DANGEROUS WATERS: ECONOMIC CONSEQUENCES TO THE STATE OF A SALES TAX ON WATER TRANSPORTATION SERVICES

Submitted to the Sales Tax Exemption Study Commission
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on behalf of the Florida Ports Council
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The argument: Removing the state sales tax exemption on services will work an injurious, perhaps destructive, effect on the shipping, distribution and cruise industries in Florida. It will drive shippers to offload cargo at other American coastal cities and at Caribbean ports, particularly those in a position to offer discounts and preferential rates. Efforts to expand services through intermodal links between Florida ports and points north will be frustrated by additional taxation. As a sales tax on maritime transportation affects Florida ports' revenues, their ability to compete in financial markets for investor dollars, as well as their ability to retire current debt, will be undermined. Finally, Caribbean ports that have steadily increased their share of the cruise ship market over the years -- especially ports that offer financial incentives to cruise lines -- will benefit from a discouraging tax climate in Florida.

Background

Unique among the several states, Florida has the greatest number of seaports -- 11 -- and its southernmost position in the continental United States has enabled it to trade efficiently and productively with Central and South America and the Caribbean islands in ways no other state has rivaled.

However, Florida's peninsular shape has undeniable drawbacks as well, and its geographic proximity to major foreign ports to the south does not automatically guarantee a lucrative seagoing trade in custom and passengers.
Florida's land mass, from the Port of Miami near its tip to the Georgia border, is over 400 miles. That statistic has always been -- and always will be -- a factor in the decision by a particular shipper to dock at a Florida port with non-Florida-bound goods. Is it cheaper, for example, to offload coffee at Miami and ship it over land to distribution points outside the state? If there is no economic benefit to be gained, that coffee cargo will simply head for New York City, which until the early 1980s was the traditional port of entry.

For decades, Florida ports have watched as cargo from South America, Europe and the Far East steamed to ports in Washington State, California, Texas, Louisiana, Georgia, South Carolina and New York. In recent years, however, port officials have made inroads in that traffic by taking a more aggressive negotiating stance in an effort to lure commerce to Florida. With shippers' profit margins razor-thin, even apparently small financial savings become a major excuse to alter a cargo's itinerary. Competition in the shipping industry, needless to say, is cutthroat.

By the same token, a 5 percent increase in the cost to ship goods through a Florida port is a major disincentive to shippers. It is well to recall the state's flirtation with a unitary tax earlier in the decade. During the roughly one year that the 5 percent tax was in effect on national and multinational corporations with "unitary" activities in Florida, the state became nothing less than a commercial pariah, losing a number of multinational companies headquartered in South Florida.

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The lesson of the unitary tax is clear: the business community can be flexible to a point, passing along costs to consumers until it perceives that higher prices have made its goods or services unaffordable. Just as a customer is rarely, if ever, a captive, neither is a company or even an entire industry the captive of a city or state. This is especially true when other cities and states can bring down the cost of doing business so far that relocation becomes not only feasible, but intelligent.

**The Myth of “Captured Cargo”**

There is a belief in the maritime transportation industry that, somehow, cargo bound for Florida is “captured cargo,” that is, that no shipper with goods destined for Florida markets would think twice about offloading at a Florida port.

Unfortunately, that is a hollow myth. Business, as we have seen, can come and go as far as Florida is concerned. The same applies to seagoing trade. Only a few years ago, better than 75 percent of Far East cargo bound for Florida markets entered through non-Florida ports. While that situation is changing for the better, it is wise to examine why the problem exists in the first place. The case of Evergreen Lines, a Taiwan-based shipper, offers some insight. In the final six months of 1986, its steamships were responsible for bringing in some 6,900 forty-foot-equivalent container units to South Florida. The port of entry, however, was not Miami -- it was Charleston, S.C., some 500 miles north of the container units’ final destination. The cargo was then railed in via Florida East Coast Railway. Why was it cheaper to haul the goods...
over so much terrain? The answer has partly to do with the subsidy that South Carolina provides Charleston, enabling the port to offer lower handling charges.

It is well to remember that other states -- among them Louisiana, Alabama and neighboring Georgia -- also cushion their ports economically. Keep in mind, too, that Evergreen is by no means the only exception to the "captured cargo" notion. West Coast ports like Seattle and Long Beach have been able to attract shipments of Far East consumer products and foodstuffs bound for Tampa and Miami -- both major ports capable of servicing the respective shippers, American Presidents Line and K Line.

That the cargo did not dock in Florida waters but instead was transported intermodally over thousands of miles is eloquent testimony to the state's often uncompetitive posture. More to the point, it must be assumed that an additional 5 percent port sales tax will multiply the number of shippers who elect to find more complicated but, in the end, less expensive means of bringing cargo to Florida markets.

Intermodal Expansion

Florida ports have traditionally paid their way as maritime transshipment centers -- ports that serve as but one offloading point in a long, seagoing itinerary. To increase their appeal as intermodal ports -- ones capable of accepting goods for immediate transfer to trucks and freight trains -- has been an important goal of the Florida Ports Council. In keeping with this, South Florida officials have begun planning dedicated rail service linking the Port of Miami to the Port of Jacksonville and ultimately to Baltimore and New York City. The goal is to increase the competitive edge of the Port of Miami over, say, Atlanta and Savannah by slashing freight rates 25 percent and rail time more than 40 percent.

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We know from experience that intermodal transportation packages can lure business to Florida. About five years ago, in an effort to attract coffee cargo that had always been dropped off at the Port of New York, Miami steamship lines approached the dozen or so major coffee brokers in New York with a proposal for greatly reduced intermodal transportation. They not only offered price cuts on ocean-going freight, but had already negotiated with Florida’s three rail lines -- Florida East Coast, Norfolk Southern and Seaboard Systems -- to bring down the cost of rail shipments for guaranteed volumes of cargo. The bargaining succeeded in rerouting coffee shipments intermodally to the Northeast via the Port of Miami.

That Florida ports can, over the years, become major load centers as well as transshipment ports is clear. We have some capability now, and more efficient, cost-effective rail service puts the goal well in sight. But what would happen, were the state suddenly to impose a 5 percent tax, not only on various services performed at the port of origin, but on the transfer of container units to rail lines? We can only surmise that any competitive advantage built upon intermodal transportation from Florida ports would be wiped out. The thin profit margins true for maritime shippers are true for the transportation industry generally. As an example, the Port of New Orleans has been easily able to lure Caribbean cargo away from Miami with the bait of less than a 1 percent discount on wharfage fees. A 5 percent increase in handling goods, applied at every link in Florida’s intermodal chain, would be a powerful disincentive for any shipper considering docking in the state.

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Transshipment of Cargo

As mentioned earlier, Florida ports have historically been transshipment points: cargo from the Far East or Europe is offloaded in Florida, then transshipped to its final destination in Latin America and the Caribbean.

In a business where competition is keen, however, reputations are engraved in sand. Transshipment opportunities already exist at Panama, the Colon Free Zone, Kingston, San Juan and St. Thomas. As an example, Nordana Lines at one time called in South Florida; now, however, it puts in directly in the Virgin Islands, where European cargo is transshipped to Trinidad, Barbados, Antigua and St. Martin.

What effect would a 5 percent increase in transshipment costs have on Florida maritime commerce? Clearly, the competitive disadvantage that benefits St. Thomas at the expense of Miami would snowball. A few pennies' discount per ton, as our experience indicates, is enough to bring a shipper to Miami; a 5 percent increase would simply drive him away.

Specific Cargo Problems

Certain Florida ports are major import or export points for specific types of cargo. For Jacksonville, it is foreign cars. Pensacola ships rice and grain from the Midwest, and Panama City exports subsidized corn and soybeans as relief cargo to underdeveloped nations. Ft. Pierce and Canaveral handle citrus. How would they fare, were transportation services to be taxed 5 percent?
In the case of Ft. Pierce and nearby Canaveral, their proximity to Florida orange groves makes them natural outlets. The problem here, however, is competition from Brazil citrus growers, who have over the years come to dominate the market with cheaper produce. Florida growers are already operating at a disadvantage. It is not unreasonable to assume that a 5 percent increase in port handling and transportation charges would drive some out of business.

As for Pensacola and Panama City, they are in direct competition with the nearby state-subsidized Port of Mobile, as well as ports in Louisiana, Mississippi and Texas. With little effort, overland shipments of Midwest grain to Florida ports could be diverted to avoid a 5 percent hike in port costs. It should be pointed out that, with Pensacola, what keeps the port cost-competitive with other shipping points is its stevedore charges. According to port officials, imposing a 5 percent sales tax would boost the cost to ship a 25,000-ton cargo load by 60 to 80 cents per ton -- and drive shippers to other Gulf Coast ports.

Jacksonville's situation is especially troublesome. Appreciation in the value of the Japanese yen against the American dollar has forced the port to continually adjust labor charges downward to stay competitive. As the cost of Japanese autos climbs, manufacturers increasingly look to the Port of Brunswick, just 50 miles north and offering lower handling charges because of state subsidy. A 5 percent hike in port service and transportation costs virtually guarantees that automakers will opt for the Georgia port over the Florida one.

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The Ability to Raise Revenue

Ports in South Carolina, Georgia and Louisiana are in the enviable position of not having to show a strong profit to stay in business. Not only do state tax dollars subsidize them, but state government backs their bond issues.

Not so with Florida ports. Their continued financial viability and their ability to retire current debt depend solely on the income they generate. Voters and investors must have confidence in the balance sheets of Florida ports; otherwise, the latters' borrowing capability is diminished. Fortunately, that has so far not been a problem. In fact, fiscal health is a selling point for the Port of Miami -- Dade County voters in November passed a general obligation bond issue, of which $150 million is dedicated to Port capital improvements.

What effect would a sales tax on port services have? Our experience suggests that an unacceptable tax would drive commerce into the waiting arms of non-Florida competitors, further eroding port revenues and further threatening their survival, let alone their ability to expand and improve services. We are mindful that the fallout from a 5 percent sales tax could be great indeed. Last year, for example, the state imposed a 5 percent severance tax on phosphates, making Florida phosphate less competitive with North Carolinian and African product. The result: the Port of Tampa almost immediately lost 50 ship callings to the Port of Wilmington, NC. That bitter experience, multiplied by 11 ports, would drain the state's economy by hundreds of millions of dollars annually. And, because the financial "image" of Florida ports depends strictly on income-generating ability, any loss of revenue is a double-edged sword.

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A Laundry List of Charges

What port services would be taxed, and how much would the tax generate? A hypothetical example would be the taxes imposed on handling a 20-foot-equivalent container load of coffee shipped from Guatemala to Miami, with New York City as the final rail destination. The following average service costs would presumably be taxed at 5 percent:

<table>
<thead>
<tr>
<th>Service Description</th>
<th>Cost</th>
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<tbody>
<tr>
<td>Stevedoring</td>
<td>$150</td>
</tr>
<tr>
<td>U.S. port charge, wharfage, job security program and container royalty fund</td>
<td>$60</td>
</tr>
<tr>
<td>Handling at pier</td>
<td>$300</td>
</tr>
<tr>
<td>Trucking from pier to warehouse</td>
<td>$40</td>
</tr>
<tr>
<td>Stripping/reloading of cargo</td>
<td>$226</td>
</tr>
<tr>
<td>Trucking from warehouse to railyard</td>
<td>$40</td>
</tr>
<tr>
<td>Rail charges from Miami to New York</td>
<td>$878</td>
</tr>
<tr>
<td>Broker documentation fee</td>
<td>$50</td>
</tr>
<tr>
<td>TOTAL CHARGES</td>
<td>$1,744</td>
</tr>
<tr>
<td>Sales Tax at 5 percent</td>
<td>$87.20</td>
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</tbody>
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The $87.20 total tax represents a cost that the shipper can either absorb or, running the risk of losing the coffee grower's business, pass along. The shipper, of course, has a third, far more appealing alternative: he can offload at Savannah, pay discounted charges there, and ship by rail at rates that compete favorably with rail transportation in Florida. If $87 more per load seems modest, remember that the coffee shipper can only expect to make a modest profit anyway. Reduce that, and he will take his cargo elsewhere.

**Florida's Cruise Industry**

The state is host to two-thirds of the world's cruise market, and Miami today is the undisputed cruise capital of the world. How the Port of Miami earned that title has much to do with virtually uninterrupted growth in its ability to accommodate Caribbean-bound passengers. That growth is nothing less than phenomenal. In 1977, 978,000 passengers passed through the Port. When cruise lines, anticipating increased traffic, boosted new building by $1.5 billion in subsequent years, Miami responded with new handling capacity -- and today is home to more than 20 cruise vessels. In 1986, more than 2.5 million cruise passengers passed through its terminals-- an increase of 155 percent in just 10 years' time -- and projections call for 3 million passengers annually by 1990.

While Miami's port underwent expansion, however, a number of Caribbean countries emerged as significant competitors. Jamaica, Barbados, the Virgin Islands and Martinique are working hard to steer cruise ships away from Florida. Puerto Rico, in particular, has become a major threat, having persuaded three of the world's largest cruise lines --

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Carnival, Norwegian Caribbean and Royal Caribbean -- to move ships away from Miami to the Port of San Juan, despite the fact that the lines are all Miami-based. Puerto Rico accomplished this coup in part because it could offer a special incentive: whereas the Port of Miami levies a $7 head tax on cruise traffic, San Juan will charge the same amount but then rebate $4 per capita after the cruise line reaches a certain quota. San Juan can afford such generosity because the port is government-subsidized.

Solid as Miami's reputation may appear to be, it is not proof against tough competition from the Caribbean. Other cruise lines than the three just mentioned are doubtless considering their options at other ports. Florida will only simplify that decision-making if, instead of making its ports more competitive, it slaps a 5 percent sales tax on services to the cruise shipping industry.

Conclusion

The economic consequences for Florida of a 5 percent sales tax on maritime transportation would be onerous. It is not merely a question of lost income. In human terms, thousands of jobs statewide would be jeopardized -- directly in the transportation sector and, through the ripple effect, in related industries. We would lose more money by chasing away business than could possibly be earned from sales tax revenues.

Foreign policy considerations also play a role in whether port services should be taxed. The nation's Caribbean Basin Initiative, begun in 1983, is an effort to assist in diminishing Latin America's debt crisis by improving its balance of trade. Florida is a linchpin in that program, exporting and importing largely to and from the region. It is hoped that Florida ports and ports in the Americas and the Caribbean can become

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equal partners. A healthy economic climate at both ends of the trade route is to everyone's advantage.

That health is imperiled when Florida ports are encumbered by taxes. What we lose, in terms of cargo or passengers, to Caribbean ports ultimately hurts our ability to buy Latin American goods. Momentary gains made by foreign ports are purchased at the expense of their ability to export to the United States.

Trade is a two-way street, and the power to tax, as a U.S. Supreme Court justice once said, is the power to destroy. The question facing the State Legislature in the debate on sunsetting the tax exemption is what services are at greater risk if a sales tax becomes reality. With Florida maritime transportation's already narrow profitability, that risk becomes a sure thing.

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