

REPORT TO CONGRESS ON THE PROGRESS OF THE VESSEL DISPOSAL PROGRAM

January 2008



Maritime Administration James River Reserve Fleet, Virginia



**U. S. Department of Transportation
Maritime Administration**

TABLE OF CONTENTS

| | |
|---|-----------|
| INTRODUCTION | 1 |
| I. MARITIME ADMINISTRATION ACCOMPLISHMENTS AND ACTIVITIES IN FISCAL YEAR 2007 | 1 |
| Overview | 1 |
| New Program Challenge – Aquatic Nuisance Species | 3 |
| AbleUK Contract for Foreign Recycling | 6 |
| Ship Disposal Funding | 7 |
| Ship Disposal Contracts | 8 |
| Transfer of Ships to the Navy for Disposal | 8 |
| Comprehensive Management Plan | 9 |
| Performance Measures | 11 |
| Program Progress in FY 2007 | 13 |
| Vessel Disposal Alternatives | 16 |
| Conclusions | 19 |
| II. PROGRESS OF THE U.S. NAVY’S VESSEL DISPOSAL PROGRAM ... | 22 |
| Introduction | 22 |
| Navy-Titled Obsolete Vessels in the Maritime Administration National Defense Reserve Fleet | 22 |
| Accomplishments Since July 2007 | 22 |
| Domestic Ship Dismantling | 22 |
| Navy Sink Exercises | 22 |
| Artificial Reefing | 23 |
| Remaining Inventory | 23 |
| Navy/Maritime Administration Cooperation | 23 |
| Planned Activities | 23 |
| Navy/Maritime Administration Cooperation | 24 |
| Conclusions | 24 |
| III. APPENDICES | |
| Appendix 1: Figure 1 – Trend of Navy-Titled Obsolete Ships in the MARAD National Defense Reserve Fleet from FY98 to Present | 26 |
| Appendix 2: Table 1 – Navy Titled Obsolete Vessels in the Maritime Administration National Defense Reserve Fleet designated for disposal | 27 |
| Appendix 3: Table 2 – Ship Disposal Project Task Order Status Fiscal Year 2007 | 28 |
| Appendix 4: List of Acronyms | 29 |

Report to Congress on the Progress of the Vessel Disposal Program

INTRODUCTION

This report is submitted pursuant to the following statutory direction:

- The Senate Report [109-109, July 26, 2005] accompanying the Transportation, Treasury, Housing and Urban Development, the Judiciary, the District of Columbia, and Independent Agencies Appropriations Act, 2006, P.L.109-115; 119 Stat. 2396 (2005), which requires periodic reporting on the progress made by the Maritime Administration to dispose of the entire inventory of obsolete ships within the National Defense Reserve Fleet (NDRF). The NDRF consists of three fleet sites; Beaumont Reserve Fleet (BRF), James River Reserve Fleet (JRRF) and Suisun Bay Reserve Fleet (SBRF).
- The National Defense Authorization Act for Fiscal Year 2006, P.L. 109-163, Section 3505(a)(f); 119 Stat. 3552 (2006), which requires periodic reporting by the Secretary of Transportation, in coordination with the Secretary of the Navy, on progress made in implementing plans to dispose of obsolete ships in its programs.

Section I of this consolidated program report summarizes the Maritime Administration's vessel disposal accomplishments in Fiscal Year (FY) 2007 and outlines the vessel disposal outlook and challenges for 2008. A review of the previous reports of the Ship Disposal Program, hereafter referred to as the Program, provides a historical perspective prior to FY 2007. In coordination with the Secretary of the Navy, this Report also includes in Section II the progress of the U.S. Navy's vessel disposal program.

I. MARITIME ADMINISTRATION ACCOMPLISHMENTS AND ACTIVITIES IN FISCAL YEAR 2007

Overview

The Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001, Pub. L. 106-398, § 3502, 114 Stat. 1654A-490 (2000) (the Act), required the disposal by September 30, 2006, of all vessels in the Maritime Administration's NDRF that were not assigned to the Ready Reserve Force or otherwise designated for a specific purpose. In 2001, the Maritime Administration established the Program to accomplish the requirements of the Act. Since the establishment of the Program, the Maritime Administration has aggressively pursued all feasible disposal alternatives including domestic recycling, artificial reefing, deep-sinking, donation, the sale of ships for recycling and reuse, and the potential for foreign recycling. Because of significant capacity limitations within the domestic recycling industry at the time, it became apparent at the start of the Program in 2001 and 2002 that conventional domestic dismantling, as the predominant means of disposal, was not adequate to dispose of

all of the Maritime Administration's non-retention vessels by the September 2006 deadline as required by the Act. The domestic recycling industry continues to have a very limited capacity despite the fact that the Maritime Administration had eight qualified domestic facilities as of the end of FY 2007 to compete for recycling contracts, seven of which have been awarded contracts by the Maritime Administration. To date, the eighth facility has not been competitive from a best-value standpoint. In addition, in October 2007, one qualified facility located in Baltimore, Maryland, ceased operations causing the Maritime Administration to terminate six recycling contracts at the facility and to reprocure recycling services with other qualified facilities. Further, another qualified facility located in Louisiana was precluded, for the majority of FY 2007, from receiving other Maritime Administration contracts while that State assessed concerns related to the potential risk of transmitting aquatic invasive species from biological growth on vessel hulls. On December 13, 2007, the State of Louisiana agreed to accept vessels from the BRF after vessel hulls have been cleaned according to the Maritime Administration's protocol. The domestic ship recycling industry is heavily dependent on the supply of the Maritime Administration and Navy ships, thus adequate capacity will be increasingly problematic if budgets for ship disposal are not maintained causing recycling contractors to experience large variations in workloads that result in the lay off of trained and skilled workers.

At this time, because of statutory restrictions in the Toxic Substances Control Act (TSCA) and other environmental regulations, foreign disposal of obsolete vessels is not a commercially practicable option. This is primarily because TSCA prohibits the export of polychlorinated biphenyls (PCBs), and the time consumed to complete the lengthy formal Environmental Protection Agency (EPA) administrative rulemaking process for an exemption to export the Maritime Administration's obsolete vessels containing PCBs above the regulated limit.

From the start of FY 2001 through FY 2007, the Maritime Administration awarded contracts for the disposal of 100 obsolete ships, removed 92 ships from its fleet sites, and completed disposal action on 75 vessels. While currently there are 108 non-retention ships in the fleets not under contract and awaiting disposal, this figure includes 94 retention ships that have been downgraded since 2001 and added to the disposal queue.

The Maritime Administration first reported to the Congress in 2002 that because of several factors, it was unlikely to meet the statutory deadline. These factors included insufficient domestic capacity; the lack of any active, qualified recycling facilities on the West Coast; the large influx of additional obsolete ships into the program; and the lack of access to foreign recycling. All of these factors have limited the number of ships that can be disposed of annually. Even with the increases since 2003, domestic recycling capacity remains limited in spite of continued robust market demand for ferrous and non-ferrous scrap metal by both domestic and foreign smelters and record high prices in particular for ferrous scrap metals. Access to additional cost-effective capacity, either foreign or domestic, will be necessary for the Maritime Administration to achieve expedited disposition of the remaining vessels in the NDRF inventory, including additional vessels that are added to the disposal inventory annually.

New Program Challenge – Aquatic Nuisance Species

In addition to challenges related to TSCA and PCBs, the Maritime Administration faced a new environmental challenge starting in FY 2006 that had, and will continue to have, significant budget and disposal rate implications for the foreseeable future. The Maritime Administration was notified by the United States Coast Guard (USCG) late in the first quarter of FY 2006 that the Maritime Administration's obsolete ships were required to comply with 33 CFR Part 151, Subpart D (pertaining to aquatic hull growth), which became effective in September 2004 and is the USCG's implementing regulation for the National Invasive Species Act (NISA). While the regulation appears to apply to "operating vessels" only, the USCG's interpretation expanded the definition to include all vessels, including the Maritime Administration's non-retention ships, which are not operational and will only be towed to a recycling facility for disposal. The USCG interpretation is meant to address the potential that the movement of ships for disposal might serve as a vector for transmitting aquatic invasive species within the United States. There has been much disagreement with the USCG interpretation and application of NISA and its regulations to Maritime Administration vessels, while both Coast Guard and Navy vessels are exempt.

In the spring of 2006, the USCG and the Maritime Administration reached an agreement to accomplish in-water hull cleaning (commonly known as scamping) to remove soft aquatic growth prior to the movement of these vessels.

Compliance with the regulations since early FY 2006 has resulted in the Maritime Administration incurring significant additional costs associated with the use of mechanical hull cleaning methods. This interim mitigation action, which was developed into hull cleaning best management practices by the Maritime Administration, was agreed to by the USCG while the Maritime Administration developed a programmatic plan for defining and taking appropriate steps to reduce the potential risk of transferring non-native aquatic species. Because there is little science that defines the risks of transferring aquatic species by hull fouling from one specific geographic location to another, the Maritime Administration has been involved in research to identify potential invasive species on its vessels, risks related to various disposal alternatives, and possible mitigation measures appropriate to identified risks.

The USCG application of this regulation has also delayed the removal of ships from Maritime Administration fleet sites and added significantly to ship disposal costs in FY 2006 and 2007. Mitigation and testing costs to date involving 22 ships have averaged approximately \$122,000 per ship for a total cost of \$2.7 million. The potential exists for even greater costs and disposal delays if research shows that the interim hull cleaning measures currently in effect do not sufficiently reduce the risk of invasive species transfer.

In August 2006, the State of California raised concerns that the in-water cleaning of hulls by the Maritime Administration prior to their tow might release hazardous materials contained in some hull coatings into State waters, and that the practice possibly violated the Clean Water Act (CWA) and might require permitting by California State and/or regional Water

Quality Control Boards (WQCB). The Maritime Administration is still engaged in discussions with the WQCB to determine whether the in-water hull cleaning activities are subject to additional regulatory requirements at the State or local level. In the meantime, no vessels have been removed from the Suisan Bay Reserve Fleet (SBRF) since January 2007.

The situation in California entails a series of conflicting Federal and State laws and regulations with which the Maritime Administration must attempt to comply and which placed the Maritime Administration in the position of negotiating with each State and local jurisdiction in order to continue transporting vessels for recycling. The Federal and State regulations related to hull cleaning requirements, and control of discharges incidental to hull cleaning operations, have added significant costs and delays to the expedited disposal of obsolete ships mandated by Congress.

On February 21, 2007, the Maritime Administrator issued a temporary suspension of any additional movement of non-retention vessels from the NDRF anchorages in California, Texas, and Virginia. This action was precipitated by the concerns of California, the possibility of challenges to disposal activities from other States and the situation of conflicting Federal and State environmental mandates, and constraints on ship disposal activities. The temporary suspension was also put in place to avoid violating the many Federal, State, and local laws that now apply to these vessels due to the USCG's hull cleaning requirement. The suspension was intended to remain in place until agreements were reached with USCG, EPA, and State officials that sufficiently addressed the known and reasonably foreseeable issues such as NISA and the CWA that were impeding the movement and disposal of Maritime Administration obsolete ships. Since the suspension, the Maritime Administration has consulted with the Department of Justice, USCG, the Navy, Office of Management and Budget, and the affected States, to determine which laws are applicable and identify potential legal jeopardy when the program resumes.

States affected include California, Texas, and Virginia where the Maritime Administration's reserve fleets reside and pre-tow hull cleaning activities occur, and the States of Texas, Virginia, Maryland, and Louisiana where qualified recycling facilities are located. Since the suspension, the Maritime Administration has reached agreement with Texas and Virginia with regard to in-water hull cleaning, and agreement with Maryland, Virginia, Louisiana, and Texas to allow vessels that have been cleaned in other geographic locations into their State waters for disposal. The qualified facility in Maryland has since ceased operations.

Status as of the date of this report:

- Virginia has agreed to allow ships to be scamped in the James River Reserve Fleet (JRRF), which is located in Virginia.
- Maryland has agreed to allow ships into its waters for recycling from the State of Virginia if the ship's hulls are cleaned before movement into State waters.
- The State of Texas has agreed to allow ships from the Beaumont Reserve Fleet (BRF) to be towed to Brownsville without scamping; however, in order to further reduce potential risk, the Maritime Administration is scamping those vessels. Texas has also agreed to allow scamping in its waters at the BRF and has agreed to allow ships into

state waters for recycling from all sources, if the ship's hulls are cleaned prior to arriving in State waters.

- Louisiana has agreed to allow Maritime Administration vessels that originate in Texas into its waters after hull cleaning, but has not yet agreed to allow ships from Virginia or California into their waters.
- California has not agreed that the ships can be cleaned in its waters and has indicated such cleaning may constitute a violation of the CWA. The State's current position is that total containment of the solid and liquid scamping discharge is required.

Because of the agreements reached with the States of Virginia, Maryland, Louisiana, and Texas, the Maritime Administrator has partially lifted the disposal suspension to allow the disposal of JRRF and BRF ships at qualified facilities in those States only. Lifting the suspension to allow scamping and disposal of SBRF vessels will come only after additional discussions with California, to resolve concerns about scamping discharge containment.

The Maritime Administration has continued discussions with California, however, those discussions have yet to result in an agreement to allow in-water hull cleaning. The issues involved in the impasse include the potential discharge of hazardous substances from hull coatings during the scamping process and concern for exfoliating paint falling from non-retention ships at the SBRF while awaiting disposal. The State of California originally asked the Maritime Administration to contain some of the particulate discharge during scamping but now wants to require containment of all liquids and solids. There is no known operational in-water hull cleaning technology that can totally contain all liquid and solid discharges.

While drydocking is one of the alternatives the Maritime Administration is exploring, this alternative is limited by several factors. These include: the risk and liability issues associated with drydocking older SBRF ships that are in poorer material condition; the existence of just two operating drydocks in the San Francisco Bay area and the availability and cost of those drydocks to accomplish hull cleaning of lower priority ships that have an acceptable level of risk when drydocking. The Maritime Administration needs the option to use all feasible alternatives, including in-water hull cleaning. California has resisted efforts to consider a proposed demonstration project to test the effectiveness of a solid discharge containment system developed and successfully tested earlier in 2007 by a Maritime Administration contractor.

Complicating the resolution of issues in California is the recent filing of a lawsuit against the Maritime Administration by the Natural Resources Defense Council (NRDC) in California related to the scamping and exfoliating paint issues of the SBRF vessels and the involvement of other agencies in addition to the WQCB, such as the California State Lands Commission from which the Maritime Administration leases the SBRF site.

The Maritime Administration is in the process of developing a new programmatic Environmental Assessment (EA) to supplement and update a programmatic EA prepared in 1997. The Maritime Administration has also engaged a contractor to develop best

management practices (BMPs) for reserve fleet operations which is a part of the Administrator's Environmental Excellence Initiative (EEI). While diligently pursuing a resolution in California, the Maritime Administration is continuing with recycling awards to dispose of the lower priority vessels in the JRRF and BRF. In October, 2007, a qualified East Coast recycler located in Baltimore ceased operations due to financial difficulties. The Maritime Administration successfully reprocurd recycling services for the six ships awarded to that facility; however, the closure of that facility decreases overall domestic recycling capacity and reduces the number of qualified East Coast facilities to one. Despite the closure of the Baltimore facility and the impasse in California, it is anticipated that the non-retention ship award, removal and disposal goals for FY 2008 will be met.

Because of the potential liability faced by the Maritime Administration as custodian of ships owned by other agencies that are moored at Maritime Administration fleet sites on a reimbursable basis, on March 9, 2007, the Maritime Administration notified the Navy, USCG, the National Oceanic and Atmospheric Administration (NOAA), and the Army Corps of Engineers (ACE) that their ships in the Maritime Administration's reimbursable custody would not be released until they had provided documentation showing that the local and State governments of the vessel's destination agree to accept the vessels from those agencies upon satisfaction of NISA requirements. The Maritime Administration authorized release of Navy ships on May 25, 2007, after the Department of the Navy gave written acknowledgement of the potential liabilities that they faced and assumed all responsibility for same.

AbleUK Contract for Foreign Recycling

In FY 2003, the Maritime Administration awarded a contract to export 15 ships (including two vessels to be transferred in a vessel sales agreement) to a qualified facility in the United Kingdom (UK). With four of the ships already in the UK, the Sierra Club and the Basel Action Network sued alleging that the Maritime Administration and EPA had violated TSCA and other environmental statutes. A temporary restraining order was issued with respect to nine of the remaining vessels identified for dismantling in the AbleUK contract. (The four ships towed to the UK in 2003 and two post-1980 built (PCB-free) ships were not subject to the temporary restraining order.) Although this suit was dismissed, the Sierra Club has indicated to the Maritime Administration and EPA that there would be further litigation if the Maritime Administration attempts to export remaining vessels for disposal. The legal challenge in the UK resulted in AbleUK being required to reapply for its local planning permissions/licenses and a Waste Management License for the facility upon gaining the local permissions. A timely approval would have allowed AbleUK to begin work in FY 2006 on the four Maritime Administration ships at its facility and make possible the export of the remaining ships under the contract in 2007.

AbleUK was expected to gain the required local permits in October 2006 with approval by the Hartlepool Borough Council (HBC); however, the HBC refused to approve AbleUK's applications, contrary to the strong, nearly unanimous recommendation for approval by HBC's own planning review committee.

Since the October 2006 vote, discussions with AbleUK and the UK Environmental Agency (UKEA) resulting in a modification to the original contract that will limit the recycling of obsolete ships to only the four ships currently in the UK plus the two unfinished oilers allowed under the original contract. The additional tonnage (approximately equivalent to nine ships) specified in the original contract has been disposed of in domestic facilities. In October 2007, AbleUK successfully reacquired its local planning permits and licenses related to the recycling of obsolete ships at the facility. AbleUK is in the process of reapplying for its national waste management license from the UKEA which would permit the recycling work to begin on the Maritime Administration ships as early as May 2008. The Maritime Administration is available upon request to brief Members of Congress regarding the AbleUK contract.

Ship Disposal Funding

In FY 2007, the program operated under a continuing resolution at FY 2006 funding levels, which included \$18 million for the disposal of obsolete ships and \$3 million for the continued decommissioning process for the nuclear reactor and hazardous materials on board the retention vessel NS SAVANNAH. FY 2008 appropriations included \$12.3 million for ship disposal and \$4.7 million for the NS SAVANNAH.

In spite of the suspension of disposal awards in FY 2007 through June 1, 2007, due to the NISA issues, there have been contract awards for the disposal of 23 obsolete ships in FY 2007. With less emphasis by the Navy on conventional dismantling as a disposal method and an increase in the number of domestic contractors competing for the Maritime Administration's ships, the cost-per-ton disposal rate continued to trend lower throughout FY 2006 and FY 2007, resulting in the award and eventual disposal of more ships than anticipated and at a significantly lower cost-per-ton disposal rate than was projected. Fiscal Year 2007 cost-per-ton calculations included the sale of six ships for recycling.

Despite awarding contracts for a number of vessels that exceeded the targeted goal, there was a significant carryover of non-committed FY 2007 funds into FY 2008 in the amount of approximately \$14 million. A significant factor in the Ship Disposal Program carryover for FY 2007 into FY 2008 was the Administrator's suspension of vessel removals until agreements could be reached with the States in which the Maritime Administration's three fleets reside and the five States where qualified recycling facilities are located. The required agreements centered on in-water hull cleaning process (required by the USCG's ballast water regulations) and approval by the receiving States to allow scamped ships into their waters.

Other factors that contributed to the funding carryover were the continued high market price of scrap steel and strong competition among facilities for recycling work, both of which kept recycling prices relatively low throughout 2007. The suspension resulted in no recycling contracts being awarded for five months from the first week of January 2007 through the first week of June 2007. The carryover into FY 2008 will be absorbed to a large degree by rising fuel prices (which substantially increase tow costs) and increasing costs associated with regulatory compliance activities related to hull cleaning and invasive species mitigation.

Those activities include biological sampling, laboratory analyses, underwater hull cleaning and baseline aquatic species studies at the fleet sites.

It is difficult to predict how or when the issues related to hull cleaning and exfoliating paint in California will be resolved; however, it is probable that costs associated with those resolutions will be significantly greater than the current regulatory compliance costs that are necessary and prerequisite to the removal of obsolete ships from the Maritime Administration's three fleet sites. The funding carry-over may also allow the Maritime Administration to award contracts for additional obsolete ships into FY 2008. A major benefit of the carry-over is that the additional disposal awards into FY 2008 will level out the flow of dismantling work to the industry and thereby allow the industry to keep a level work force employed throughout the year.

Ship Disposal Contracts

Utilizing the Federal Acquisition Regulation (FAR) Test Program for Certain Commercial Items (TPCCI), in January 2005 the Maritime Administration implemented the use of Standing Quotations as the primary procurement method for soliciting ship disposal services. The use of Standing Quotations is a simplified acquisition procedure for the competitive procurement of commercial ship dismantling/recycling services. The Standing Quotation process allows interested vendors to submit quotations and proposals on a continuous basis. Since it is not possible to predict which vessels may have a positive recycling value to contractors (offerors), the Standing Quotation process includes a solicitation for both sales (purchase) offers and fee-for-service offers. Those ships not receiving purchase bids are then considered for fee-for-service contracts. Proposals are evaluated, and those offers determined to be technically acceptable from the pool of standing quotations are considered for award. Based on the evaluation criteria posted in the Request for Quotation, contracts are then awarded for the offers that represent the best value to the Federal Government. The TPCCI which expired on December 31, 2007, was extended by the Congress. The Maritime Administration has posted a phased vessel sales and fee-for-service solicitation that will allow revised prices and contract awards through the TPCCI program for FY 2008.

Transfer of Ships to the Navy for Disposal

The National Defense Authorization Act for Fiscal Year 2006, P.L. 109-163, Section 3505(b); 119 Stat. 3552 (2006) required the Maritime Administration to transfer at least four obsolete ships to the Navy for disposal through its vessel disposal program. A similar requirement to transfer an additional three ships to the Navy in FY 2007 appeared in the John Warner National Defense Authorization Act for Fiscal Year 2007, P.L. 109-364, Section 35040; 120 Stat. 2517 (2006).

The Maritime Administration and the Navy have utilized their 2003 Memorandum of Agreement to transfer vessels to the Navy for use in Navy fleet at-sea, live-fire training exercises, which result in sinking commonly known as the SINKEX program. The Maritime Administration has approved the transfer of 10 vessels to the Navy under the program and

believes that funding each of these transfers is in the best financial interest of the United States. Nine vessels have been transferred to the Navy for use in the Navy Fleet training sink exercises, and one vessel has been transferred to be recycled under the existing Navy recycling contract. Thus far, one vessel (the MAUNA KEA) has been sunk and one vessel (MISSISSINEWA) is in the process of being recycled under a Navy recycling contract.

Prior to passage of the 2006 Department of Defense Authorization Act, the Maritime Administration informed the House Armed Services Committee staff that a transfer of vessels to the Navy for disposal via the Navy's existing recycling contracts provided little economic or convenience advantage to the Maritime Administration. Since the Maritime Administration has more qualified recycling facilities than the Navy, and the two Navy facilities are also Maritime Administration qualified facilities, the use of the Navy's recycling contracts offered the Maritime Administration no additional recycling capacity or competition.

A number of ships were identified by the Maritime Administration to the Navy in 2006 for disposal via the Navy's recycling program. Upon receipt of the quotations of the cost of these services, the Maritime Administration was able to approve one vessel for such disposal. Determinations and findings made pursuant to the Economy Act, which were required under the terms of the Department of Defense Authorization Acts of 2006 and 2007, showed that this one vessel was economically comparable to previous ships awarded by the Maritime Administration and could be disposed of more conveniently through the Navy's program, principally because of the Navy's oversight of the recycling project. With respect to the other vessels offered to the Navy for disposal, given the prices received from the Navy, the Maritime Administration was unable to make the required Economy Act findings that it was more economical to use the Navy's contractual recycling program than to use the Maritime Administration's current procurement program.

Comprehensive Management Plan

The FY 2006 Authorization of Appropriations, Title XXXV, Maritime Administration, P.L. 109-153, Section 3505(a), 119 Stat. 3551 (2006) contained a requirement for the Maritime Administration to develop a Comprehensive Management Plan (CMP) for the disposal of its obsolete ships. The CMP was developed, implemented, and delivered to the Congress in July 2006. The plan addressed the Program's strategy, performance measures, funding, and decision-making framework for vessel disposal in addition to identifying external factors that could affect execution of the plan.

The Maritime Administration's disposal strategy, as discussed in the CMP, continues to be an integrated plan that includes the critical elements considered for both long-term disposal strategy and short-term disposal decisions. Elements that affect the cost and disposal rate of the Maritime Administration's obsolete ships include:

- Capability, capacity, and effectiveness of the various disposal options to cost-effectively expedite the disposal of vessels

- Domestic and international scrap steel markets
- Disposal alternatives available to the Program
- Non-retention vessel condition and location
- Availability of non-retention ships to the Program for disposal
- Suitability of vessels for various disposal options
- Timing, level, and availability of funding
- Environmental considerations for specific vessels
- Ship-specific proposals received by the industry
- Demand for ships to be artificially reefed, purchased, and used in the Navy's fleet training exercises

The Program's emphasis continues to be the expedited disposal of obsolete ships presenting the greatest environmental risk. Reutilization and disposal alternatives such as artificial reefing, donation, use in the Navy Fleet training exercises, and sales are less effective at reducing environment risks because the best candidates for those disposal options are generally vessels that are cleaner and in better condition. The Maritime Administration's responsibility in this area is first and foremost the mitigation of environmental threats posed by older, deteriorated hulls that contain residual oil. While the Maritime Administration's disposal strategy continues to focus on dismantling/recycling as the most expeditious option currently available, all disposal options are continuously being evaluated.

Through the use of full and open competition, the Maritime Administration continues to utilize all feasible disposal options available to achieve an environmentally acceptable end. Maritime Administration goals contained in the Comprehensive Management Plan include:

- Eliminating the backlog of high priority vessels accumulated in the 1990s. This has nearly been accomplished; only four vessels are not currently under contract for disposal.
- Removing from the fleet sites all "high" and "moderate" priority ships at a target rate of 20-24 ships per year. Elimination of the remaining four high and 23 moderate priority ships not currently under contract for disposal mitigates the greatest risks to the environment. The number of vessels removed by each disposal alternative will depend on and be determined by industry proposals and pricing, funding availability, suitability of each ship for the disposal methods available and proposed, the outcome of the foreign recycling legal challenges, the availability of obsolete ships for disposal (i.e., not on hold for historical assessment or for donation), and other factors.
- Maintaining only "low" priority/low-risk ships at the fleet sites. The long-range target number of low priority obsolete vessels to be maintained on an annual basis is a total of no more than 70 at all three fleet sites. With the projected addition of four to five Maritime Administration and Department of Defense non-retention ships per year, an annual reduction rate of 20-24 ships will have to be maintained for 2-3 years

beyond 2008 in order to achieve and maintain an obsolete vessel fleet size at a maximum range of 50-70 ships.

- Having level annual funding that permits the “end state” near-term annual disposal rate of 20-24 ships and then a level of funding in the out years that permits the disposal of at least the number of ships that are designated as obsolete on an annual basis. A failure to achieve an adequate level of funding and to maintain all disposal options will result in an accumulation of obsolete vessels, as occurred in the 1990s.

Critical factors that impact the achievement of a realistic and environmentally responsible disposal “end state” include:

- The availability of foreign recycling as a viable disposal option in 2009 and beyond particularly for West Coast vessels that currently must be towed 5000+ miles to be recycled domestically in Texas.
- Sufficient funding levels in 2008 and beyond to allow consideration of proposals that include economies of scale.
- Designation of a majority of vessels as obsolete in the future that are in “fair” or “good” condition (i.e., low priority vessels with hull conditions rated at #4 & #5).

Performance Measures

The Program’s performance measures of vessels awarded, vessels removed, and vessels disposed of are the best and most direct measure of progress in disposing obsolete ships and meeting the Department’s environmental stewardship targets. Performance measure projections are based on variable factors including, but not limited to, the following:

- Timing of annual appropriations
- Feasibility of disposal methods available to the Program
- Legal challenges to Program initiatives
- The competitiveness, capacity, and production throughput of recycling facilities
- The costs of aquatic nuisance species sampling, assessment, and threat mitigation
- The costs of environmental remediation of hazmat streams present on the obsolete ships
- The market price of recyclable steel

The Department’s ability to meet future performance targets is subject to the same variables. Negative trends in any one or a combination of those variables can significantly affect the attainability of the performance targets. The targets for each year are established during the annual budget request process one and one-half years prior to the specified budget year.

The three performance measures listed below are the major milestones of the vessel disposal cycle. The annual cost-per-ton measure is indicative of the Program's efficiency even though variables that can significantly affect that particular measure, such as the market price of recyclable steel, are beyond the Program's control. The following tables include target and actual results through September 30, 2007 and the targets for FY 2008.

The difference (Δ) between the target and actual results for vessel awards, removals and disposals over the last seven years shows that the goals have been exceeded over the long term in spite of annual goals not being met on a few occasions. The positive differential (Δ) between the targets and actuals is indicative of the Program's overall progress and effectiveness.

Number of contract awards for the removal of obsolete vessels from the National Defense Reserve Fleet sites for subsequent disposal.

| | <u>2001</u> | <u>2002</u> | <u>2003</u> | <u>2004</u> | <u>2005</u> | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>Totals (thru 2006)</u> |
|----------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|---------------------------|
| Target: | 3 | 3 | 11 | 14 | 15 | 13 | 13 | 12 | 72 |
| Actual: | 6 | 2 | 15 | 13 | 20 | 21 | 23 | | 100 (Δ +28) |

Number of obsolete vessels removed from the National Defense Reserve Fleet sites for subsequent disposal.

| | <u>2001</u> | <u>2002</u> | <u>2003</u> | <u>2004</u> | <u>2005</u> | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>Totals (thru 2007)</u> |
|----------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|---------------------------|
| Target: | 3 | 3 | 4 | 4 | 15 | 13 | 13 | 16 | 55 |
| Actual: | 6 | 6 | 2 | 15 | 18 | 25 | 20 | | 92 (Δ +37) |

Number of obsolete vessels disposed of (i.e., disposal action completed) from the National Defense Reserve Fleet sites.

| | <u>2001</u> | <u>2002</u> | <u>2003</u> | <u>2004</u> | <u>2005</u> | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>Totals (thru 2007)</u> |
|----------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|---------------------------|
| Target: | 3 | 3 | 4 | 4 | 15 | 15 | 15 | 16 | 60 |
| Actual: | 4 | 9 | 3 | 6 | 13 | 20 | 20 | | 75 (Δ +15) |

The following table shows the disposal achievements for FY 2007. The FY 2007 awards, removals, and disposals exceeded the program's goals.

| FY 2007 Maritime Administration Ship Disposal Goals/Progress | | | |
|---|-------------|---------------|-----------------|
| | <u>Goal</u> | <u>Actual</u> | <u>Variance</u> |
| Ships Awarded Disposal Contracts | 13 | 23 | +10 |
| Ships Removed from MARAD Fleets | 13 | 20 | +7 |
| Ships Disposed (Disposal Completed) | 15 | 20 | +5 |

The table below is a breakdown by Fiscal Year, indicating the average cost-per-ton for disposal actions for Fiscal Years 2001 through 2008 based on the value of contract awards. The figure for Fiscal Year 2008 is a projection. Disposal actions include vessel sales, legislated sales, legislated donations, artificial reefing, deep-sinking, and dismantlement service contracts. The actual cost-per-ton figures for FY 2005 and FY 2006 includes SBRF vessels that were awarded to facilities in Texas because of a lack of qualified West Coast facilities. The cost-per-ton of those vessels elevated the overall cost-per-ton average for FY 2005 and FY 2006, with costs associated with West Coast vessel awards ranging \$0.6 to \$1.0 million higher than JRRF or BRF vessels.

The award of West Coast ships to Texas facilities includes a significant cost premium for the 5000+ mile tow, which includes a transit of the Panama Canal. As a point of comparison, the tow distance of 5000 nautical miles from the SBRF in California to Texas significantly exceeds the 3000+ nautical mile distance from the JRRF to the AbleUK facility in the UK. Notwithstanding the premium paid to dispose of the SBRF ships domestically, the overall Program cost-per-ton has decreased from FY 2004 to FY 2007. The cost decrease during this period is a result of rising scrap market steel prices and strong domestic competition that did not exist prior to 2004. The disposal cost per ton for the 23 vessels awarded in FY 2007 is \$79, which includes the sale of seven vessels. Fiscal Year 2008 costs per ton are anticipated to be comparable to FY 2007. The figures include all costs associated with vessel tow preparations, towing, NISA compliance, hazardous material remediation, and disposal.

| Annual Program Cost/Ton Based on Disposal Actions Awarded in the Fiscal Year | | | | | | | | |
|---|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| | FY '01 | FY '02 | FY '03 | FY '04 | FY '05 | FY '06 | FY '07 | FY '08 |
| Number of Ships | 6 | 2 | 15 | 13 | 20 | 21 | 23 | 12 |
| Target Avg. Cost/Ton | (\$250) | (\$250) | (\$200) | (\$150) | (\$175) | (\$200) | (\$200) | (\$170) |
| Actual Cost/Ton | (\$253) | (\$127) | (\$188) | (\$106) | (\$106) | (\$83) | (\$79) | |

Program Progress in FY 2007

The program tracks three performance measures for the disposal of each vessel. These performance measures are vessels awarded, vessels removed from the fleets, and vessels disposed. The three performance measurements are not confined to a specific time frame or fiscal year. Often vessel disposal projects can span 1, 2, or even 3 fiscal years. Table 1 indicates the date (bolded) for which one, two, or all three performance measures occurred in FY 2007. Program actions resulting in measurable performance on dozens of ships in a single year represent significant progress in the disposal of obsolete ships and the mitigation of any environmental risks presented by those ships. All FY 2007 contracts awarded have been to domestic recycling facilities or to coastal States for artificial reefing, with the exception of three vessels sold in Japan for re-use.

The Maritime Administration's accomplishments in FY 2007 were a result of executing its CMP to continue the removal of the highest priority ships in all three reserve fleet sites. With award of the vessels shown in Table 1, only four high priority ships remain in the Maritime Administration's three fleet sites. Two of the four have recently become available for disposal. Previously they were being held for donation to non-profit organizations or being assessed for historical significance. Of the four remaining high priority vessels, one is located in the JRRF in Virginia and three are located in the SBRF in California. As the high priority vessels become available for disposal they will be given priority for disposal; however, in the meantime the Maritime Administration's comprehensive plan is focused on the 23 moderate priority vessels that are not yet under contract for disposal, which includes 19 moored in the SBRF, one moored in the BRF, and the three moored in the JRRF. The Maritime Administration's plan is to expedite the disposal of these ships to mitigate any potential for increased risk to the environment. Unfortunately, the current suspension of disposal activities for SBRF ships precludes the timely removal of those ships.

The rate of vessels awarded and removed has been negatively impacted by the disposal suspension imposed by the Maritime Administrator pending resolution of conflicting Federal and State environmental mandates and regulations related to NISA and the CWA.

The Maritime Administration is working to identify cost-effective, qualified facilities on the U.S. West Coast that are interested in recycling the obsolete vessels located in the SBRF. A few foreign facilities have submitted cost-effective proposals for disposal of a large number of ships. The Maritime Administration's challenge is to ensure cooperation with the EPA, that the facilities have the capability of dismantling ships in a manner that protects the environment and worker safety and health. There are currently no operational West Coast facilities dedicated to vessel dismantling/recycling available to the Navy or the Maritime Administration. The absence of both a foreign recycling outlet and a West Coast recycling facility will continue to have a significant effect on the disposal cost and rate for SBRF vessels.

The Maritime Administration has pre-qualified a West Coast contractor that would establish a dismantling facility in Vallejo, California if awarded a contract. However, in the past this company has submitted higher bid prices than Brownsville, Texas, companies, even with the significant cost differential advantage associated with the Brownsville companies towing the ships from the West Coast through the Panama Canal. Thus, the cost of domestically dismantling recycling is inherently more expensive for ships located at the SBRF than for ships located at either the JRRF or BRF. The Maritime Administration has mitigated this impact to a small extent by arranging with the Navy to environmentally prepare ships from Suisun Bay, on a reimbursable basis, for use in the Navy fleet training exercises. The Navy works with the active Navy fleet to use the ships as targets during fleet exercises and removes the ships via tow, prior to sinking the ships. Unfortunately, demand for the ships in training exercises has diminished significantly over the past two years.

Table 1: MARAD FY 2007 Disposal Actions
(Bolded dates indicate FY 2007 disposal actions)

| Ship | Fleet | Contractor | Site | Vessel Award | Vessel Removal | Vessel Disposal | Final Amount (\$) |
|------------------|-------|-------------------------|-------|-----------------|-----------------|-----------------|-------------------|
| PAWCATUCK | JRRF | Bay Bridge Enterprise | VA | 8/26/05 | 10/19/05 | 10/7/06 | (\$569,373) |
| MONTICELLO | SBRF | Navy SINKEX** | CA | 9/9/05 | TBD | TBD | (\$915,548) |
| PYRO | SBRF | Navy SINKEX** | CA | 9/9/05 | TBD | TBD | (\$754,549) |
| MAGALLANES | BRF | All Star Metals, Inc. | TX | 11/14/05 | 1/6/06 | 10/13/06 | \$25,286 |
| POINT LOMA | SBRF | Marine Metals, Inc. | TX | 12/15/05 | 2/14/06 | 10/27/06 | (\$897,792) |
| FLORENCE | SBRF | All Star Metals, Inc. | TX | 12/28/05 | 2/15/06 | 1/10/07 | (\$996,992) |
| GILMORE | JRRF | Bay Bridge Enterprises | VA | 2/10/06 | 3/30/06 | 4/26/07 | (\$742,675) |
| PRIVATE MURPHY | BRF | Esco Marine, Inc. | TX | 2/23/06 | 4/11/06 | 2/16/07 | \$5,550 |
| BEAUJOLAIS | BRF | Esco Marine, Inc. | TX | 3/14/06 | 4/27/06 | 12/15/06 | (\$1,047,137) |
| ALLISON LYKES | BRF | S. Scrap Material Co. | LA | 5/30/06 | 7/8/06 | In Progress | \$50,000 |
| MALLORY LYKES | BRF | S. Scrap Material Co. | LA | 5/30/06 | 7/1/06 | 8/9/07 | \$50,000 |
| PRIDE II | BRF | All Star Metals, Inc. | TX | 6/2/06 | 8/8/06 | 6/7/07 | (\$591,584) |
| SAUGATUCK | JRRF | Bay Bridge Enterprises | VA | 6/2/06 | 7/18/06 | In Progress | (\$549,999) |
| BRINTON LYKES | BRF | Marine Metals, Inc. | TX | 6/2/06 | 7/13/06 | 5/23/07 | (\$555,212) |
| ORION | JRRF | N. Amer. Ship Recycling | MD | 6/2/06 | 7/27/06 | 7/27/07 | (\$734,230) |
| HANNIBAL VICTORY | SBRF | Marine Metals, Inc. | TX | 6/2/06 | 8/8/06 | 6/18/07 | (\$978,698) |
| BARNARD VICTORY | SBRF | All Star Metals, Inc. | TX | 6/2/06 | 7/10/06 | 4/17/07 | (\$1,442,804) |
| OCCIDENTAL V. | SBRF | All Star Metals, Inc. | TX | 6/2/06 | 10/5/06 | 8/1/07 | (\$1,191,987) |
| SIOUX FALLS V. | SBRF | Marine Metals, Inc. | TX | 6/2/06 | 8/2/06 | 8/27/07 | (\$978,698) |
| FLORIKAN | SBRF | Navy SINKEX** | CA | 9/8/06 | TBD | TBD | (\$396,984) |
| CLAMP | SBRF | Navy SINKEX** | CA | 9/8/06 | TBD | TBD | (\$363,484) |
| RECLAIMER | SBRF | Navy SINKEX** | CA | 9/8/06 | TBD | TBD | (\$363,484) |
| MISSISSINEWA | JRRF | Navy IDIQ (ISL)** | TX | 9/19/06 | 1/30/07 | In Progress | (\$.02) |
| TEXAS CLIPPER I | BRF | State of Texas (ESCO) | TX | 10/3/06 | 11/3/06 | In Progress | (\$1,500,000) |
| MAUMEE | BRF | Esco Marine, Inc. | TX | 11/3/06 | 1/23/07 | 6/22/07 | (\$405,726) |
| VULCAN | JRRF | Bay Bridge Enterprise | VA | 11/3/06 | 12/19/06 | In Progress | (\$494,000) |
| MARYLAND | BRF | Esco Marine, Inc. | TX | 11/3/06 | 2/1/07 | 8/27/07 | (\$400,000) |
| JASON | SBRF | Marine Metals, Inc. | TX | 11/9/06 | 1/15/07 | In Progress | (\$1,426,035) |
| QUEENS VICTORY | SBRF | Esco Marine, Inc. | TX | 11/9/06 | 12/31/06 | In Progress | (\$1,180,000) |
| LEXINGTON | BRF | S. Scrap Material Co. | LA | 11/14/06 | 1/10/07 | In Progress | \$1 |
| NODAWAY | Japan | (Re-use Sale) | Japan | 12/15/06 | 12/15/06 | 12/15/06 | \$308,333 |
| ALATNA | Japan | (Re-use Sale) | Japan | 12/15/06 | 12/15/06 | 12/15/06 | \$308,333 |
| CHATTAHOOCHEE | Japan | (Re-use Sale) | Japan | 12/15/06 | 12/15/06 | 12/15/06 | \$308,333 |
| PENN. TRADER | BRF | S. Scrap Material Co. | LA | 1/5/07 | 1/30/07 | In Progress | \$1 |
| HUNLEY | JRRF | S. Scrap Material Co. | LA | 1/5/07 | 3/7/07 | In Progress | \$1,500 |
| VANDENBERG | JRRF | State of FL (Colonna's) | FL | 1/26/07 | 3/30/07 | In Progress | (\$1,250,000) |
| CAPE CLEAR | JRRF | Esco Marine, Inc. | TX | 6/12/07 | 7/12/07 | In Progress | (\$537,726) |
| STATE | JRRF | Bay Bridge Enterprises | VA | 6/12/07 | 7/18/07 | In Progress | (\$851,194) |
| HOIST | JRRF | Bay Bridge Enterprises | MD | 7/17/07 | 8/29/07 | In Progress | (\$95,000) |
| LAKE | JRRF | All Star Metals, Inc. | TX | 7/31/07 | 8/16/07 | In Progress | (\$454,690) |
| SPHINX | JRRF | Bay Bridge Enterprises | MD | 8/7/07 | 8/29/07 | In Progress | (\$695,000) |
| SOUTHERN CROSS | JRRF | Esco Marine, Inc. | MD | 8/24/07 | TBD | TBD | (\$690,729) |
| CAPE CHARLES | JRRF | Marine Metals, Inc. | MD | 8/24/07 | TBD | TBD | (\$488,965) |
| SCAN | JRRF | Marine Metals, Inc. | MD | 8/24/07 | TBD | TBD | (\$479,678) |
| PRIDE | JRRF | Marine Metals, Inc. | MD | 8/24/07 | TBD | TBD | (\$468,609) |
| DUTTON | BRF | All Star Metals, Inc. | TX | 9/4/07 | TBD | TBD | (\$1,078,294) |

** -Vessels identified to the Navy Inactive Ships Program Office per FY 2006 & 2007 Nat'l Defense Authorization Act transfer requirement.

Bolded dates indicate disposal actions completed in FY 2007

Vessel Disposal Alternatives

Domestic Recycling and Contractor Performance – The current high value of scrap metals, among other factors, is reducing the per ton domestic recycling costs, allowing the Maritime Administration to contract for additional ships to be dismantled. To date, domestic recycling is the most expedient of disposal alternative compared to transfer of ships for use in Navy sink exercises, artificial reefing, or ship donation. With the increase in scrap metal commodity prices, the Maritime Administration has seen an increase in the number of domestic companies it has pre-qualified for dismantling services since 2004.

In FY 2001, the Maritime Administration contracts involved only three domestic companies. Since then, four additional domestic companies have been awarded ship dismantling contracts, two of which are located on the East Coast. However, the state of the domestic industry is uncertain due to the closing in 2007 of one of the two East Coast facilities and concerns by the State of Louisiana related to invasive species that precluded the award of recycling contracts to a qualified facility located in New Orleans for the majority of 2007. To date, a facility located in California has not been competitive from a best-value standpoint.

In FY 2001, six ships were disposed of domestically through contract awards to three different facilities. The final unit costs were approximately \$253 per ton. In FY 2003, the AbleUK contract involved the export of 13 ships at a unit cost of \$144 per ton; with the barter provision for title to two additional obsolete ships, the total disposal unit cost for the 15 ships was \$104 per ton. Since FY 2003, the per ton disposal cost has continued to decrease, down to \$79 in FY 2007, which included the sale of seven ships for recycling. The decrease in per ton costs since FY 2001 is attributable to a combination of factors, including the increased competition represented by foreign proposals and domestic contractors, and an increase in the international market price of recyclable steel. While the decrease in per ton costs is encouraging, the significant capacity limitations of the domestic disposal industry show little potential for increases in the annual disposal rate of ships.

Further, even at award rates that are lower than the industry's potential capacity, the throughput limitations of many domestic facilities often result in significant post-award delays by contractor in removing the vessels from the fleets and commencing dismantling work. This is particularly true when multiple ships are awarded at the same time to the same facility. It is also not uncommon for domestic facilities to request significant schedule extensions for completing the work beyond the original contract performance period, only a portion of which can be defined as excusable delays. Over the past two years, the majority of the Maritime Administration's qualified domestic facilities have had significant production throughput problems, significantly delaying completion of recycling projects awarded by the Maritime Administration.

While timely performance of many of the contractors in the limited domestic vessel disposal industry is at times a challenge to the Program, it has been considered manageable because of the direct, hands-on project/contract management and on-site facility oversight applied by the

Maritime Administration. However, an area of concern is the additional pressure that may be placed on domestic industrial capacity as a result of the number of vessel disposal awards made by the Maritime Administration and Navy disposal programs. However, this concern may lessen overtime as the Navy expects to decrease the number of ships scheduled to be recycled due to decreasing inventory of non-retention ships.

The Navy's program currently awards recycling contracts to only two domestic facilities, which is sufficient to meet its reduced projected dismantling rate, which is fewer than five ships per year. The two Navy contractors are also qualified contractors under the Maritime Administration's program and are considered the two domestic facilities with the greatest current capacity. One of the two contractors has several on-going Maritime Administration disposal contracts in addition to Navy work, and the other currently has only Navy recycling projects. The combined effect of the Navy and Maritime Administration awards to these two contractors has the potential to exceed the capacity for FY 2008, barring some unforeseen increase in those facilities' resources and production throughput. In fact, because of the backlog of work, one of the two contractors has not been active in pursuing Maritime Administration awards for most of FY 2007 and has indicated to the Maritime Administration that it may not be able to respond to the Maritime Administration's solicitations into FY 2008.

While the Maritime Administration has aggressively pursued the participation of domestic facilities in the recycling of the Maritime Administration ships, and is encouraged with the increase from three to eight in the number of qualified facilities since 2003, there is a note of caution moving forward because of the sharing of limited industrial facilities between the Maritime Administration and the Navy. The capacity, resources, and management of domestic contractors will be tested given the significant number of disposal awards scheduled for completion in FY 2008 and in light of the number of vessel awards anticipated for 2008 by both Programs. Inflated capacity claims by the domestic industry in the past, which have not materialized, will also be tested. Increasing schedule overruns by dismantling contractors are anticipated to continue in FY 2008 as the limits of domestic capacity and capability are reached.

Foreign Recycling - The best value contract award in 2003 was to a qualified UK facility and included 15 ships. The contract was recently renegotiated and is still considered feasible, because the company has been successful in obtaining the necessary local operating and environmental permits. The company is now working to acquire the national Waste Management License (WML) required for its facility. The four vessels exported as part of the original contract are unable to be dismantled until the WML is issued which is expected in May 2008. The Maritime Administration has renegotiated the contract to include only the four ships awaiting dismantling in the UK plus two unfinished oilers. The other nine ships included in the original contract have not been included in the recently renegotiated contract.

The Maritime Administration has put a hold on accepting new proposals for foreign recycling; however, foreign proposals previously submitted are being evaluated. The Maritime Administration is currently in the iterative process of evaluating foreign recycling

proposals involving two countries other than the UK. The effective loss of vessel export as a disposal option has prevented the Maritime Administration from taking advantage of very cost-effective proposals, including some that are revenue-producing to the government. These options would be especially valuable for the Maritime Administration's vessels on the West Coast where there is only one provisionally-qualified facility for vessel disposal, which thus far has not successfully won a competitive procurement.

Artificial Reefing - Reefing has potential that is currently constrained by limited demand for ships by the coastal States. The limited demand is a result of a general reluctance of States to be responsible for the preparation, tow, and sinking of the ships, and to share in the significant costs associated with reefing activities. In FY 2006, the Maritime Administration was granted a legislative change that provides the flexibility to determine the time and place of vessel transfer to a coastal State. This change will allow the Maritime Administration to take an active role and share more responsibilities for preparing a ship for reefing, if it is determined to be in the best interest of the government. Cost-sharing with the States also has the potential to increase demand to some degree. The Maritime Administration has the authority to provide financial assistance to the States and will consider such requests if they are comparable to the costs of other feasible disposal methods. However, the Maritime Administration will consider providing significant financial assistance to States only for vessels considered to be of a higher disposal priority. Unfortunately, the fact remains that higher priority ships, generally, are not good reefing candidates.

Best Management Practices (BMP) for the preparation of ships to be used as artificial reefs have been developed through the interagency efforts of the Maritime Administration, EPA, Navy, National Oceanic and Atmospheric Administration (NOAA), USCG, ACE, and National Marine Fisheries Service (NMFS). The BMPs were implemented in FY 2006 and will provide consistent vessel preparation guidance nationwide. However, the requirements in the BMPs to remove all solid PCBs above the regulated limits or apply for a risk-based approval to dispose of PCBs in a marine environment for purposes of creating an artificial reef could negate potential cost advantages of artificial reefing compared to conventional dismantling.

The vessels TEXAS CLIPPER I and VANDENBERG have been transferred to Texas and Florida, respectively, for reefing preparations. The TEXAS CLIPPER I was sunk as a reef in November 2007. The VANDENBERG is scheduled to be sunk in the summer of 2008. In addition, the Maritime Administration currently has one additional ship in the approval process for use as an artificial reef in the Cayman Islands.

Vessel Sales - This is a low-revenue to no-cost option to the Government for selected vessels. Prior to 2006 the sale of vessels was not a significant disposal option in terms of numbers of ships. In FY 2006, an increase in domestic vessel purchases resulted from the increased market price of steel and "sales of opportunity" for the companies purchasing the vessels. In spite of the sale of five vessels in FY 2006 and six additional vessels in FY 2007, it is not likely that the sale of obsolete ships is a trend that can be relied upon for a significant number of disposals on an annual basis. The six vessels sold in FY 2007 include the sale for re-use

of three obsolete vessels deployed in Japan that were recently downgraded and that would have otherwise been returned to the United States for disposal at significant expense.

It is not surprising that, given the large demand for scrap metal on the international markets, the Maritime Administration continues to receive numerous inquiries for the sale of its obsolete vessels to foreign ship recyclers. However, because of the restrictions that TSCA imposes on the export of Maritime Administration ships that contain regulated levels of PCB's, foreign sales for recycling currently are not commercially practicable in the present legal environment, even to environmentally sound facilities.

Vessel Donation - Donation of vessels is based on the demand of non-profit historical preservationist and humanitarian groups. Historically, donation has not been a significant disposal option in terms of numbers of vessels; however, the Maritime Administration has established a formal donation program to support the efforts of legitimate not-for-profit groups to acquire and preserve vessels. The formal program replaces the previous practice where organizations obtained special legislation for the donation of ships. The authorization for the formal program is contained in Section 3512 of Pub. L. 108-136, the National Defense Authorization Act for Fiscal Year 2004.

Navy Fleet Training Exercise - This joint Navy and Maritime Administration project meets the Fleet requirement for target vessels in Navy at-sea live-fire training exercises. Deep-sinking is a low-volume option with costs comparable to artificial reefing. Vessels are prepared for sinking by the Navy in accordance with procedures that protect the environment as set out in 40 CFR 229.2. The Maritime Administration and the Navy executed a Memorandum of Agreement on September 5, 2003, for disposal of the Maritime Administration ships through the Navy's program. Pursuant to this agreement, the vessel GAGE has been prepared by the Navy; however, the sinking of this vessel has been postponed due to recent donation interest in the vessel. Three ships were prepared for the Navy fleet training exercise in FY 2005 and one was sunk. Four ships were also approved by the Maritime Administration for the Navy fleet training exercise in FY 2006. Those four ships were prepared for sinking by the Navy and are now awaiting to be scheduled for a sink exercise. The feasibility of the Navy fleet training exercise as a future disposal option will depend on cost estimates from the Navy that are comparable in cost to the Maritime Administration's other disposal alternatives. A sink exercise disposal rate of two to three ships per year is considered possible.

Conclusions

This report outlines the significant legal challenges affecting domestic and foreign resources for disposing obsolete ships in the inventory of the Maritime Administration. Nonetheless, an aggressive program of maximizing the use of disposal funding and pursuing all feasible disposal options resulted in the award of 77 contracts to dispose of obsolete vessels in the last 4 years. Those awards and the subsequent removal of vessels from the fleet sites reversed a trend in the growth of the number of obsolete ships in the Maritime Administration's custody.

The progress and momentum gained since FY 2003 needs to be sustained to achieve the goals identified by the Administration and the Congress. The award and removal of the majority of the Maritime Administration's high priority ships since the start of the Program in 2001 have significantly mitigated the threat of residual oil discharge into the environment. Section 3502 of the National Maritime Heritage Act (P.L. 106-398, signed October 30, 2000), which extended the congressional disposal mandate to September 30, 2006, also listed 39 obsolete ships that posed the most immediate threat to the environment. Of the 39 ships identified in 2000 as high priority, only one ship has not yet been removed from the Maritime Administration's fleets. That ship will be removed from the SBRF as soon as the disposal suspension has been lifted for obsolete Maritime Administration ships in California.

These successes notwithstanding, the statutory disposal deadline of September 30, 2006, for all of the Maritime Administration's obsolete ships, was not met. However, as the Maritime Administration first reported to the Congress in 2002, it was unlikely that the Maritime Administration would be able to dispose of the more than 120 obsolete ships by the deadline, due to external impediments that did not allow access to all cost-effective disposal methods and the lack of sufficient domestic competitive vessel disposal capacity. Those constraints still exist today, despite the increase in qualified domestic disposal facilities from three to seven. Moreover, the legal challenges to vessel export that the Maritime Administration encountered in 2003 on the AbleUK disposal contract have effectively negated as a vessel disposal option the export of vessels containing solid PCBs. In addition, the lengthy TSCA formal rulemaking process has significantly delayed near-term prospects for awarding foreign contracts based on cost-effective export proposals previously submitted to the Maritime Administration.

Regardless of the ultimate outcome of the AbleUK contract, it has become clear to the Maritime Administration that, under existing environmental laws and regulations, the export of ships for recycling is currently not a practicable method of disposal for the Maritime Administration or for recycling companies interested in foreign recycling. Given the legal requirements imposed by TSCA that must be met before any foreign vessel disposal can take place, the Maritime Administration is restricted to using domestic recycling facilities as the only option for expedited disposal. A favorable March 2, 2005, ruling by the U.S. District Court for the District of Columbia did not provide the Maritime Administration with relief from the requirements of TSCA. While the Court concluded that the environmental assessment prepared by the Maritime Administration fully met its obligations under the National Environmental Protection Act (NEPA) and dismissed the plaintiff's complaint, the court's ruling does not remedy the underlying environmental issues under TSCA that triggered the legal action initially.

While the various vessel disposal methodologies present many difficult challenges, all such alternatives are needed for a cost-effective, long-term, responsible and safe vessel disposal program. Without access to additional disposal alternatives, the rate of disposal is unlikely to increase beyond the current rate and the cost associated with vessel disposal is unlikely to decrease beyond current levels.

Exfoliating paint is one of many reasons that the Maritime Administration has focused vessel disposal efforts on removing the worst vessels from its fleet sites first. The Maritime Administration continues to believe that removing the ships is the most effective method for addressing all environmental risks posed by the obsolete vessels in the fleets. However, because of the ongoing challenges with NISA and the CWA that have delayed the removal of obsolete vessels, the Maritime Administration is now faced with longer-term management of the vessels. As such, this year the Maritime Administrator established the EEI to review the Agency's fleet practices in the context of long-term management. The EEI includes refining procedures for accepting vessels into the fleets, identifying and evaluating environmental risks associated with long-term management of vessels (including exfoliating paint), and development or adjustment of management practice to reduce environmental risks further. The sampling of the paint is one step in that process.

The Maritime Administration will continue to investigate all alternatives identified in this report, and any others that are identified, to expedite the disposal of its obsolete vessels at qualified facilities and at the least cost to the Government, while giving consideration to worker safety and the environment, as required by the Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001 P.L. 106-398, Section 3502; 114 Stat. 1654A-490.

PROGRESS OF THE U.S. NAVY'S VESSEL DISPOSAL PROGRAM

Introduction

The Navy portion of this report is submitted pursuant to the National Defense Authorization Act for Fiscal Year 2006, P.L. 109-163; Section 3505(a)(f), 119 Stat, 3552 (2006), which requires periodic reporting by the Secretary of Transportation, in coordination with the Secretary of the Navy, on progress made in implementing plans to dispose of obsolete ships in programs.

Navy-Titled Obsolete Vessels in the Maritime Administration National Defense Reserve Fleet

Since Fiscal Year 1998 the Navy has reduced the number of ships in the Maritime Administration facilities by eighty three (83) percent as shown in Appendix 1, Figure 1. As of October 31, 2007, the total number of Navy-titled vessels that are designated for disposal and that are remaining in the Maritime Administration National Defense Reserve Fleet (NDRF) facilities are nine (9) ships and two (2) service craft. Table 1 provides information regarding the method of disposal and projected cost of these vessels.

Accomplishments since July 2007

Domestic Ship Dismantling

The Navy continues to execute its strategy of utilizing multiple vessel disposal methodologies to reduce the size of the inactive ship inventory, including foreign military sales, ship donations, experimental/target use, and domestic ship dismantling. In addition, 10 U.S.C. 7306b provides authority for the Navy to transfer vessels stricken from the Naval Vessel Register directly to a State, Commonwealth, and possession of the United States, municipal corporation, or political subdivision for use as an artificial reef.

Since July 2007, five (5) additional ships have been completely dismantled and recycled under the Navy's Ship Disposal Project contracts. During Fiscal Year 2007, a Request for Proposal was released for two (2) ships that will be contracted in Fiscal Year 2008. All task orders are firm-fixed price, were competed between two (2) contractors, and are administered by Navy Supervisor of Shipbuilding, Conversion and Repair USN (SUPSHIP) Bath, ME. Table 2 identifies the status of FY 2007 task orders under the new Ship Disposal Project contracts awarded in FY 2005. This program enables the Navy to continue reducing its inventory of stricken ships, as expected in Senate Armed Services Committee report 107-62 of 12 Sep 01, while ensuring that ship dismantling will be completed in a timely and cost effective manner, and remaining in compliance with all environmental and occupational safety laws and regulations.

Navy Sink Exercises

Since July 2007, two (2) additional ships¹ have been environmentally prepared and sunk during Fleet at-sea live-fire training exercises in water depths of at least 6,000 feet and at least 50 miles from land, in accordance with Title 40 Code of Federal Regulations Section 229.2.

¹ Inactive ships sunk during Fleet at-sea live-fire training exercises since July 2007 include ex-KNOX (FF 1052) and ex-JOUETT (CG 29).

Artificial Reefing

The ex-FORRESTAL is currently being prepared for reefing in accordance with EPA document *Best Management Practices for Preparing Vessels for Use as Artificial Reefs*, and based on lessons learned from the ex-ORISKANY project. The Navy has created a comprehensive sampling plan that was used to sample the ship for Polychlorinated Biphenyls (PCBs). This plan was released to Environmental Protection Agency (EPA) Region I via Naval Station Newport, RI where the vessel is currently located.

Remaining Inventory

As of October 31, 2007, the Navy's inventory of inactive conventionally powered ships totaled 57, including 12 retention assets for possible future reactivation, 6 logistic support assets held for extended Fleet stripping, and 39 ships designated for disposal by Foreign Military Sales transfer, ship donation for public display, domestic dismantling, or artificial reefing.

Navy/Maritime Administration Cooperation

The Navy and Maritime Administration are also engaging in cooperative strategies addressing their respective inactive ship inventories and are meeting at regular intervals to share lessons learned on vessel disposal programs. Ongoing initiatives include:

- The Navy and Maritime Administration executed a Memorandum of Agreement (MOA) in 2003 that supports the Maritime Administration with on-site contract surveillance where the Navy and Maritime Administration both have ship dismantling contracts in place with the same contractor.
- Since July 2007, no Maritime Administration ships have been sunk under our turn-key Memorandum of Agreement of 2003 to utilize Maritime Administration ships for Navy training exercises.
- Navy and the Maritime Administration executed a Memorandum of Agreement (MOA) in 2003 where which ex-Navy vessels are transferred from the Maritime Administration to the Navy for disposal under current Navy Ship Dismantling IDIQ contracts. This MOA can be used in implementation of requirements of Section 3505 of the FY06 National Defense Authorization Act for fiscal year 2007. The ex-MISSISSINEWA (AO 144) was awarded in September 2007 under the Navy contract to International Shipbreaking Ltd., in Brownsville, TX, under terms of this MOA. Dismantling is approximately 65 percent complete with a completion date of March 2008.

Planned Activities

Domestic Ship Dismantling

In first the quarter of FY08, the Navy plans to sign two contracts to recycle two additional ships under its IDIQ contracts for dismantling, which would further reduce the inventory of inactive ships.

Navy Sink Exercises

The Navy will continue to environmentally prepare ships stricken from the Naval Vessel Register for Fleet at-sea, live-fire training exercises and in support of new ship acquisition

programs. The Rim of Pacific Exercise (RIMPAC) currently scheduled for summer of 2008 will require four vessels for this event. One of the four vessels will be removed from the Maritime Administration Suisun Bay facility to support this event.

Artificial Reefing

The Navy is finalizing the application and evaluation process for awarding ex-FORRESTAL as an artificial reef. An application will be sent to each reefing coordinator in the Gulf Coast and Atlantic Coast as well as the governor of Florida's office. Responses to the application will be due thereafter, at which point the Assistant Secretary of the Navy for Research, Development and Acquisition will make a decision on award of the ex-FORRESTAL. Due to classification issues with Side Protection Systems on the Forrestal Class, the Navy requires that this vessel must be reefed in a minimum of 450 feet of water. The goal of this deepwater reef project is to provide habitat for the protection and enhancement of deepwater snapper and grouper species.

In addition to preparing the ex-FORRESTAL, the ex-ARTHUR W RADFORD (DD 968) will be offered to States for use as an artificial reef. The composite mast system was potentially a floatable item and was removed by the Navy. The Navy is working with the Atlantic Marine Fisheries Commission and the Gulf Cost Marine Fisheries Commission regarding the availability to States for transfer of ex-ARTHUR W RADFORD.

Navy/Maritime Administration Cooperation

The Navy and Maritime Administration will continue to engage in cooperative strategies addressing their respective inactive ship inventories and are meeting at regular intervals to share lessons learned on vessel disposal programs. Future initiatives include:

- The Maritime Administration requested the preparation of ex-GAGE (APA 168) located at the Maritime Administration James River, Virginia, for sink exercises under the Navy and Maritime Administration Memorandum of Agreement.
- The Maritime Administration has agreed to work with Navy and Coast Guard on investigating and developing best management practices for NISA compliance.
- Four Osprey Class Mine hunters were decommissioned in December 2007 and will be temporarily stored at the Maritime Administration Beaumont, Texas, facility pending passage of the Naval Vessel Transfer Act of 2007, which authorizes the transfer of these vessels to a foreign country via the Foreign Military Sale process.

Conclusions

The Navy remains committed to reducing and eliminating any environmental risks posed by its inactive ships. Their goal is also to reduce the size of the inactive ship inventory utilizing multiple vessel disposal methodologies (i.e., foreign military sale transfers, ship donations, experimental/target use, title transfers to the Maritime Administration, domestic ship dismantling, and artificial reefing) that are most advantageous to the Navy, while also evaluating additional options for vessel disposal.

Delaying vessel disposal creates unnecessary risks and increases life cycle costs as inactive ships designated for disposal continue to deteriorate with age and the cost to maintain those increases.

However, the Navy cannot sustain full utilization of all available vessel disposal methodologies with limited future budgets for vessel disposal.

The Navy and the Environmental Protection Agency (EPA) in consultation with the Coast Guard and other agencies, are currently working together to implement the Uniform National Discharge Standards (UNDS) program, which addresses all incidental discharges from armed forces vessels.

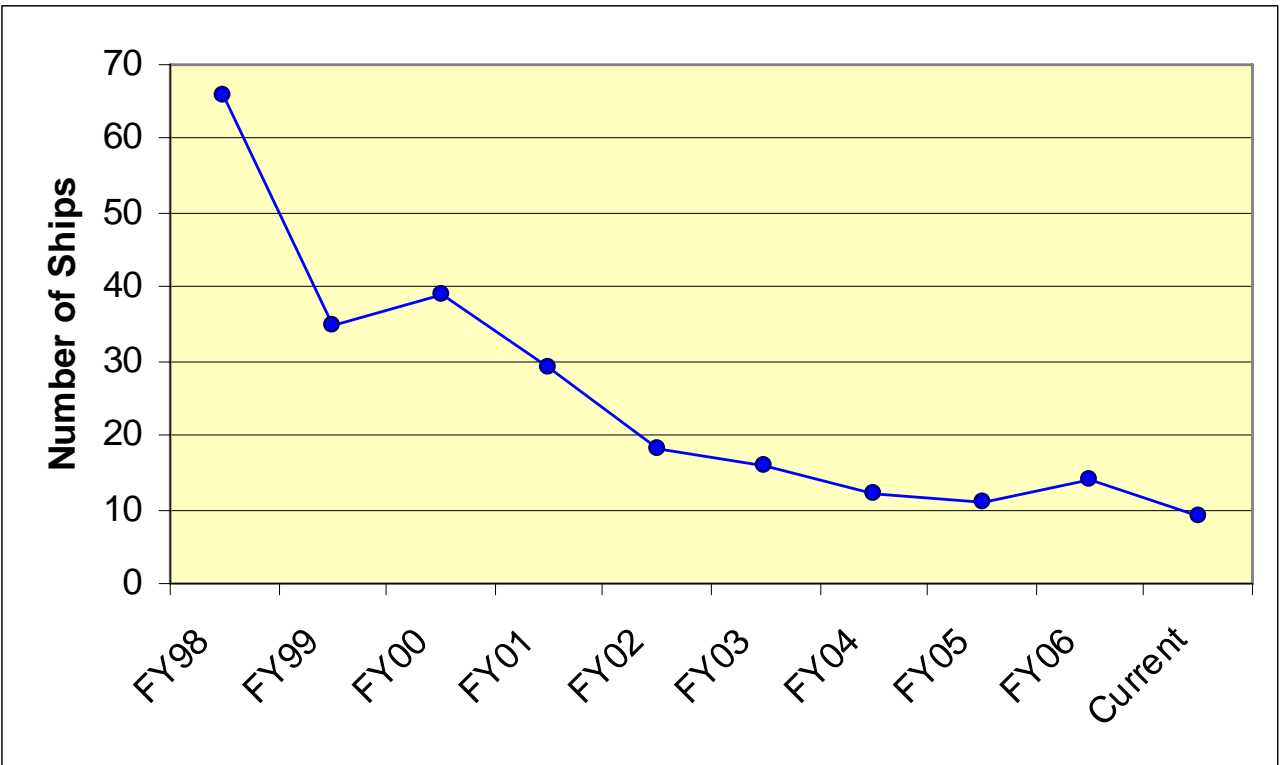
APPENDIX 1**Trend of Navy-Titled Obsolete Ships in the MARAD National Defense Reserve Fleet from FY98 to Present**

Figure 1 – Navy-Titled Obsolete Vessels in the MARAD National Defense Reserve Fleet designated for disposal

APPENDIX 2

Table 1 – Navy-Titled Obsolete Vessels in the Maritime Administration National Defense Reserve Fleet designated for disposal

| Ship | Location | Method of Disposal | Projected Cost of Disposal |
|-----------------------------|---|--|-----------------------------------|
| AFDM 2 drydock | Maritime Administration Beaumont, TX | H.R. 1815 Section 1013 (FY06 National Defense Authorization bill) proposes to grant AFDM 2 to the Port of Port Arthur, TX | \$0 |
| Oriole (MHC 55) | Maritime Administration Beaumont, TX | Foreign Military Sale | \$0 |
| Falcon (MHC 59) | Maritime Administration Beaumont, TX | Foreign Military Sale | \$0 |
| Osprey (MHC 51) | Maritime Administration Beaumont, TX | Logistics Support Asset | \$500,000 |
| Robin (MHC 54) | Maritime Administration Beaumont, TX | Logistics Support Asset | \$500,000 |
| Iowa (BB 61) | Maritime Administration Suisun Bay, CA | Donation hold | \$0 |
| Sea Shadow (IX 529) | Maritime Administration Suisun Bay, CA | Donation hold | \$0 |
| Triumph (AGOS 1) | Maritime Administration Suisun Bay, CA | Transfer to another Navy activity for use as a training vessel | \$0 |
| Horne (CG 30) | Maritime Administration Suisun Bay, CA | Navy Sinkex Exercise – RIMPAC 08 | \$750,000 |
| Fort Fisher (LSD 40) | Maritime Administration Suisun Bay, CA | Disposal Method TBD | \$400,000 |
| Higgins (AO 190) | Maritime Administration Suisun Bay, CA | Foreign Military Sale | \$0 |

Notes: Ships designated for Navy sink exercise or artificial reefing may also be placed under contract for domestic ship dismantling based on availability of funding and determination of the disposition that is most advantageous for the Navy for the purpose of inactive ship inventory reduction.

APPENDIX 3

Table 2 – Ship Disposal Project Task Order Status – Fiscal Year 2007

| Ship | Contractor | Awarded | Completed | Net Cost to Navy # | Cost Per Ton |
|---|-------------------|----------------|--|---------------------------|---------------------|
| Sacramento (AOE 1) INACTSHIPMAINT O Bremerton, WA | ESCO Marine, Inc | Apr 2007 | Estimated completion date March 04, 2008 | \$1,141,152 | \$60 |
| Camden (AOE 2) INACTSHIPMAINT O Bremerton, WA | ESCO Marine, Inc | Apr 2007 | Estimated completion date March 04, 2008 | \$1,141,152 | \$55 |

APPENDIX 4

List of Acronyms

| | |
|--|-----------|
| Army Corp of Engineers | (ACE) |
| Beaumont Reserve Fleet | (BRF) |
| Best Management Practices | (BMP) |
| Clean Water Act | (CWA) |
| Comprehensive Management Plan | (CMP) |
| Deep Sink Exercises | (SINKEX) |
| Department of Defense | (DOD) |
| Environmental Agency | (EA) |
| Environmental Excellence Initiative | (EEI) |
| Environmental Protection Agency | (EPA) |
| ESCO Marine Incorporation | (ESCO) |
| Federal Acquisition Regulation | (FAR) |
| Fiscal Year | (FY) |
| Hartlepoole Borough Council | (HBC) |
| Indefinite-Delivery\Indefinite-Quantity | (IDIQ) |
| James River Reserve Fleet | (JRRF) |
| Memorandum of Agreement | (MOA) |
| National Defense Reserve Fleet | (NDRF) |
| National Environment Protection Act | (NEPA) |
| National Invasive Species Act | (NISA) |
| National Marine Fisheries Services | (NMFS) |
| National Oceanic and Atmospheric Administration | (NOAA) |
| Polychlorinated biphenyls | (PCB) |
| Suisan Bay Reserve Fleet | (SBRF) |
| Supervisor of Shipbuilding Conversion and Repair | (SUPSHIP) |
| Toxic Substance Control Act | (TSCA) |
| Uniform National Discharge Standards | (UNDS) |
| United States Coast Guard | (USCG) |
| United Kingdom | (UK) |
| Waste Management License | (WML) |
| Water Quality Control Board | (WQCB) |