPRM's inaccurate assessment of its economic impacts and gross understatement of the actual rates paid (and revenues generated) by the Proposed Methodology should the NPRM become final.

The NPRM has also failed to account for the distribution of the increased pilotage expenses to ratepayers. The NPRM estimates that the Proposed Methodology will increase pilotage fees by approximately 50 percent. This figure, alarmingly high though it is, is based on a system-wide average, thus disguising even harsher negative impacts in certain instances. USCG admits that it "did not conduct a route by route analysis but rather focused on the revenue needed across the system to ensure safe, efficient and reliable pilotage service." *See* E-mail from D. Dean to S. Theis, Re: NPRM Question (Sept. 30, 2015). Based on our internal calculations using actual invoices, in 2015, if a U.S. pilot manned a Class 4 ship for all U.S. pilot segments of the transit from Thunder Bay to Montreal, with no interruptions or detentions, the fee for that transit was $ 37,739. If we keep the same assumptions but use the hourly rates under the

[2] This assumption is based in reality. According to GLPA provided data, in the 2014 shipping season the average weighting factor was 1.28 for all vessel traffic.

Proposed Methodology, the fee for that same voyage in 2016 will be $ 63,352. This represents a 68 percent cost increase. Certain other transits will experience fee increases well over 100 percent under the Proposed Methodology.[3]

The Proposed Methodology will effect a dramatic increase in costs for all vessel owners, and this effect may be especially harsh to vessels that operate on certain routes. While the Commenters do not oppose the weighting factor, as we recognize the rate formula must take into account each vessel owner's ability to pay for vessels of various sizes, the NPRM must consider the effect of the weighting factor on anticipated revenues when setting rates.

2. USCG fails to consider whether a peak-demand staffing model is necessary, in the public interest, or cost-efficient.

USCG has access to multiple sources of data to project demand for pilotage services in subsequent years, including historical data, input from pilots and industry, periodicals and trade magazines, and information from conferences. While relying upon these data sources, there has been little fluctuation in the number of pilots servicing the Great Lakes. And in fact, each year, from 2009 through 2015, USCG estimated that the number of pilots needed was either equal to or less than the number of pilots needed in the prior year.

USCG recommends in its Proposed Methodology that it switch to a peak-demand model without any analysis of the necessity or cost-efficiency associated with such a change. In the Current Methodology, the number of pilots is determined by first calculating the projected bridge hours necessary to service a particular area for an upcoming shipping season. This calculation is based on the time that a pilot spends on board a vessel providing basic pilotage service. The

[3] For example, consider the pilotage expense for a large vessel with a 1.45 weighting factor transiting from Port Huron to Burns Harbor (a trip that would take approximately 39.5 hours). Under the Current Methodology, the pilotage fee for this trip is $8,982. Under the Proposed Methodology, the fee would be $20,103. This represents a 123.8 percent increase in cost.

projected bridge hours are then divided by 1000 or 1800 to determine the number of pilots needed for designated or undesignated waters, respectively.

USCG proposes a rate designed to support employment of the "the number of pilots needed to meet each shipping season's peak pilotage demand periods without interruption to service." 80 Fed. Reg. 54,489. Under the Proposed Methodology, USCG determines each area's peak-demand over an historical multi-year base period. The NPRM provides two reasons to support this change: (1) "pilots frequently have commented in previous years' ratemaking rules that we should also take into account necessary demands on pilot time that go beyond bridge hours"; and (2) pilots have commented "that Step 2.B does not specify sources for our bridge hour projections and that inaccurate projections distort the rest of our ratemaking calculations." *Id.*

USCG must consider necessity and public interest in imposing the substantial cost increases proposed under the peak staffing model in the proposed rulemaking. The NPRM determines the number of pilots needed based on "each shipping season's peak pilotage demand periods." *Id.* USCG acknowledges that "peak traffic demand is concentrated at the beginning of a shipping season, to handle the traffic buildup created by the previous season's closure, and at the end of the season, when vessels seek to complete their voyages before closure." 80 Fed. Reg. 54,490. Nonetheless, the peak-demand staffing model maintains pilots on hand *throughout the season*, based on these discrete peak traffic times. The Bridge Hour Definition and Methodology Study (the "Study")[4] captures a 2011 snapshot of peak demand in each district. The Study shows District Three experienced a shortage of pilots on only one day out of the 270-day season. *See*

[4] USCG commissioned this June 25, 2013 study with MicroSystems Integration, Inc. of Pawcatuck, Connecticut. The purpose of the study was to develop a series of recommended adjustments to the ratemaking process in order to increase objectivity, increase transparency and understanding, and promote stability of rates. The Study was not embraced by Great Lakes Pilotage Advisory Committee.

Study at C-16. The statistics that year were similar for Districts One and Two. *See* Study at C-14, C-15. And on many other days during that same period, the number of pilots exceeded the amount needed to handle the available assignments. *Id.*

In spite of these statistics, the NPRM assumes that on average in late season over the base period, "one pilot could move one vessel per day. However, to fully meet peak season demand, the pilot association must be staffed to provide double pilotage in the designated waters of Areas 1, 5, and 7." 80 Fed. Reg. 54,496. The NPRM proposes to increase the number of pilots by a total of 14 pilots to meet peak-demand periods, at a cost of $312,500 per pilot, a lavish overall increase in revenues of $4,375,000. Using 2011 figures, USCG's proposed peak-demand methodology would cost industry $437,500 per day to ensure zero delays.[5] This approach is inefficient, costly, and not something that users of pilotage services have demanded or advocated. These costs are particularly indefensible when USCG does not require an increase in pilot staffing. Absent the adoption of measures that ensure increased staffing to meet the NPRM's ratemaking assumptions, the Proposed Methodology may simply increase revenues without commensurate increases in the number of pilots, thus simply magnifying individual pilot compensation rather than increasing pilot rosters or capabilities.

USCG has maintained that it has been able to provide safe, efficient and reliable service on the Great Lakes over the past five years while the demand has steadily risen and the number of pilots has steadily decreased. In some areas, though the number of pilots has remained constant, the hours of vessel delays have fluctuated greatly. *See* Study at C-11. In at least one instance, the total delay hours decreased despite a pilot being removed from an area. *Id.*

The NPRM's peak-demand staffing model assumes increases in the number of pilots required and over-staffs the number of pilots needed through the majority of the season. There is

[5] This figure assumes operations in designated waters.

no clear rationale expressed for this decision. USCG must study the effect of these proposed changes on industry members and determine the efficiency of such a change in light of the dramatic increased costs to ratepayers.

USCG should also evaluate less-costly alternative means of providing service during peak periods. These alternatives include the use of part-time contract pilots to supplement the full-time workforce (a practice utilized in the past), and cross-qualifying pilots such that pilots from one area are able to help relieve traffic delays in another area. Under the current inflexible work rules, pilots do not operate outside their geographic district.

While the Commenters and other affected parties support efforts to ensure adequate capacity in pilot staffing, we respectfully suggest that efficiency, safety, and cost-awareness can be reasonably and responsibly addressed at a less-than-peak-demand ratemaking assumption. While USCG is charged with providing efficient and reliable services, it is not necessary for USCG to strive for zero delays in the system. Further, USCG has not analyzed the public interest or the effects of these costs on ratepayers for a peak-demand staffing model or alternatives to that model.

3. The NPRM fails to consider the magnitude of expenses incurred by charging basic rates for periods of delay and detention.

Under Current Methodology, a pilot's hours are calculated by reference to bridge hours, that is "the number of hours a pilot is aboard a vessel providing pilotage services." 80 Fed. Reg. 10,374. In 2015, USCG explained, "we do not include, and never have included, pilot delay, detention, or cancellation in calculating bridge hours." *Id.* However, the Proposed Methodology recommends "amending § 401.420 (charges for a vessel's cancelling, delaying or interrupting pilotage service) . . . and basing those charges on the applicable hourly rates we would specify in § 401.405." 80 Fed. Reg. 54,487. USCG's consideration of these additional time factors necessarily inflates the number of hours worked by pilots.

Vessel delays and detentions are caused by external factors that cannot be predicted with precision, such as accidents and weather conditions. Under the Proposed Methodology, pilots will have the luxury of receiving government-mandated payments to ensure financial performance when unforeseen events intervene and targets are not met. Ratepayers, the vessel interests, have no such protection. Pilots' organizations are independent business entities which, like others in the commercial world, should be expected to bear some of the risk of providing service, especially when they enjoy no competition for the services.

4. USCG should not decide whether a mandatory change at Iroquois Lock is necessary during the ratemaking methodology debate.

This NPRM is not the appropriate venue to amend pilot change points. This docket addresses two substantial issues, the Proposed Methodology and the 2016 annual review of pilot rates. The NPRM summarily states that "in addition to the proposed methodology revisions and proposed 2016 rates, we also propose an additional location for beginning and ending pilot assignments (a 'change point') at Iroquois Lock." 80 Fed. Reg. 54485. The NPRM discusses this topic in one short paragraph, citing as support for this change the National Transportation Safety Board general recommendation that USCG promulgate new "hours-of-service rules." 80 Fed. Reg. 54487. The decision as to whether a mandatory change point at Iroquois Lock is necessary or cost effective merits additional discussion and a thorough investigation; it should not be decided as a drive-through topic in the NPRM.

USCG has not sufficiently investigated the necessity of a permanent pilot change point at Iroquois Lock. The NPRM lacks data concerning pilot fatigue and no discussion of shortcomings of the current policy of authorizing pilots on overnight assignments to request a new pilot at Iroquois Lock. The mandatory change point will leave pilots stranded at Iroquois Lock, which will necessarily increase costs and require additional pilots in District One. The NPRM does not investigate the impact of this proposed change on the number of Pilots needed in District One, nor does it include this change in the estimation of fees under the Proposed Methodology. *See* 80 Fed. Reg. 54485, 54487. We believe this proposal is of sufficient importance to merit full factual investigation of its operation and cost impacts, and detailed consultation with Canadian authorities, with a view to determining if there exists consensus about fatigue abatement measures. Currently, Canadian practice is to provide a pilot change at Iroquois Lock between 1600 and 0600 hours at no charge to the user. Commenters recommend that, following an investigation, this issue be made subject to a separate rulemaking proceeding.

5. **USCG failed to consider the effect of calculating all pilotage rates on an hourly basis.**

Currently, the rate tables calculate pilot rates differently for each area. *See* 46 C.F.R. 401.405, 401.407, 401.410. "Most of the pilotage costs charged in designated waters are for transits between two points." 80 Fed. Reg. 54487. In contrast, the pilotage costs in undesignated waters are generally calculated by an hourly fee. *Id.* The NPRM suggests that "[t]his mixed approach complicates an otherwise simple transaction of paying for a pilot's service[.]" *Id.* In response, the NPRM proposes to eliminate charges for transit between two points, and move to an hourly model regardless of whether the pilot is in designated or undesignated waters. *Id.* This is a novel suggestion, to our knowledge, no other pilotage area in North America bases pilotage services solely on an hourly rate.

Commenters oppose this proposal. Point-to-point pilot rates in designated waters are tailored to match the fee to the complexity and general conditions of the transit. A fixed fee per task regime provides certainty for vessel owners when calculating charter and freight rates. This rate structure encourages efficiency as pilots are paid for the service. Efficiency is particularly important in designated waters where the pilot is actively navigating the vessel, as opposed to in undesignated waters where the pilot is merely available.

6. The costs of American Pilots Association membership dues should not be subsidized by ratepayers.

In past ratemakings, American Pilots Association dues were, quite correctly, excluded from the ratemaking process as expenses that were unnecessary for pilot licensure. In the Proposed Methodology, USCG allows American Pilots Association dues to be recognized as a permitted operating expense "that is necessary and reasonable for the safe conduct of pilotage on the Great Lakes" because the American Pilots Association "shares[s] best practices and facilitate[s] the development of training plans for the U.S. Great Lakes Registered Pilots." *See* Great Lakes Pilotage Rates – 2014 Annual Review and Adjustment, 78 Fed. Reg. 48376 (Aug. 8, 2013). USCG itself recognizes that "it remains true that APA membership is not needed for licensure." *Id.* The Proposed Methodology places the burden of American Pilots Association membership on the ratepayers, entities whose benefit from the Association's activities are, at best, attenuated and indirect. These expenses are non-trivial and should not be allowed as recoverable expenses.[6]

B. The NPRM must meet the APA's "arbitrary, capricious, an abuse of discretion, and otherwise not in accordance with the law" standard of review.

Under the "arbitrary and capricious" standard, a reviewing court must conduct a "searching and careful" inquiry into the record in order to assure itself that the agency has examined the relevant data and articulated a reasoned explanation for its action including a

[6] Commenters recognize that American Pilots Association is a well-regarded association that has made positive contributions to the advancement of marine safety. However, it is also an advocacy and a potential litigant espousing positions that are at times either adverse to or at least not entirely congruent with the interests of ratepayers. *See, e.g., Am. Pilots' Ass'n, Inc. v. Gracey*, 631 F. Supp. 827 (D.D.C 1986) (challenging validity of minimum licensing requirements for certain pilots).

"rational connection between the facts found and the choice made." *Burlington Truck Lines v. United States,* 371 U.S. 156, 168 (1962). As the Supreme Court elaborated:

> Normally, an agency rule would be arbitrary and capricious if the agency has relied on factors which Congress has not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise.

Motor Veh. Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co., 463 U.S. 29 (1983). Most fundamentally, the court's task is "to ensure that the [agency] engaged in reasoned decisionmaking." *Int'l Ladies' Garment Workers' Union v. Donovan,* 722 F.2d 795, 815 (D.C. Cir. 1983); *see Am. Gas Ass'n v. FPC,* 567 F.2d 1016, 1029–30 (D.C. Cir. 1977).

When data which formed the basis of an agency decision are challenged, the agency is not always required to use new data, but must "provide a full analytical defense" and show that it is "conscious of the limits of" the data. *Eagle–Picher Indus., Inc. v. E.P.A.*, 759 F.2d 905, 922 (D.C. Cir. 1985); *Ass'n of Oil Pipe Lines v. F.E.R.C.*, 83 F.3d 1424, 1433–35 (D.C. Cir. 1996) (FERC's choice of index in setting pipeline rates was not arbitrary and capricious where record demonstrated "reasoned judgment in selecting" the "most suitable" index). Although courts will defer to the agency's choice of data when the agency was faced with competing data or models, *Pub. Emps. for Envtl. Responsibility v. U.S. Dep't of the Interior*, 832 F. Supp. 2d 5, 26 (D.D.C. 2011), the agency's choice is arbitrary and capricious when "there is simply no rational relationship between the model and the known behavior of the items to which it is applied." *Greater Yellowstone Coal. v. Kempthorne*, 577 F. Supp. 2d 183, 198 (D.D.C. 2008) (National Park Service's Final Environmental Impact Statement, relating to snowmobiles in Yellowstone, was vacated as arbitrary because it relied on unsound use level analysis which contained significant discrepancies).

The "arbitrary and capricious" standard demands that an agency provide a reasoned justification for its decision to alter an existing regulatory scheme. *See Motor Veh. Mfrs. Ass'n*, 463 U.S. at 42. While changed circumstances may justify the revision of regulatory standards over time, this does not eliminate the burden upon the agency to set forth a reasoned analysis in support of the particular changes finally adopted. *See id.*

1. USCG gives undue weight to GLPAC recommendations.

The Great Lakes Pilotage Advisory Committee (GLPAC) is a congressionally authorized federal advisory committee. *See* Federal Advisory Committee Act (FACA), 5 U.S.C. § 1, *et seq.* FACA requires that the membership of advisory committees be "fairly balanced in terms of the points of view represented and the functions to be performed by the advisory committee." 5 U.S.C. § 5(b)(2). The purpose of GLPAC is to serve as a sounding board for USCG to consult when taking significant action and formulating policy relating to the Great Lakes. 46 U.S.C. § 9307. The Proposed Methodology reflects considerable uncritical reliance on GLPAC recommendations. This reliance distorts USCG analysis of the impacts of the proposed rule.

GLPAC, as presently structured, has become weighted to reflect pilot interests to the detriment of ratepayers and other Great Lakes Seaway system stakeholders who will be adversely affected by this proposal. The current structure of GLPAC fundamentally favors pilots' interests.[7] GLPAC voting requirements ensure that industry views are extremely unlikely

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[7] As of the time of this comment, the current members who represent pilot interests include representatives from Lakes Pilots' Association, St. Lawrence Seaway Pilots Association, and Western Great Lakes Pilots Association. In July 2014, the USCG appointed the President of the Great Lakes District Council of the International Longshoremen's Association (ILA) to serve on the GLPAC as the member representing the interests of ports. Since 2006, Seaway Pilot, Inc., an affiliate of District One's pilot association St. Lawrence Seaway Pilots' Association, has been a party to a collective bargaining agreement with the International Longshoremen's Association, Local #2000. *See* St. Lawrence Seaway Pilots' Association 2014 Financial Statements (available at http://www.uscg.mil/hq/cg5/cg552/pilotage.asp) (last visited Dec. 8, 2015). Because the ILA's membership includes pilot association employees (e.g., office staff and boat crew), and because the President of a union presumably represents union members, the Coast Guard has effectively augmented pilot representation on GLPAC by reducing ratepayer/industry representation by one seat.

to obtain requisite votes.[8] This fact is critical considering that USCG has effectively interpreted GLPAC's July 2014 meetings as "votes" for various provisions contained in the Proposed Methodology. *See, e.g.*, 80 Fed. Reg. 54,498 (noting a 4-2 vote did not meet GLPAC's standards to approve a recommendation regarding total pilot compensation); *id.* at 54,487 (citing a GLPAC 5-1 vote to re-baseline the billing scheme). These "votes" are not representative of the ratepayers and should not be relied on as validation for any particular concept in the NPRM. GLPAC's recommendations adopted by USCG in the Proposed Methodology uncritically accept pilot-backed revenue enhancements. *See, e.g.*, *id.* at 54,490 (recommending 10-day recuperative rest period for pilots); *id.* at 54489 (recommending number of pilots needed should be based on number required to meet each season's peak pilotage demand periods without any interruption to service); *id.* at 54487 (eliminating rates based on distance in favor of rates based on hours).

GLPAC's recommendations are devalued, at least in a ratemaking context, because of industry under-representation.[9] The community quantitatively most affected by pilotage rates, non-U.S.-flag shipping interests, cannot serve due to advisory committee citizenship restrictions.[10] The owners and operators of vessels that contract for pilotage services are all foreign entities based abroad. At best, their positions find indirect expression in GLPAC. Industry has expressed its interest in improving the efficiency of pilotage services on the Great Lakes by: allowing cross-certification between districts to allow pilots to move vessels between

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[8] "Any recommendations to the Secretary under subsection (a)(2) must have been approved by at least all but one of the members then serving on the committee." 46 U.S. Code § 9307.

[9] At the time of this writing, the vice-president of CHS, Inc. is the sole industry representative. The U.S. Great Lakes Shipping Association representative's term expired on September 30, 2015.

[10] The NPRM states that "[a]lthough foreign citizens may not serve on GLPAC and therefore the foreign vessel owners are not GLPAC members, we believe the U.S. shipping agents are aware of and can adequately represent their interests. Also, the foreign vessel owners can and do attend GLPAC meetings and raise their concerns during each meeting's public comment period." 80 Fed. Reg. 54,486-87. However, as noted in the text above, these important stakeholders do not have direct voting representation and a prevalent characteristic of the NPRM is the absence of any expression of concern for ratepayer interests.

districts in times of peak traffic; by reevaluating the need for double pilotage due to the increased use of modern vessels with improved navigation technology; by equipping pilots with personal pilot electronic chart/navigation systems; and by encouraging the consolidation of pilot associations to minimize redundant expenses such as accounting and dispatching. None of these suggestions from industry have been adopted by GLPAC or supported by its pilot members.

The NPRM gives undue weight to comments and proposals arising out of GLPAC. As constituted, GLPAC is a pilot-dominated interest group and should be regarded as such. Its recommendations will all support additional pilot revenue. It may well be that useful operational suggestions can arise based on the on-the-water experience of its participants. It should not, however, carry any particular weight in deciding revenue issues such as those considered in the NPRM. USCG has been overly deferential to GLPAC in drafting the NPRM.

2. USCG arbitrarily excludes data in determining its historical multi-year base period.

Under the Proposed Methodology, the NPRM determines the number of pilots needed each year in part based on "each area's peak demand over an historical multi-year base period." 80 Fed. Reg. 54,489. This historical multi-year base period relies on the average peak-demand over the past five years to "compensate for normal year-to-year fluctuation in traffic and pilot availability[.]" *Id.* USCG then decides whether any of the data contained in that five-year period are "unavailable or unreliable," which is defined to include data from "an outlier year in which traffic was abnormally low or high and so could significantly distort our calculations." *Id.* The NPRM further notes that "[g]enerally, a traffic distortion of significant proportion, one that we would not expect be replicated within the next decade, would form the basis of this determination." *Id.*

Traffic patterns on the Great Lakes are highly variable. The concept of an "average" or typical season does not apply in the Great Lakes. Every season is unique due to a variety of factors that affect demand for vessel services. Rather than relying on objective statistics to determine whether the demand in a given year was an outlier, the NPRM relies on subjective assessments. Under the Proposed Methodology, *two of the five* years the NPRM considers in calculating its five-year historical model are deemed to be unrepresentative of actual traffic in the Great Lakes. It considers 2014 to have been an unreliable outlier season because of a 17 percent increase in shipping traffic, extended ice conditions and associated delays, and the extensive use of double pilotage due to unusually hazardous conditions. 80 Fed. Reg. 54,495. The NPRM also casts out 2009 as an unreliable outlier season because of abnormally low traffic reflecting the 2008 global recession. *Id.* Each of these years is a part of the factual reality of Great Lakes Shipping and should be included in the NPRM's analysis of activity in the Lakes. The NPRM also could have factored in available traffic data from the beginning of the 2015 shipping season to the time the NPRM was published in September. Lake traffic volumes will fluctuate from season-to-season. However, the deletion of 40 percent of the traffic data from any five-year measurement period is more distortive of actual conditions than is taking the data as they come over a base period sufficiently extensive to prevent significant anomalies. The decision to arbitrarily exclude the 2009 and 2014 seasons and to fail to consider the available data on the 2015 season has, in our view, resulted in a gross underestimation of the pilot associations' revenues for 2015. As previously stated, the increases proposed in the NPRM will almost certainly result in revenues that far exceed target revenues.

The docket states that actual 2014 revenue was approximately $18.3 million. Commenters recognize that 2014 reflects an extended double pilotage period at the beginning of the shipping season. However, the NPRM removed 2014 from the historical base instead of extracting the extra revenues generated from the extended double pilotage period to determine adjusted revenue for that year. This would allow increased compatibility with other years. Because vessel traffic in 2015 (per the GLPA data through the end of October) is approximately the same as 2014, it seems that the 2014 traffic volume is not atypical. The NPRM was published in September of 2015, late enough in the season to note the vessel traffic in 2015 and to recognize that 2014 is not an outlier year.

When 2015 closes and actual full-year traffic and revenue data are available (leaving to one side problems in how revenue data are compiled, maintained, reported, and verified), we think it highly likely that 2015 actual revenues will far exceed target levels set for that year. This excess seems inevitable given the 10 percent increase in base rates for 2015 and the 10 percent surcharge for training. USCG has established no mechanism for returning this expected excess revenue to the ratepayers, either through refund or through being input into calculations of the 2016 rate.

Commenters further respectfully suggest that it is highly likely, barring dramatic external events that drastically depress cargo levels, that 2016 revenues will far exceed the $18.6 million revenue requirement set out in the NPRM.

C. 2016 Rate Levels based on the Proposed Methodology reflect a process that is arbitrary, capricious, an abuse of discretion, and otherwise not in accordance with law.

1. The NPRM arbitrarily adjusts pilots' target compensation upward by 10 percent on the basis of Canadian pilot compensation and proposed similar rates for designated and undesignated waters.

The NPRM notes that the "difference in status between [the Canadian Great Lakes Pilotage Authority (GLPA)] employees and independent U.S. pilots creates significant differences in their relative compensation." 80 Fed. Reg. 54,498. Based solely upon this assertion, it notes that "these differences constitute supportable circumstances for adjusting target pilotage compensation by increasing it 10 percent over our projected 2016 GLPA compensation figure." *Id.* The NPRM notes that "the appropriateness of 10% as an adjustment figure was not put to a vote," but relies on certain by comments of GLPAC members in a July 2014 meeting. *See* Great Lakes Advisory Committee 07-24-2014 Meeting Transcripts at 45:7-8 (stating that $295,000 is "the Canadian rate times 10%. It's the Canadian number times 10."); *id.* at 45:9-15 ("Boyce: I think its well justifiable to be 10 percent higher."). The NPRM admits that there are "no economic data that suppl[y] supportable circumstances for additional adjustments to target pilot compensation." 80 Fed. Reg. 54,498. For rulemaking purposes, that should be the end of the discussion. The 10 percent upward adjustment is completely arbitrary and unsupported by empirical analysis.

Comparisons between U.S. and Canadian pilots must be undertaken carefully. Canadian pilots perform a larger proportion of their services in designated waters; U.S. pilots in the Great Lakes often operate vessels over long stretches of undesignated waters that are not particularly challenging from a navigational or pilotage standpoint. Unlike pilots in designated waters, pilots in undesignated waters are only required to be "available" to the Master. *See* 46 U.S.C. § 9302. Service in undesignated waters is less demanding as most of their time on board does not require active pilotage, a fact that has been recognized in previous ratemakings. To the extent that comparisons with Canadian pilotage should be reflected in a rate setting context, data are necessary to ensure that these comparisons are for like services and activities. Canadian pilots also earn higher compensation because their pilotage system is organized into a single entity. As a result, lower administrative expenses and fixed costs may increase the take-home compensation for individual pilots. Again, the record does not explore these issues and offers no basis for "plussing" up revenues by a factor of 10 percent other than someone mentioning that figure at a meeting. The record does not support a conclusion that there are significant differences in pilot compensation for similar services or that what differences that exist are not the result of elective factors that could be resolved through non-revenue adjustments.

2. USCG cannot authorize ratemaking methodologies that permit cost recovery of expenses not yet incurred.

For the past twenty years, the purpose of the ratemaking provisions has been "to ensure safe, efficient, and reliable pilot services are provided on the Great Lakes." 80 Fed. Reg. 54,484. Embedded in the text of the NPRM is the suggestion that the purpose be revised and expanded to "promote safe, efficient, and reliable pilotage service on the Great Lakes, by generating for each pilotage association sufficient revenue to reimburse its necessary and reasonable operating expenses, fairly compensate trained and rested pilots, *and provide an appropriate reserve to use for improvements.*" *Id.* at 54,488 (emphasis added). This change is significant, arbitrary, and an unexplained deviation from past practice and reasoning. In the past, when faced with a request to authorize rate increases prior to costs being incurred, USCG consistently stated that "the regulations are clear that expenses are recognized on a reimbursable basis only." Rates for Pilotage on the Great Lakes, 71 Fed. Reg. 16,505 (Apr. 3, 2006). And thus, "[o]nly reasonable and necessary expenses actually incurred in the course of a pilotage season are subject to reimbursement." *Id.*

Wielding this proposed new standard, the NPRM makes several references to the future revenues the pilot associations are said to require to provide "improvements," but it never defines what these improvements might appropriately entail. One such new expense, though not described as an improvement, is an estimated $900,000 in costs "to be incurred in 2016" for training expenses. The NPRM proposes to permit the ratemaking mechanisms to anticipate these estimated costs *before* the expenses are actually incurred.[11] This action is prohibited under generally accepted ratemaking principles. *See Tennessee Gas Pipeline Co. v. F.E.R.C.*, 606 F.2d 1094, 1121 (D.C. Cir. 1979) (noting that when "advances [a]re not 'used and useful' for providing service to then current rate payers, [the] traditional rate making principles would call for exclusion from rate base."). The proposed new language regarding the creation of an "appropriate reserve" should be deleted absent substantial explanation of what costs are included in this reserve, and detailed quantification of what costs will be allowed over the multi-year period for which the new methodology is proposed. As now stated in the NPRM, this new standard, a standard that has no precise definition or quantification, becomes a potential rate increase driver in out-years, limited only by the imagination as to what expense items might constitute improvements.

D. USCG must consider suggested alternatives to the Proposed Methodology.

It is well established that an agency has a duty to consider responsible alternatives[12] to its chosen policy and to give a reasoned explanation for its rejection of such alternatives. *See, e.g., Motor Veh. Mfrs. Ass'n*, 463 U.S. at 49-51; *Int'l Ladies' Garment Workers' Union*, 722 F.2d at 815.

1. USCG should eliminate the Step 8 discretion in setting rates under the Proposed Methodology.

[11] USCG erroneously included a similar advance payment surcharge for pilot training expenses in its 2015 NPRM.

[12] The "arbitrary and capricious" standard does not "broadly require an agency to consider all policy alternatives in reaching decision." *Motor Veh. Mfrs. Ass'n*, 463 U.S. at 51. Agency action "cannot be found wanting simply because the agency failed to include every alternative device and thought conceivable by the mind of man . . . regardless of how uncommon or unknown that alternative may have been." *Vermont Yankee Nuclear Power Corp. v. NRDC, Inc.*, 435 U.S. 519, 551 (1978). However, the process in this instance reflects very little consideration of alternatives to the proposed increases.

Step 8 of the Proposed Methodology allows USCG to make discretionary adjustments to initial rate calculations if the adjustment is made under "supportable circumstances" and is "necessary and reasonable." 80 Fed. Reg. 54,491. According to USCG, a supportable circumstance can be found in a broad range of circumstances, including any factors mentioned in the current U.S.-Canadian agreement relating to Great Lakes pilotage. *See id.*

In past years commenters have noted that USCG has abandoned the current calculation methodology and instead exercised its discretion to implement a fee that is based on external circumstances. *See, e.g.,* Comments to Great Lakes Pilotage Rates: 2015 Annual Review and Adjustment, Docket ID: USCG-2014-0481-0015. USCG personnel have acknowledged this possibility. *See* Great Lakes Advisory Committee 07-24-2014 Meeting Transcripts at 118:3-13 ("Haviland: I don't mean to be argumentative but Rich can tell me if I'm wrong. I don't think our regulation allows us to [make associations whole on capital expenditures]. Walters[13]: You know, Todd, it would probably come under step seven, your *famous discretion.* Haviland: Okay. Walters: You know, so I wouldn't say you can't do it. It's just, you know, how do I -- how do I wordsmith your thinking.") (emphasis added). Although the Proposed Methodology requires a "necessary and reasonable" condition, the potential for abuse of discretion under Step 8 of the Proposed Methodology remains. For example, as noted above, USCG used its Step 8 discretion in reaching the determination that it intends to allow $900,000 in additional fees for training that has not yet occurred. Not only is this a substantial amount to impose upon ratepayers with little justification, but, as previously discussed, USCG does not have the statutory authority to implement this type of surcharge. USCG's application of discretion in the past has not inspired confidence among ratepayers in a system that permits unconstrained discretionary adjustments to rates and steadily rising fees. On two other occasions, USCG unilaterally elected to impose

[13] Richard Walters is counsel for the United States Coast Guard.

discretionary rate increases despite the applicable methodology indicating that a decrease in rates was required. For example, in 2013 the methodology resulted in a 15.89 percent rate reduction, but USCG arbitrarily implemented a 1.87 percent increase. *See* 77 Fed. Reg. 45,540. Likewise, in 2014, the methodology resulted in a 10.28 percent reduction in pilotage rates, but USCG arbitrarily chose to implement a 2.5 percent increase. *See* 79 Fed. Reg. 12,088. USCG's discretion appears to be biased in favor of rate increases – regardless of the calculation of rates according to the approved methodology.

We therefore recommend that the Proposed Methodology remove Step 8. If USCG is unwilling to eliminate Step 8 in its entirety, we recommend an amendment to Step 8 that would expressly acknowledge that in exercising this "famous discretion," USCG must consider the economic and financial impacts of such discretion on ratepayers, other economic interests in the region, and the public interest.

2. USCG should utilize an alternate negotiated rulemaking process.

USCG should begin each ratemaking process with a negotiated rule. Negotiated rulemaking is a consensus-based process through which an agency develops a proposed rule by using a neutral facilitator and a balanced negotiating committee composed of representatives of all interests that the rule will affect, including the rulemaking agency itself. *See* 5 U.S.C. § 562. This process gives all interested parties the opportunity to try to reach an agreement about the main features of a rule before the agency proposes it in final form.

A negotiated rulemaking process would solve a critical flaw of the USCG's ratemaking process, namely that it is largely a dialogue between USCG and pilots about how much money to take from vessel operators to give to pilots. This alternate rulemaking process would allow an opportunity for direct dialog and an interchange of views among industry and pilot associations.

Negotiated rulemaking would develop a complete and accurate record of decisions and has potential for arriving at a constructive and creative synthesis of different viewpoints, from all affected interests.

Many other agencies utilize a negotiated rulemaking process. Since enactment of the Negotiated Rulemaking Procedures Act in 1990, over 85 regulated negotiations have been completed, with several agencies utilizing this procedure including the Department of Interior, Department of Labor, Department of Transportation, Department of Education, and the Department of Housing and Urban Development. *See* David M. Pritzker & Deborah S. Dalton, Negotiated Rulemaking Source Book (Sept. 1995). USCG has utilized this process on at least two occasions. *See* Drawbridge Operation Regulations, Chicago River, IL, 60 Fed. Reg. 18,061 (Apr. 10, 1995) (*codified at* 33 C.F.R. Pt. 117); Vessel Response Plans and Carriage and Inspection of Discharge-Removal Equipment, Notice of Intent to Form a Negotiated Rulemaking Committee, 56 Fed. Reg. 58,202 (Nov. 18, 1991) (*codified at* 33 C.F.R. Pt. 155).

We recommend the approach followed by many U.S. Government agencies to utilize negotiated rulemakings and bring stakeholders together at the beginning of the process to find agreement.

3. USCG should consider the economic realities of vessel operations on the Great Lakes in its ratemaking determinations.

Pilotage rates under the Current Methodology, for reasons uncorrected in the Proposed Methodology, have little relationship to the economic conditions that affect ratepayers using pilotage services. Both Current and Proposed Methodologies impose an asymmetric, disconnected system in which ratepayers are subject to the vagaries of international economic conditions and the volatile economics of shipping conditions, but a major cost (in some cases *the* major cost) element of a Great Lakes vessel call is dictated by government rulings based on projections and suppositions that are never trued up to actual data. This is not a sustainable regulatory system.

We note that USCG found no small entities would be adversely affected by the rates under the Proposed Methodology because "large, foreign-owned shipping conglomerates or their subsidiaries owned or operated all vessels engaged in foreign trade on the Great Lakes." 80 Fed. Reg. 54,503. The NPRM failed to consider the significant impact that pilotage rates have on commerce in the St. Lawrence Seaway/Great Lakes system. Pilotage rates are a substantial cost factor for vessel traffic in the Great Lakes. Currently, the daily cost of pilotage services can exceed the daily cost of chartering the entire vessel, including crew wages and insurance. *See* Richard Greiner, Ship Operating Costs, (available at http://greece.moorestephens.com/en/Publications.aspx) (last visited Dec. 9, 2015); *see, e.g.*, GAP SA Grains & Produit Comment, Docket ID USCG-2015-0497 (Nov. 6, 2015). This significant cost impact directly affects the competitiveness of the shipment of goods by vessel as opposed to other modes of transport such as trucking, rail, and barge. *See* GAP SA Grains & Produit Comment, Docket ID USCG-2015-0497 (Nov. 6, 2015).

Similarly, if pilotage rates are too high, vessel operators may choose another route to market that avoids the Great Lakes altogether. Vessel operators who pay these pilotage rates operate on thin margins. Cost increases may necessarily be passed on to the manufacturer. Pilotage rates also affect a manufacturer's determination as to whether it should import or export goods at all. A manufacturer's decision to reduce the amount of goods it ships due to costs will have a ripple effect on many small businesses that depend on ship and cargo traffic, such as ship agents, towage companies, stevedoring and terminal operators, and trucking and distribution companies. A radical increase in pilotage rates, as proposed in the NPRM, can have a negative impact far beyond the "large, foreign-owned shipping conglomerates" cited by the USCG. A 2011 study of the economic impacts of Great Lakes Seaway shipping shows that foreign-flag shipping that is subject to pilotage requirements supports 13,741 jobs in the United States, generates $1.7 billion in U.S. business revenue, and supports $1.1 billion in personal income for Americans. These data reveal that USCG decisions will have a broad potential impact on American citizens. *See* Martin Associates, *The Economic Impacts of the Great Lakes and St. Lawrence Seaway System* (Oct. 18, 2011) (available at http://www.greatlakes-seaway.com/en/seaway/facts/eco_impact.html.) (last visited Dec. 9, 2015).

4. USCG should consider options to decrease costs and increase efficiency.

USCG's mandate requires that it strive to encourage "safe, *efficient*, and reliable services." The Proposed Methodology does not promote efficiency in the delivery of pilotage services.

The U.S. waters of the Great Lakes and the St. Lawrence Seaway are divided into three districts. Pilotage in each district is provided by an association certified by the USCG Director of Great Lakes Pilotage to operate a pilotage pool. USCG sets overall revenue methodology, but does not direct the actual compensation that pilots receive. Actual compensation is determined by each of the three district associations, each of which uses different compensation practices. This structure has led to several distortions that adversely affect ratepayers. The Current Methodology incentivizes pilot associations to understaff pilots and to overestimate overhead. For example, during the 2014 shipping season, only 11 pilots were operating in District Three despite the 2014 annual review setting rates based on a need for 15 pilots operating in the District. *See* Great Lakes Pilotage Rates – 2014 Annual Review and Adjustment, 79 Fed. Reg. 12,094 (Mar. 4, 2014). The net effect of this understaffing is that each pilot operating in District

Three received a larger share of the profits.[14] Neither the Current or Proposed Methodology addresses this kind of disconnect between ratemaking assumptions and association practices. In fact, absent control over the cost structure of pilot services, the methodologies encourage costly inefficiencies.

We recommend that USCG consider consolidating the three U.S. Great Lakes pilotage organizations to achieve cost efficiencies.[15] Consolidation would eliminate redundant functions such as bookkeeping, accounting, dispatch, and administrative duties. Consolidation would also enable pilots to be trained and flexibly deployed to work where needed. This would do much to eliminate service delays. It is important to note that a single entity provides pilotage services for the same geography on the Canadian side of the Great Lakes. Thus, there is strong evidence that a similar structure would work in the United States.

USCG should also examine how the pilotage function itself might be improved and made more cost-effective with new technologies, utilization of personnel, and new business models used by vessel operators. The 2014 season made extensive use of double pilotage, the practice of assigning two pilots to a vessel, because of unusually hazardous conditions such as ice and the seasonal removal of aids to navigation. However, given the increased use of modern vessels and improved navigation technology, USCG should consider decreasing the use of double pilotage. Instead, USCG unilaterally assumes that an increase in the use of double pilotage is necessary to meet the Proposed Methodology's peak-demand assumptions.

5. USCG should study the issues affecting pilot recruitment and retention.

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[14] While pilot associations may assert that district understaffing is due to the inability to retain and recruit pilots, USCG has not, to our knowledge, researched whether recruiting and retaining pilots is an issue. If recruiting and retention is an issue, we recommend that USCG study this issue, as discussed in Section D (5) of this comment.

[15] USCG has authority to limit the number of pilotage pools under 46 U.S.C. § 9304(b)(1).

The NPRM cites pilot association claims that "several experienced pilots have left the system and that other desirable mariners have been discouraged from applying" due to the pilots associations having inadequate revenues to recruit and retain adequately qualified pilots. *See* 80 Fed. Reg. 54,486. USCG cites these claims as a primary justification for enhanced revenue to pilot organizations and pilots. Unfortunately, the USCG cites no evidence of having verified these claims or having examined the many issues – beyond compensation – that effect pilot recruitment and retention. USCG has never, to our knowledge, conducted a disciplined, empirical evaluation of recruitment issues to develop strategies to address the concerns noted by the pilot associations.

We recommend that USCG consider the inputs affecting pilot recruitment and retention.[16] For example, we recommend USCG study:

1. Whether entry barriers, such as apprentice periods, buy-in costs, application requirements, etc. discourage applicants, or conversely, whether modest financial incentives paid to applicants at the outset of the recruitment process might encourage new applicants;
2. Whether other available incentives would improve the pilot associations' abilities to attract and retain new pilots such as quality of life, living standards, and job satisfaction;
3. Statistical and historical pilot retention issues by, among other means, conducting interviews with pilots who have left the Great Lakes system; and
4. Whether the revenue sharing practices used by pilot associations discourage new entrants.

V. RESPONSES TO QUESTIONS POSED BY USCG

The NPRM requested comments on six questions. The questions and our responses follow:

[16] Many of these recommendations were also included in the Study. *See* Study at B-60.

A. Question: Please note that we propose making the following procedural and rate changes effective 30 days after publication of a final rule, almost half a year earlier than the August 1 effective date we have used in previous rulemakings. We specifically request comments on this proposed change.

   Response: The proposed rate should be published at least 90 days in advance of implementation to meet common marine industry contract requirements. The final rate should be established at least 90 days in advance of the estimated commencement of the shipping season to permit ratepayers to betters assess their costs when making vessels commitments.

B. Question: We specifically request public comment on whether there is an objective standard that we can and should use in each annual ratemaking, to determine whether a particular shipping season should be treated as an "outlier."

   Response: As stated in the body of the comments, there is no "typical" or average season on the Great Lakes. Furthermore, USCG should: (1) consider the latest available data, including the 2014 and 2015 shipping seasons; (2) consult vessel owners, trade associations, and entities servicing the Great Lakes to understand factors and trends that affect the forecast; and (3) information from exporters and importers, shipping companies, ports, marine organizations (e.g., American Great Lakes Ports Association, Great Lakes Pilotage Association, United States Great Lakes Shipping Association, Shipping Federation of Canada, and Canadian Shipowners Association), and trade associations (e.g., boards of trade and chambers of commerce).

C. Question: We specifically request public comment on other possible sources of available and reliable data for shipping seasons prior to 2009.

   Response: Accurate data collection is essential to the ratemaking process. We are less concerned about pre-2009 data than we are about data used to set rates for the current period. For more recent data, USCG should consider information from the following sources: Exporters, Importers, Shipping Companies, Ports, Marine Organizations such as the American Great Lakes Ports Association, Great Lakes Pilotage Association, United States Great Lakes Shipping Association, the Shipping Federation of Canada, Trade Associations such as Chambers of Commerce, and Board of Trade.

D. Question: For this 2016 ratemaking, we considered three sources for possible benchmark compensation data that provide compensation data for occupations similar to that of a Great Lakes pilot. All of these sources provide current and available data that is open for public review: Canadian Laurentian Pilotage Authority (LPA) pilot compensation data; masters, mates and pilots wage data from the BLS, and Canadian GLPA registered pilot compensation. We specifically request public comments suggesting any other current, reliable, and publicly available sources we should consider in setting the 2016 season's target pilot compensation.

Response: We do not agree that Canadian pilot compensation should be used as a benchmark. Canada has its own unique social programs, tax regime, and currency. Further, U.S. pilots are self-employed, while Canadian pilots are employed by a government corporation. Canadian pilots work a higher proportion in "designated" waters than U.S. pilots. In other words, comparisons with Canadian pilots require a detailed awareness of distinctions between them and their American counterparts. These distinctions are sufficiently complex to discourage any high degree of reliance on comparison data. We urge USCG to retain the current benchmark - the compensation of first mates on U.S.-flag Great Lakes vessels. USCG provides insufficient discussion explaining why this current benchmark is being abandoned. USCG cites that the data is no longer being made publically available by the American Maritime Officers Union (AMOU); however, this seems to be unclear. AMOU submitted comments to the docket during the 2014 rate setting in an effort to clarify their compensation level. Thus AMOU appears to have recently been willing to provide the needed information. Current Appendix A regulations cite that target compensation it to be determined based on the most current union contracts. The regulations do not limit those contracts to the AMOU. The Marine Engineers Beneficial Association (MEBA) also represents U.S.-flag vessel officers. USCG provides no evidence that it sought compensation data from MEBA. We urge USCG to continue to use the current benchmark and form an industry working group to resolve information access issues with AMOU and/or MEBA. This information, although recently withheld by the relevant union, probably could be derived or otherwise constructed with some degree of accuracy. The use of BLS data, particularly if it can be disaggregated to approximate Great Lakes specific data, may be a positive substitute for union data. We remain convinced that the proper avenue is for similar rates, once properly compared, to be charged by both the GLPA and the USCG (in line with the Memorandum of Understanding between the United States Coast Guard and the Great Lakes Pilotage Authority in 2013).

E. Question: As previously discussed, the difference in status between GLPA employees and independent U.S. pilots creates significant differences in their relative compensation. These differences constitute supportable circumstances for adjusting U.S. target pilot compensation by increasing it 10 percent over our projected 2016 GLPA compensation figure, taking our proposed U.S. individual target pilot compensation to $312,500. Although the appropriateness of 10 percent as an adjustment figure was not put to a vote, that figure and no other was cited by several speakers at GLPAC's July 2014 meeting as balancing the different status of the U.S. and GLPA pilots. We invite public comment on whether the 10 percent adjustment figure is appropriate for the 2016 rate.

Response: We have addressed the problems of this approach in the body of our comments and in our response to Question D, above. We question whether there are "significant differences" in compensation between U.S. and Canadian pilots once comparability adjustments are rationally applied. In any event, we submit that the rate-setting process is legally and logically defective if, in any aspect, it works backward from individual pilot compensation figures, assuming those figures are reliable. The process should identify permissible costs and provide revenue sufficient to cover those costs. Such costs include reasonable pilot compensation.

F. Question: We also note that our proposed individual target pilot compensation, $312,500, is 10 percent higher than what we project as 2016 GLPA individual pilot compensation. By contrast, $355,000 would be about 25 percent higher than the GLPA compensation, and $394,000 would be about 39 percent higher; we question whether such large disparities can be justified. We specifically request public comment and supporting data on the pilot associations' proposal for setting the 2016 individual target pilot compensation.

   Response: We do not believe that USCG is using the correct benchmark for target compensation. *See* Response to Question D above.

VI. CONCLUSION

The Commenters, while opposing the NPRM in many of its aspects, appreciate the Coast Guard's efforts to find a defensible, economically sustainable methodology for setting pilotage rates. The NPRM is sufficiently flawed to require its withdrawal. However, there is no question that the ultimate goal of all interested parties is an efficient, economically sustainable rate structure that fairly compensates competent pilots for their contributions to safe navigation on the Great Lakes. We are prepared to work with the Coast Guard, pilots, and other affected interests to achieve a fair, rational, and lawful rate structure.

Respectfully submitted,

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