

UNIVERSITY OF KWAZULU-NATAL

**BAREBOAT CHARTER REGISTRATION: THE WAY FOR SOUTH AFRICA
TO REGAIN A MERCHANT FLEET UNDER ITS REGISTER**

By

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DECLARATION

I, Daniela Christin Franck, declare that

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ACRONYMS AND ABBREVIATIONS

AJRA	-	Admiralty Jurisdiction Regulation Act
AU	-	African Union
BCR	-	Bareboat Charter Registration
BIMCO	-	Baltic and International Maritime Council
BIMP	-	Brunei Darussalam, Indonesia, Malaysia and the Philippines
CIF	-	Cost Insured Freight
DOT	-	Department Of Transport
DWT	-	Deadweight Tonne
EAGA	-	East Asian Growth Area
FOC	-	Flag of Convenience
FOB	-	Free on Board
GRT	-	Gross Register Tonne
ILO	-	International Labour Organisation
IMO	-	International Maritime Organisation
ISR	-	International Ship Register
ITF	-	International Transport Workers' Federation
MARINA	-	Maritime Industry Authority
NEPAD	-	New Partnership for Africa's Development
OR	-	Open Register
PHP	-	Philippine Peso
SADC	-	Southern African Development Community
SAMSA	-	South African Maritime Safety Authority
SASR	-	South African Ships Register

SPWEL	-	Special Processing Window/Express Lane
SRA	-	Ship Registration Act
STCW	-	Standards of Training, Certification and Watchkeeping for Seafarers
UNCCROS	-	United Nations Convention on Conditions for Registration of Ships
UNCLOS	-	United Nations Convention on the Law of the Sea
UNCTAD	-	United Nations Conference on Trade and Development
US	-	United States
USD	-	United States Dollar

ABSTRACT

The economic benefit of a merchant fleet is well recognised in South Africa. As a means of articulating its aspirations, the government has drafted and implemented several policies designed to make the South African Ship Register more attractive. Evidence of these policies has been manifested in the rolling out of Operation Phakisa. Against this background, the dissertation will evaluate and analyse these policies.

The thesis investigates possible reasons for the absence of a merchant fleet flying the South African flag and the impact which this has had on the country, and reflects on the effectiveness of the new policies. The aim of this work is to explore options that South Africa may employ through these policies, in its endeavour to re-establish itself as a respectable maritime nation. The central question the thesis asks is whether bareboat charter registration can be seen as a possible solution for increasing the merchant fleet under the South African Registration Act, 1998.

Bareboat charter registration has been used by various developed and developing countries over the past centuries and offers substantial benefits in facilitating ship finances and encouraging joint ventures to promote commercial maritime expansions. This thesis seeks to establish whether BCR is a practice which should be promoted in South Africa in order to regain a merchant fleet.

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CHAPTER 1 Introduction

1.1 Background of the study

About 98 per cent of South Africa's trade is conducted by sea, all of which is carried by foreign-owned vessels.¹ The reason for this is that at present South Africa does not have a merchant fleet on its register.² The South African register is generally seen as uncompetitive. The nature of shipping is such that it is one of the most globalised industries and one where capital is highly mobile. Therefore, a shipowner whose place of business is in one country has the option of having his/her fleet registered outside that country to a more competitive environment where profit could be maximised without the need to move the company.

It is therefore the prevailing objective of any government to ensure that domestic shipping businesses keep their fleet in national registers. However, shipowners will always be looking to move their fleet to the register that offers the most benefits, which traditional shipping registers find hard to keep up with.

The South African government is no exception, but South Africa has over the years struggled to realise its aspirations.

The struggle emanates from several factors. Firstly, the ranking of mortgage claims under the Admiralty Jurisdiction Regulation Act (AJRA) is unfavourable for shipowners in South Africa. Secondly, a shipowner faces problems in financing the purchase of a vessel in South Africa because of exchange control restrictions. And finally, the taxation regime has for some time been unfavourable to shipowners as they have been subjected to the general taxation law of South Africa. This problem has recently been rectified with the promulgation of Act No. 43 of 2014: the Taxation Law Amendment Act 2014. However, the effects of this amendment have not yet been felt.

These problems are predominantly associated with traditional ship registration as opposed to bareboat charter registration (BCR). It is on this basis that this thesis suggests BCR as the only viable and realistic means by which South Africa can rebuild a merchant fleet under its register.

¹ West E. 2014. Time for SA to own its merchant shipping, Brics meeting hear. *BDliveOnline*, 25 March. <http://www.bdlive.co.za/business/trade/2013/03/25/time-for-sa-to-own-its-merchant-shipping-brics-meeting-hears> [Accessed on: 06 May.2015].

² On 20 August 2015, the *Cape Orchid* was registered in South Africa.

BCR temporarily allows a vessel to fly the flag of another country while ownership continues to be registered in the underlying registry. A vessel can fly the flag of its bareboat charterer's state upon consent of the underlying registry for the duration of the bareboat charter. BCR is not a synonym for open registries, as a number of traditional maritime states³ have adopted legislation regarding vessels "flagging-in" and/or "flagging-out".⁴ As it provides a welcome element of flexibility in various commercial situations.

BCR possesses some advantages. For instance, the charterer has the option to register the bareboat chartered ship in another flag state to take advantages of the laws of the flagging-in state, such as taxation benefits, participating in coastal cabotage traffic and being allowed to carry cargo which is restricted to only nationally owned ships. South Africa therefore needs to implement policies to make the South African Ships Register (SASR) attractive for bareboat charterers.

South African maritime and general transport policies focus on stimulating the local register through policies. These policies seek to encourage the use of South African-flagged ships for carriage of South African cargo and coastal operations based on some international policies and regional treaties⁵. If the policies come into effect, then a foreign shipowner who registers his/her fleet under BCR in South Africa, can profit from these measures as a result of the right to sail in cabotage traffic and carry cargo restricted to South African-flagged vessels only. As a side issue, this paper criticises proposed cabotage restrictions and cargo reservation measures in South Africa which are contrary to the present international trend towards globalisation and deregulation. As such, the thesis will focus on a case study on BCR and show the relevance of cabotage restriction on this type of ship registration. The Philippines will be used as a primary case study, with the aim of determining whether or not this practice may be positive for South Africa.

³ United Kingdom, France, Italy, Spain and Germany to name a few.

⁴ Ready, N.P. *Ship Registration*. 3rd Ed. London, Hong Kong: LLP, (1998) 40.

⁵ TRANSNET. 2015. *Operation Phakisa Presentation Invest in South Africa Ocean Economy Seminar 6-7 July, South Africa House London, United Kingdom*. [Online]. Available at: <http://www.fbicommunications.com/downloads/Transnet%20Operation%20Phakisa%20Invest%20in%20SA%20Seminar%20July%202015.pdf> [Accessed: 20.08.2015].

1.2 Objectives of the study

The *Cape Orchid* is the first merchant vessel to be registered in South Africa in three decades.⁶ Government needs to consider how to encourage more shipowners to register their fleets in South Africa. In keeping with its objectives, the South African government has, over the past decade, drafted several policies with the aim of promoting the SASR. This study examines why South Africa has failed to attract a merchant fleet, and evaluates whether South Africa's policies have effectively addressed the problems. The study also provides an insight into the challenges of the SASR and explores possible solutions.

The thesis suggests that BCR is the type of register for South Africa to promote, because it will not be affected by the problems of financing a vessel in South Africa and unfavourable ranking of mortgage claims. Therefore the thesis aims to analyse the option of rebuilding a fleet under BCR and briefly examines the numerous and complex problems often encountered in BCR owing to the many different parties involved. The ancillary question is therefore whether South Africa would be able to manoeuvre its way around these challenges.

1.3 Rationale of the study

South Africa's inability to carry its own import and export cargos, by its very nature, makes this study important. There is also the very important issue that having no commercial fleet leads to significant loss of public and private sector maritime experience and deprives the country of the development and innovation normally associated with owning and operating an indigenous merchant fleet.

This study is relevant to South Africa as it seeks to evaluate alternatives to having a domestically flagged commercial fleet which the country can exploit in its trade, thus sharing in transport revenues currently enjoyed by foreigners. Based on the fact that there are foreign vessels already plying trade in South Africa, the thesis suggests the possibility that some of these foreign vessels that can be flagged into South Africa through BRC to acquire tonnage.

There are a number of benefits that South Africa would enjoy in having its own fleet. Firstly, the development of a national commercial fleet could improve the balance of payments

⁶ Wyngaardt van, M. 2015 Cape Orchid merchant vessel arrives in Saldanha for Kumba Iron Ore. *Engineering News Online*, 25 September. <http://www.engineeringnews.co.za/article/cape-orchid-merchant-vessel-arrives-in-saldanha-for-kumba-iron-ore-2015-09-25> [Accessed:20 October2015].

resulting from the current foreign exchange requirement for South African cargo owners to pay foreigners for ships' space.

Secondly, a national fleet will not only generate employment for seafarers but can also create associated jobs linked to the management, finance, insurance and supply of vessels.

Thirdly, BCR brings the benefits of having a merchant fleet in SASR without the financial strain of purchasing a vessel. Hence, in South Africa, no commercial bank offers industrial ship financing and insurance. In addition, exchange control restrictions prohibit the granting of United States dollar (USD) denominated finances. It is therefore factually impossible for a South African ship-owning company to obtain equitable finance of a long-term nature to finance the acquisition of a ship.

The research undertaken indicates a lack of research conducted in evaluating if BCR is the most suitable type of registration for South Africa to promote. The study therefore makes a theoretical contribution to the literature by filling the gap in South African academic studies assessing the feasibility of promoting BCR and its impact on the South African economy.

1.4 Research methodology

The thesis entails a desktop study with secondary data collection. Content analysis is utilised to sort the data into themes.

The study uses secondary data research methods when searching for relevant information and material applicable to the research problem. The primary sources used in this thesis are policies, international conventions and preparatory work.

An online research was conducted to gather data from the Philippines' register in order to compare it with the SASR. This analysis contributes to the recommendation of the study regarding changes which need to be made.

Industry magazines, journal articles and online sources such as Sabinet provided useful material. When information in this thesis is based on second-hand sources, there might be problems concerning the accuracy of the information. I have therefore tried to make a distinction between sources based on the authority of the authors and the standing of academic journals utilised, where legal text was not available. Hence such sources are assumed to be more reliable.

1.5 Study overview

The study is divided into eight chapters. Chapter 1 gives the background for the study, defines the objective, rational research methodology used and also provides an overview of the study. Chapter 2 discusses the underlying principles and nationality regimes with regard to vessel registration. Different types of register are also briefly outlined. Chapter 3 gives background information on bareboat chartering and explores problems associated with BCR. Chapter 4 examines the reasons why the South African register is seen as uncompetitive, which leads to the conclusion that Bareboat Charter Registration (BCR) should be promoted in South Africa. It also clarified in this chapter that the South African Ship Registration Act (SRA) of 1998 allows for BCR in South Africa. Chapter 5 discusses the effectiveness of policies which the South African government has implemented, in order to rebuild the South African-flagged fleet. In Chapter 6, a case study of the Philippines' register is conducted in order to establish how the government of the Philippines has successfully promoted BCR through its policies. Moreover, this chapter discusses the application of cabotage restrictions in the Philippines. Chapter 7 evaluates different means of state interference which that government uses in order to protect their merchant fleet and examines if these would be feasible for South Africa to apply. Chapter 8 provides the final conclusion of the study.

CHAPTER 2 Principles underlying regimes of ship registration

2.1 Background

This chapter will examine the general principle of the freedom of the high seas and the rules governing a vessel's nationality and registration. These are essential in the identification and exercise of jurisdiction over ships. The chapter will briefly define other types of ship register in order to carry out a meaningful analysis of BCR. However, it is beyond the ambit of the study to cover all legal aspects such as documentation and flag. Therefore the study highlights those aspects that are deemed to be of most relevance to BCR, namely nationality and registration. Nationality refers to the link between the ship and the state that has jurisdiction over the vessels, while registration is the entering of the ship in the public record which is the precondition for testing the vessel's nationality.

2.2 The freedom of the high seas⁷

The 1958 Geneva Convention on the High Seas defines the freedom of the high seas as follows: "The high seas being open to all nations, no state may validly purport to subject any part of them to its sovereignty⁸." In other words, the open oceans are not part of the exclusive economic zone, territorial seas or internal waters of any state. The principle of the freedom of high seas therefore allows for unrestricted access of vessels belonging to all nations and is one of the essential rules of international maritime law. Thus, vessels belonging to all nations have the right to take advantage of this freedom. A shipowner may therefore decide to register his/her vessel in a foreign state to gain economic advantages such as lower taxation and salary costs.

International conventions such as the Geneva Convention of the High Seas, 1958 and United Nations Convention on the Law of the Sea (UNCLOS), 1982 lay down a number of rules to provide a framework for the exercise of such freedom. It is, however, up to the individual state to enforce compliance with those rules. Furthermore, it is up to the flag state to decide who will be rendered the right to fly the state's flag and to prescribe the rules governing such an agreement. The history of registering a ship in a state different to that of the beneficial owners dates back to the 16th century when British ships improperly used the Spanish flag to overcome

⁷ Farthing, B. and Brownrigg, M. *Farthing on International Shipping*. 3rd Ed. Berlin Heidelberg: Springer-Verlag.(1997) 1.

⁸ Geneva Convention of the High Seas, 29 April 1958, Art. 2.

trade restrictions in the West Indies⁹. It was however only in 1905 that the Hague Court of Permanent Arbitration in the case of the *Muscat Dhows* (1916) – a vessel engaged in the slave trade which was flying the French flag but was owned by the Muscat Sultan – stated that “generally speaking it belongs to every sovereign to decide to whom he will accord the right to fly his flag and to prescribe the rules governing such grants¹⁰.” Attempts have been made to define the meaning of this requirement in the United Nations Conventions. However, the Geneva Convention on the High Seas, 1958 restated the principle:

Each State shall fix the conditions for the grant of nationality to ships for the registration of ships in its territory, and for the right to fly its flag. Ships have the nationality of the State whose flag they are entitled to fly. There must exist a genuine link between the State and the ship; in particular, the State must effectively exercise its jurisdiction and control in administration, technical and social matters over ships flying its flag¹¹.

The UNCLOS, 1982 prescribes the same principle in Article 91. An attempt to define the international minimum requirements that need to be fulfilled before a ship can be considered to have gained a certain nationality were made in the United Nations Conventions on the Conditions for Registration of Ships, 1986. The objective of this convention was to strengthening the genuine link between a state and the ships flying its flag¹².

2.3 Nationality and registration of ships

Although the high seas are open to all states, a ship needs to have a nationality in order to engage in lawful trade with different ports. A ship possessing no nationality is a stateless ship, which will be denied entry by ports and will not enjoy protection in international law. The ship’s nationality is generally apparent from the flag it flies and must only have one nationality. The concept behind the nationality of the ship stems from the fundamental characteristics of the mobility of the ship beyond the jurisdictional limits of the state into the high seas where no jurisdiction would otherwise prevail. For this reason, the Geneva Convention on the High Seas,

⁹ Francisco, J. 2003. Open registers: past, present and future. *Marine Policy* 27, 513-523. <http://www.sciencedirect.com.ezproxy.ukzn.ac.za:2048/science/article/pii/S0308597X03000770> [Accessed 03 June2015].

¹⁰ Li, K. X., Wonhama, J. 1999. New Developments in Ship Registration. *International Journal of Marine and Costal Law*, Vol 14, Issue 1, 137-154. http://www.heinonline.org.ezproxy.ukzn.ac.za:2048/HOL/LuceneSearch?terms=Registration+of+Vessels.+wonham&collection=journals&searchtype=advanced&typea=text&tabfrom=&other_cols=yes&submit=Go [Accessed: 08 June2015].

¹¹ Geneva Convention of the High Seas, 1958. Article 5(1).

¹² United Nations Convention on Conditions for Registration of Ships. Article 1.

1958¹³ and the UNCLOS, 1982¹⁴ provide that the flag states have exclusive control and jurisdiction over their vessels on the high seas. A vessel therefore requires nationality in order to enjoy protection in the international law; otherwise, it would be a stateless ship.

Nationality is therefore a matter of substantive law, whereas registration is the procedural mechanism through which nationality is conferred¹⁵. Registration means entering a ship in the public records and is a precondition for the test of the vessel's nationality. Nationality refers to the link between the ship and the state that has jurisdiction over the vessels concerned. This is the public law function of registration¹⁶. Hence the national character of registration provides the ship with protection on the high seas and enters the vessel in its country's system of law. The master and crew working on board the ship are obliged to follow the law of the country of registration and are protected by the same law. Furthermore the owner of the vessel is obliged to adhere to the safety regulations of the state of registration. International conventions therefore are mainly concerned with the public law functions. Thus the Geneva Convention of the High Seas provides in Article 5 that "the State must effectively exercise its jurisdiction and control in administrative, technical and social matters over ships flying its flag" and Article 10 provides that "every State shall take such measures for ships under its flag as are necessary to ensure safety at sea". It may therefore be said that public law sees the ship as a floating community carrying with it the sovereignty of the state whose flag she flies. Private law, on the other hand, sees the ship as a moveable property over which one or more persons may have rights which the law considers worthy of protection. Among the private law functions are the protection of the title of the registered owner and the preservation of priorities between persons holding security interest over the vessel, such as mortgages¹⁷.

2.4 Types of ship register

In order to carry out a meaningful analysis of BCR in South Africa it is useful to define the different types of ship register. The main types of ship register are "Open Register" (OR) also referred to as "Flag of Convenience" (FOC) or "International Ship's Register" (ISR), "Closed Register" (CR) and "Second Register" (SR). The majority of developing countries operate ORs

¹³ Geneva Convention on the High Seas, 1958. Article 6.

¹⁴ United Nations Convention on the Law of the Sea, 1982. Article 92.

¹⁵ Mukherjee, K. and Brownrigg, M. 2013. *Farthing on International Shipping*. 4th Ed. Berlin Heidelberg: Springer-Verlag, 202.

¹⁶ Ready, N.P. *Ship Registration*. 3rd Ed. London, Hong Kong: LLP, (1998) 6.

¹⁷ Ibid. p.7.

which is perceived as unfair competition by the traditional maritime nations which operate CRs. The different type of registers will be analysed in the next section.

The terms OR and FOC are used interchangeably for the registration of a ship in a country other than the country in which the ship is beneficially owned, managed and controlled. Countries such as Panama, Liberia and other Caribbean countries have successfully established a merchant fleet through the FOC concept. These countries offer the shipowners the opportunity to register their ships without a genuine link to the country of registration, or offer simple requirements to establish a link such as a “letterbox company” in the country of registration. This gives the internationally operating shipowner the option to register his/her vessels in a country other than the country of business or domicile. The Rochdale Committee of Inquiry into Shipping(1970) states that the FOC registry “has neither the power nor the administrative machinery to effectively impose any government or international regulations nor the wish or the power to control the companies themselves¹⁸”. Ships registered in a FOC state are therefore a concern for the International Transport Workers’ Federation (ITF) with regard to safety standards, long working hours, wages and unsafe working conditions for seafarers¹⁹. The shipowner therefore has to consider the stigma which is attached to registering the vessel in a FOC state but the commercial benefits often overrule those concerns. The reasons a shipowner may choose to register his vessel in a FOC state are versatile and include the following considerations:

- Easy registration of ships. Registration is often possible through the consul of the flagging-in state in the country of the shipowner.
- Easy flagging-out options.
- A low tax regime on company’s earnings or tonnage tax regime.
- Freedom for employment of foreign nationals.
- Low registration and survey fees.
- Relaxed foreign exchange controls.

¹⁸ Tally, W. 2012. *The Blackwell Companion on Maritime Economics*. [Online]. West Sussex: Blackwell Publishing Ltd. Available at: https://books.google.co.za/books?id=I_Uu4_VRDxUC&pg=PA284&lpg=PA284&dq=%22Rochdale+committee%22+flag+of+convenience&source=bl&ots=SlOWYPcbet&sig=9GtWiihq_-7YdCSfabWzsaqlzal&hl=en&sa=X&ved=0CBsQ6AEwAGoVChMlrSzNt4PtyAIVhMUUCh21zA4X#v=onepage&q=%22Rochdale%20committee%22%20flag%20of%20convenience&f=false [Accessed: 09 October 2015].

¹⁹ Ibid

In contrast to the FOC, requires the CR that the shipowner or demise charterer is a national of the flag state with a body corporate registered and active in that state²⁰. Some very traditional CRs require that the crew of the ship or at least senior officers are nationals of the state of register. The majority of countries who register is a CR are traditional maritime nations with a long history in ship registration such as Germany, United Kingdom and Italy. They have a wealth of knowledge in the maritime field, and through long years of maritime administration have established a responsible framework regarding ship regulations and have ratified a high number of International Maritime Organisation (IMO) and International Labour Organisation (ILO) conventions²¹. Those high standard have the side effect that the CRs are at a competitive disadvantage with FOC's. Therefore many beneficial shipowner with domicile in a CRs flag State chooses to register their fleet in a FOC state. As a result, many CRs have reduced their strict requirement and allow for a greater percentage of crew to be foreign nationals or introduced the SR.

SRs were created by traditional maritime countries with a CR due to the loss of their national fleet to FOC country due to the economic advantage. The SR is the additional registration of the vessel usually in a FOC country in order for the shipowner to benefit from the special regulations of that country with regard to employment and taxation regulations. However, the main register remains that of the CR state and therefore the higher standards apposed in the country of the CR are maintained and enforced. Since the SR is administered and controlled by the CR's nation, the high standards for maritime safety and the implementation of international regulations are maintained ²².

BCR is the dual registration of a ship in two flag states. Often the bareboat charterer chooses a FOC country for the registration but this is a different practice than the registration of the ship in the SR and will be further examined in Chapter 3. BCR has been adopted with enthusiasm by the shipowning community and government alike. Hence it provides the bareboat charterer

²⁰ Mansell, J. 2009. *Flag State Responsibility: Historical Development and Contemporary Issues*. [Online] Berlin Heidelberg: Springer-Verlag, 102. Available at: https://books.google.co.za/books?id=JWdsgKxvmeUC&pg=PA101&dq=definition+%22closed+register%22+shipping&hl=en&sa=X&ved=0CBoQ6AEwAGoVC_hMI_Pjux5HtyAIVRTcUCh1iOgZJ#v=onepage&q=definition%20%22closed%20register%22%20shipping&f=false [Accessed: 07 October 2015].

²¹ Ibid

²² Li, K. X., Wonham, J. 1999. New Developments in Ship Registration. *International Journal of Marine and Coastal Law*, Vol 14, Issue 1, 137-154. http://www.heinonline.org.ezproxy.ukzn.ac.za:2048/HOL/LuceneSearch?terms=Registration+of+Vessels.+wonham&collection=journals&searchtype=advanced&typea=text&tabfrom=&other_cols=yes&submit=Go [Accessed: 08 June 2015].

with the advantage of registering the ship in a different state to reduce operating costs and allows for commercial and fiscal benefits.

2.5 Conclusion

The above discussion shows that BCR is not an isolated legal concept apart from or beyond what a particular set of ship registries would permit. In other words, it is a form of ship registration that depends on the parameters of ship registration that operate in two separate states. Therefore it is imperative for anyone intending to use BCR that they understand the rules and principles applicable in each registry concerned.

CHAPTER 3 Bareboat charter registration (BCR)

3.1 Background

BCR is the dual registration of a ship in two flag states. The “flagging-in” state is the state of the bareboat charter registry. It is the responsibility of the flagging-in state to ensure that the right to fly the flag of the primary state is suspended. The bareboat charter vessel is therefore under the full control and jurisdiction of the flagging-in state. The flagging-out state is the state of the primary registry. It is the register to which the vessel reverts upon termination of the bareboat charter. Often the bareboat charterer would choose an FOC country to register the ship. This practice could be confused with the registration of the ship in the second register; the difference between the two will be explained below.

BCR has been enthusiastically adopted by private operators and ship-owning governments alike, given its effectiveness. The most obvious attraction of BCR practice lies in its commercial viability. It gives the bareboat charterer the advantage of registering the ship in a different state which makes it possible to reduce operating costs and to derive commercial and fiscal benefits. In the case of a ship-owning government, BCR can be used as a means of increasing national tonnage which in turn facilitates the government’s own imperatives, for instance, relating to training and employment of local seafarers, receipt of foreign exchange and taxation without the financial strain of purchasing a vessel. BCR has therefore gained popularity in developing countries. However, this system also creates concerns such as the fact that there are no bilateral or multilateral conventions regulating BCR. It is therefore solely dependent on the legal systems in the flagging-in and flagging-out states.²³ This leads to the question whether a ship can be registered in two different states at the same time. The prima facie answer would be negative. A vessel flying two or more flags, using them for its convenience, is considered a stateless ship²⁴. The following section will therefore examine why BCR is possible and how it has evolved.

²³ Ready, N.P. *Ship Registration*. 3rd Ed. London, Hong Kong: LLP, (1998) 39–41.

²⁴ United Nations Conventions on the Law of the Sea Article 92(2) and Geneva Convention of the High Seas Article 6(2).

3.2 What is a bareboat charter?

What sets a bareboat charterer apart from other types of charterers is the fact that the owner of the ship passes possession and control of the entire asset, being the ship, to the charterer against the payment of hire as per the contractual agreement made in the charter party. Other chartering forms operate differently to this. For instance, the owner of the ship under a time charter usually reserves ownership of the vessel throughout the time charter, even if the charter extends for most of the ship's life. The charterer simply takes the use and enjoyment of the ship, but not virtual ownership, as is the case with bareboat chartering.

Commonly used BIMCO forms for the bareboat charter are BARECON and Shelltimes. The duration of a bareboat charter is usually for a long term of between five and ten years. In some instances the bareboat charter can be for the duration of the vessel's life and the owner is merely concerned with financing the vessel. As the name implies, the owner will hand the vessel over to the charterer bare and it is effectively a lease of the hull, machinery and equipment of the ship²⁵. Therefore the charterer takes both nautical and commercial control of the ship. He/she also becomes responsible for the manning and equipping of the vessel and decides where the vessel trades²⁶. In addition, the charterer is responsible for maintenance and insurance of the vessel during the charter period. A judicial definition of the bareboat charterer was laid down in the *Giuseppe di Vittorio* case (1998) which stipulates that "the legal owner gives the charterer sufficient right of possession and control which enables the transaction to be regarded as a letting – a lease or demise, in real property terms²⁷." For this reason, the charterer is treated like the de facto owner or *owner pro hac vice*²⁸ for the duration of the charter²⁹.

3.3 BCR

BCR allows the vessel to be registered in one state but it is permitted to fly the flag of a second state for the period of the bareboat charter. The reason for this is that possession and control of the ship passes to the charterer on conclusion of the charter party. As an owner *pro hac vice*,

²⁵ Davis, M. 2000. *Bareboat Charter*. London, Hong Kong: LLP, 4.

²⁶ Ibid.

²⁷ Coles, R, and Watt, E, ed. 2009. *Ship Registration: Law and Practice*. [Online]. London: Informa Law, 45. Available at: https://books.google.co.za/books?id=LWISINR76WgC&pg=PA363&lpg=PA363&dq=Coles,+R.;Watt,+E.+Ship+Registration:+Law+and+Practice.&source=bl&ots=urtdMCx6Z7&sig=YpX33yAaa_Ve83Ci0G01KIZE81c&hl=en&sa=X&ved=0CC4Q6AEwBGoVChMIzISC2KjyAIVTGkUCh1cNQel#v=onepage&q=Giuseppe%20di%20Vittorio&f=false [Accessed: 03 March 2015].

²⁸ Latin: For this time only; for this one particular occasion.

²⁹ Davis, M. 2000. *Bareboat Charter*. London, Hong Kong: LLP, 4.

the nationality of the charter is now vested in the vessel. The bareboat charterer therefore has the option to change the vessel's nationality for the duration of the charter in order to maximise his/her benefits in utilising the preferred state³⁰. The primary register therefore becomes the flagging-out state where the vessel is temporarily deleted from the maritime registry but remains fully entered in the commercial register. The temporary cancellation or suspension paves the way for the charterer to register the vessel in the preferred register that would become the flagging-in state. In BCR the public law and private law aspects of registration are therefore split between the two states³¹. The public law function of registration is transferred to the flagging-in state such as jurisdiction over labour and safety issues³². On the other hand, the private law functions remains with the flagging-out state such as transfer of ownership in the vessel and the ship's mortgage.

3.4 Potential problems associated with BCR

At present, there is no international convention dealing exclusively with BCR. The lack of uniformity in the international field can lead to misunderstanding between the public and private law functions of registration. Hence BCR solely depends on the compatibility between the legislations in the flagging-in and flagging-out states. The conceptual approach to BCR is by no means uniform among the different states which permit this practice. For example, some jurisdictions take the view that bareboat registration is in effect a registration *de novo*³³ and insist that the vessel's underlying registration be cancelled from the primary register for the duration of registration in the secondary register. This means that the proprietary interest will have to be registered in the flagging-in state. Regulations such as these are applicable for BCR in Australia³⁴. Other states permit bareboat registration even though the primary registration

³⁰ Ademuni-Odeke. 1997. The National and International Legal Regime of Bareboat Charter Registration. *Ocean Development & International Law*, Volume 28, Number 4, 329-367.
http://www.heinonline.org.ezproxy.ukzn.ac.za:2048/HOL/Page?handle=hein.journals/ocdev28&div=22&start_page=329&collection=journals&set_as_cursor=0&men_tab=srchresults [Accessed: 06 June 2015].

³¹ Coles, R, and Watt, E, ed. 2009. *Ship Registration: Law and Practice*. [Online]. London: Informa Law, 48. Available at:
https://books.google.co.za/books?id=LWISlNR76WgC&pg=PA363&lpg=PA363&dq=Coles,+R.;Watt,+E.+Ship+Registration:+Law+and+Practice.&source=bl&ots=urtdMCx6Z7&sig=YpX33yAaa_Ve83Ci0G01KIZE81c&hl=en&sa=X&ved=0CC4Q6AEwBGoVChMizISC2KjjyAIVTGkUCh1cNQeI#v=onepage&q=Giusseppe%20di%20Vittorio&f=false [Accessed: 03 March 2015].

³² Ibid.

³³ Latin: Anew.

³⁴ Mukherjee, K. and Brownrigg, M. 2013. *Farthing on International Shipping*. 4th Ed. Berlin Heidelberg: Springer-Verlag, 214.

remains operative in respect of proprietary interest ³⁵. This could result in the vessel being registered in two different states, which would mean that the vessel has more than one nationality and is subject to different jurisdictions. This would ultimately mean that it is a stateless ship according to United Nations conventions ³⁶. Another problem associated with BCR is that some flagging-in states require that mortgages, hypothecations and other registerable liens need to be re-recorded in their register. This could lead to legal problems by way of conflicts regarding the disposition of proprietary interest.

3.5 The SASR on BCR

Firstly, the South African SRA allows for a ship on bareboat charter to a South African national to be registered on the SASR ³⁷. The Act further states that the ship must be on bareboat charter to a South African national and is registered in terms of the law of another state ³⁸. It is not a prescribed ship ³⁹ and is on bareboat charter to one or more South African nationals and to no other person ⁴⁰. The aforementioned problem with regard to the registration of mortgage is eliminated in the South African SRA in that it clearly sets out that the private law provisions that apply to registered ships do not apply to ships on BCR ⁴¹. The Act therefore clearly determines that the private law function remains with the country of primary registration. This is a very important fact of the SRA as it provides clarity, particularly when one considers that the ranking of mortgage is unfavourable for shipowners in South Africa.

³⁵ Coles, R, and Watt, E, ed. 2009. *Ship Registration: Law and Practice*. [Online]. London: Informa Law, 49. Available at: https://books.google.co.za/books?id=LWISINR76WgC&pg=PA363&lpg=PA363&dq=Coles,+R.;Watt,+E.+Ship+Registration:+Law+and+Practice.&source=bl&ots=urtdMCx6Z7&sig=YpX33yAaa_Ve83Ci0G01KIZE81c&hl=en&sa=X&ved=0CC4Q6AEwBGoVChMIzISC2KjyAIVTGkUCh1cNQel#v=onepage&q=Giuseppe%20di%20Vittorio&f=false [Accessed: 03 March 2015].

³⁶ United Nations Conventions on the Law of the Sea Article 92(2) and Geneva Convention of the High Seas Article 6(2).

³⁷ Ships Registration Act 1998. Section 16(c).

³⁸ Ibid. Section 1(6)(a).

³⁹ Ibid. Section 1(6)(b).

⁴⁰ Ibid. Section 1(6)(c).

⁴¹ Ibid. Section 31(9).

3.6 Conclusion

The rationale for countries to introduce a BCR system into their domestic register range from economic and commercial to national defence and security considerations. The South African SRA provides the legal basis for BCR in South Africa. It states as follows:

Section 1.(6) A reference in this Act to a ship on bareboat charter to a South African national is a reference to a ship that

- (a) is registered in terms of the law of another state;
- (b) is not a prescribed ship or a ship of a prescribed class or description; and
- (c) is on bareboat charter to one or more South African nationals, and to no other person.

Section 16. Subject to this Chapter, the following ships are entitled to be registered:
(c) ships on bareboat charter to South African nationals.

Section 31.(9) The provisions of Schedule 1 and regulations made for the purposes of that Schedule, or provisions of the regulations under section 56(3)(c), do not apply to ships registered in terms of section 16(c), and any matter or question in respect of such ships corresponding to those provisions are determined by reference to the law of the state of primary registration.

The practice of BCR seems not to have taken root in South Africa. So far only two ships⁴² have been registered in the South African register under BCR. The following chapters will analyse the problems of the SASR and examine how other countries have successfully increased their domestic fleet through BCR, in order to establish whether their approach could be feasible for South Africa to adopt.

⁴² Cape Orchid and Cape Enterprise.

CHAPTER 4 The need for South Africa's domestic fleet

4.1 Background

There are numerous benefits in having a national merchant fleet for any local economy. For instance, an economy will benefit through increase in revenue in the forms of taxes and other fees and the generation of foreign exchange. In addition, a national fleet can provide labour opportunities, not only in seafaring jobs, but also in associated maritime fields. It is therefore clear that South Africa would need to establish a merchant fleet under its register if it is to enjoy any or at least some of these benefits.

It is therefore unsurprising that without a merchant fleet, currently South Africa does not enjoy benefits normally associated with ship ownership. What is more alarming, however, are the huge disadvantage that the country suffers as a consequence of being unable to carry its own cargo.

This chapter deals with the perceived uncompetitive nature of the South Africa registry which is generally viewed as prohibitive to building a home-grown fleet. The chapter looks at the reasons for the perception, critically analyses the government's initiatives to rebuild the South African flag, and questions whether these make the registry any more competitive. In other words, do any of the government's initiatives change the current perception of the South African flag? The challenges associated with the South African flag which make it uncompetitive, form the basis for suggesting that BCR is the most appropriate form of registration, as it is least affected by these challenges.

4.2 Why does South Africa require a fleet under its register?

On 20 August, 2015 the first bulk carrier was registered under BCR in South Africa. Despite this reasoned success, the SASR still lacks competitiveness. Ship registration is a business decision and today's shipowners choose the register which offers them the most attractive taxation system and legal regimes.

South Africa is a maritime country with over 3 000 kilometres of coastline and eight merchant ports which are visited by about 12 000 vessels each year⁴³. The Ship Registration Act (SRA),

⁴³ TIMES LIVE. (2012) *Lack of merchant vessels is costing SA billions*. [Online] 09 May. Available from: <http://www.timeslive.co.za/local/2012/05/09/lack-of-merchant-vessels-is-costing-sa-billions>. [Accessed on: 06.05.2015].

No 58 of 1998 was implemented, which updated the administration and law relating to the SASR to current international standards, in a drive to rebuild the South African flag. However, since the inception of the Act in 2003, the SASR has up until recently seen no growth at all.

This is a huge opportunity foregone for South Africa considering that about 98 per cent of South Africa's exports are carried by sea in foreign-owned vessels and that South Africa's seaborne cargo accounts for 3.5 per cent of global sea trade. In 2014, 300 million tons of cargo moved internationally in imports and exports, which are currently carried by foreign-owned ships, according to a report by Operation Phakisa⁴⁴.

The economic benefits for a country with a strong merchant fleet are vast in terms of tax income, social contribution and employment opportunities derived from the ships under their register. According to government, the ocean economy holds potential employment for more than 700 000 people in South Africa, which would increase the contribution of the national gross domestic product from R55 billion to R177 billion by 2033⁴⁵. It is therefore the aim of the presidency and the planners participating in Operation Phakisa to rebuild the South African flag. The ambitious plans under Phase II of Operation Phakisa are to support the local registry of vessels through incentive and encouragement of using South African-flagged ships. The initiative aims to allocate 40 per cent of South African minerals to South African-flagged ships. Furthermore, all coastal operation must be done on South African-flagged vessels manned by South African seafarers⁴⁶. In order for Operation Phakisa to achieve its ambitions goal, 300 vessels will be needed to support 40 per cent of the trade and about 21 000 seafarers will be needed to man these vessels. However, at the moment South Africa produces about 240 officers per year, which leaves a huge deficit of skilled labour⁴⁷.

⁴⁴ Operation Phakisa is a Big Fast Results methodology which were first applied by the Malaysian Government successfully in the delivery of its economic transformation programme. It addresses national key priorities and sets clear plans and targets.

⁴⁵ Rensburg van, D. 2014. TALKING UP THE SEAS. What is the 'ocean economy' anyway? *Media 24 CityPress Online*, 26 October. http://m24arg02.naspers.com/argief/berigte/rapport/2014/11/01/5/BIZ%20PHAKISA_32_0_102326516.html [Accessed: 08 June 2015].

⁴⁶ OPERATION PHAKISA. 2014. *Open Day Operation Phakisa Maritime Transport and Manufacturing Posters, 2014*. [Online]. Available at: <http://www.operationphakisa.gov.za/operations/oel/mtm/Marine%20Transport%20Documents/Marine%20Manufacturing/Open%20Day%20Operation%20Phakisa%20Marine%20Transport%20and%20Manufacturing%20Posters%20%202014.pdf> [Accessed 08 June 2015].

⁴⁷ OPERATION PHAKISA. 2014. *Unlocking the Economic Potential of South Africa's Oceans*. Marine Transport and Manufacturing Executive Summary. [Online]. Available at: https://www.google.co.za/?gws_rd=ssl#q=Unlocking+the+Economic+Potential+of+South+Africa%E2%80%99s+Oceans%E2%80%99 [Accessed: 08 June 2015].

The reason for government's initiative to control South Africa's exports in South Africa is that South Africa's trade balance has worsened since 2012 and is running a current account deficit of 5.8 per cent of GDP ⁴⁸. The trade balance is calculated on the total amount of import payments subtracted from the total amount of export earnings. If there is an excess of import payments over export earnings, then it gives rise to a trade deficit. South Africa's main exports are minerals, which are sold FOB, meaning that the freight is not controlled in South Africa. It is therefore the aim of the government to have products sold as cost insured freight (CIF), which means that the seller includes the freight rate in the purchase price. This will increase the price of South African exports and help to reduce the trade deficit.

Another factor is that the low earnings on exports have an impact on the foreign exchange reserve. Normally, a country holds a kitty of foreign currencies worth three months of its imports value. The foreign exchange reserve expands and shrinks as a result of balance of payments transactions. If there is a trade deficit, then the financial account outflow exceeds the financial account inflows of foreign exchange reserve, which consequently makes foreign currency more scarce in South Africa and results in the depreciation of the rand. A weaker rand has the knock-on effect that the cost of imports rises – which will increase the trade deficit.

4.3 Lack of merchant ship registration in South Africa

The question therefore arises why the South African Register has failed to attract foreign owned vessels in its register. The main problem lies with the fiscal system which is the heart of an attractive ships register. The international trend is toward a reduction of taxation for shipping companies through tonnage tax or a total tax exemption. The taxation on the tonnage is calculated by measuring the tonnage of the ship and isn't based on the company's profit which essentially amounts to a smaller fee. In contrast South African shipping companies are subject to a corporate income tax rate of 28 per cent which makes the SASR uncompetitive and is cited as one of the main reasons why South Africa does not have merchant ships in its register. Against this background, government has assented Act No. 43 of 2014: Taxation Law Amendment Act, 2014 to provide tax relief for international shipping companies ⁴⁹. In order

⁴⁸ SOUTH AFRICA. DEPARTMENT: NATIONAL TREASURY. (2015) 2 *Economic Outlook*. [Online] Available from: <http://www.treasury.gov.za/documents/national%20budget/2015/review/chapter%202.pdf>. [Accessed: 08.06.2015].

⁴⁹ Taxation Laws Amendment Act, 2014. Government Gazette, 20 January 2015. Available at: http://www.gov.za/sites/www.gov.za/files/38405_Act43of2014TaxLawsAmend_20Jan.pdf. [Accessed on: 03.06.2015].

for a shipping company to qualify for this tax relief, the company must be a resident and hold at least one or more vessels, which are designed for international transport of goods and passengers for reward, and that are flagged in South Africa in terms of the SRA, 1998. One of the main changes of the Taxation Amendment Act is the amendment of Section 9D of the Income Tax Act, 1962 to the effect that the receipt and accruals derived by the international shipping company from the operation of a South African ship will be exempt from income tax⁵⁰. However, as a result of the capital gains and income tax exemption, the South African-flagged ship will no longer be depreciable. Furthermore, dividends paid by a qualifying shipping company will not be subject to dividend tax if the dividend is derived from the operation of the South African international transport ship. Moreover, the international shipping company will be exempt from withholding tax on interest if the interest is paid to a foreign lender in respect of a debt used to fund the construction or improvement of the South African-flagged international transport ship. In addition to this, officers and crew are exempt from tax on their salaries, irrespective of the number of days spent abroad. The previous conditions were that they had to be outside South Africa for more than 183 days⁵¹ for this tax exemption to occur.

The tax benefits for officers and crew would seem a welcome motivation for foreign shipowners to register their ships in South Africa and to hire South African seafarers. However, the wage rate for South African seafarers is relatively high in comparison to other seafaring nations. According to a study by Ruggunan (2011), the high wages out-priced South African seafarers from the global labour market⁵². If South Africa wants to encourage employment opportunities for seafarers then the labour union needs to allow for lower wage rates than ITF rates in order for South African seafarers to compete globally.

Another issue is that, according to the Employment Equity Act, HIV/AIDS testing is prohibited in South Africa unless such testing is determined to be justifiable by the Labour Court⁵³. It is however global practice that HIV testing forms part of the medical examination of seafarers.

⁵⁰ Taxation Law Amendment Act, 2014. Section 12(1)(b).

⁵¹ LEXISNEXIS. (2013) *Explanatory Memorandum on Taxation Laws Amendment Bill, 2013*. [Online] 24 October. Available from: <http://www.mylexisnexis.co.za.ezproxy.ukzn.ac.za:2048/Index.aspx>. [Accessed on: 03.06.2015].

⁵² Ruggunan, S. 2011. The Global Labour Market for Filipino and South African Seafarers in the Merchant Navy. *South African Review of Sociology*, Vol. 42 Issue 1, 78-96. http://ukzn.worldcat.org.ezproxy.ukzn.ac.za:2048/title/the-global-labour-market-for-filipino-and-south-african-seafarers-in-the-merchant-navy/oclc/4839668704&referer=brief_results [Accessed: 08 August 2015].

⁵³ Employment Equity Act. Section 7(2).

The majority of shipowners would therefore not consider hiring South African seafarers. It therefore needs to be evaluated if the Employment Equity Act provides sufficient room for such testing. Once these obstacles are overcome then South African seafarers should be welcomed by foreign shipowners. Hence there will always be a demand for well-trained English speaking seafarers. The competency of South African seafarers is guaranteed through the adherence to the International Convention on Standards of Training, Certification and Watchkeeping for Seafarers (STCW) and ILO 147 which is a convention concerning minimum standards in merchant ships.

Another key factor of the South African register being seen as uncompetitive is the ranking of mortgage claim. South African shipowners would find it difficult to find financiers to finance a ship's mortgage while mortgage ranks in South African law behind the suppliers of necessities. This is determined in section 11 of the Admiralty Jurisdiction Regulation Act (AJRA) which recognises 13 potential categories of claims with the claim for mortgage being in the 11th position⁵⁴. In most jurisdiction, mortgage claims enjoy a preference over claims for necessities. This situation clearly inhibits the development of an attractive ship's register for South Africa and needs to be addressed⁵⁵. Unfortunately to date, no legislative changes are planned to rectify the problem and amend the ranking of claims in the AJRA.

4.4 Conclusion

While there are no plans to rectify the problem with the ranking of claims according to the AJRA, the problem with regard to taxation has been addressed. Although this is a step in the right direction, it will still be problematic for shipowners to finance their fleet in South Africa. However, these are not the only options to establish a merchant fleet under the SASR. Ships do not need to be owned in order to derive trading revenues from their operation. They are often hired under a demise charter, on a five-year to ten-year charter period, during which the charterer treats the ship as its own and is responsible for the crewing and operation of the vessel. The SRA allows for bareboat chartered tonnage to fly the South African flag where the charterer is a South African national. The mortgage will therefore not be affected as it remains

⁵⁴ AJRA. Section 11(4)(d.)

⁵⁵ Lourens, M. 1998. The Ship's Mortgage In South African: Does The Draft Shipping Registration Bill Offer Solutions? *HeinOnline* [Online]. http://www.heinonline.org.ezproxy.ukzn.ac.za:2048/HOL/Page?handle=hein.journals/stelblr9&div=14&start_page=98&collection=journals&set_as_cursor=1&men_tab=srchresults. [Accessed: 4 May 2015].

against the primary register. Bareboat charterers might find the SASR attractive as a result of the amended Taxation Act.

CHAPTER 5 South Africa's maritime policy and legislative changes towards rebuilding of the ship register

5.1 Background

The South African maritime policy is currently in draft form. However, an indication of its likely final course can be found in the National Transport Policy, 1996 where it is expressed in broad statements aimed at achieving national objectives for all modes of transport. The need for a policy specific to the maritime industry cannot be overstated. It is needed to address problems and finding corrective measures in order to ensure that the national interest and national objectives are met.

The South African maritime industry has not received much attention in the recent past. As a result the industry has not grown in line with international norms, nor is it sensitive to economic and social imperatives. For instance, the conditions with regard to taxation, labour legislation and employment freedom are not favourable for ship ownership in South Africa. The lack of attention in the maritime industry has resulted in South Africa's shipping companies moving their head offices to other countries that provide more lucrative tax incentives. For instance, Grindrod Limited is the largest South African shipowner, with 42 owned or partly-owned ships, and has flagged out its ships to take advantage of more favourable conditions in other countries⁵⁶. This has resulted in a decline of the merchant ships registered in South Africa. The continued decline left the South African register with only 17 ships by 1994. In 2009, the only South African flagged merchant vessel *Safmarine Oranje* went to scrap, leaving the South African register with no commercial fleet ⁵⁷. South Africa has since had no merchant vessels on its register until the bad spell was broken in August 2015 when the first merchant vessel ⁵⁸ was registered.

With the above scenario in mind, it is clearly the aim of the South African government to rebuild a thriving merchant fleet. A healthy merchant fleet is seen as a key aspect and catalyst for job creation and economic development in South Africa's ocean economy. The Ocean Economy is defined as the economic activity, which indirectly or directly uses the ocean as an

⁵⁶ CAPE PORTS. 2015. South African Shipping Part 2 [Online], 30 November. Available at: <http://www.capeports.co.za/south-african-shipping-part-2/> [Accessed: 12 December.2015].

⁵⁷ Ibid.

⁵⁸ *Cape Orchid*

input⁵⁹. Major policy recommendations leading to the re-building of the SASR will now be analysed and critically discussed. These recommendations include the White Paper of 1996, Draft Maritime Policy of 2008 and the Green Paper of 2015. Thereafter the legislative changes that sought to enact these policies such as the SRA, 1998 and The Taxation Law Amendment Act, 2014 will be looked at. In addition, SAMSA, the body that was set up to administer the SASR as well as the task team appointed to enhance the SASR ships register known as Operation Phakisa will be examined.

5.2 Policy recommendations to enhance the SASR

5.2.1 National Transport Policy White Paper, 1996

As alluded to above, in August 1996, the South African government through the Department Of Transport (DOT) promulgated the National Transport Policy as part of its priority projects. The last meaningful analysis of transport policies in South Africa took place in the mid-1980s⁶⁰. The aim of the policy initiative, among other things, was to revisit policies that prevailed at the time which were viewed as fragmented and somewhat outdated⁶¹. The new policy was intended to formulate an integrated approach to national transport.

The new policy recognised that transport plays a strategic role in the social development and economic growth. It was highlighted in the policy that:

South Africa needs a modern ship register which is efficient, which balances the interest of the nation, ship-owners and seafarers in an internationally acceptable manner, and which accord with principles of international law relating the necessity of a “genuine link” between the state of the registry and the ship-owner. The register should be attractive to both local and foreign investors, but in no way a “flag of convenience”⁶².

This statement clearly demonstrates that one of the primary aims of the policy was to expand the South African merchant fleet. The policy emphasises interdepartmental government agencies and private initiatives to ensure the development of the SASR. Fiscal aspects, such as income tax paid by seamen, operators and shipowners, exchange controls and duties as well as the ranking of claims will therefore be reassessed with the view to change them where appropriate. Changes will be necessary in light of the fact that South African shipowners do

⁵⁹ Vega, A., Corless, R., Hynes, S. and O’Leary J. THE COASTAL AND OCEAN ECONOMY. *REDI*, 1. http://www.agresearch.teagasc.ie/rerc/CEDRA/REDI_Chapter8.pdf [Accessed: 15 December.2015].

⁶⁰ White Paper on National Transport 1996, p.3.

⁶¹ Ibid. p.68.

⁶² National Transport Policy White Paper, 1996.

not have the same competitive advantage that many foreign carriers have when participating on coastal trade. A South African coastal vessel operator would be reliant on the higher bunker prices in South Africa, which puts them at even more of a competitive disadvantage, as foreign carriers could bunker elsewhere at a better price. In order to protect coastal shipping on the Southern African countries to locally owned ships, it has been suggested that cabotage protection legislations should be investigated.

The policy highlights that South African bulk exports are carried on foreign-owned ships, and that research will be conducted to establish how other nations have successfully increased their market share in shipping their bulk exports on locally owned ships.

With regard to maritime safety and sea administration which is conducted by Port State Control, it was recognised that the department is inadequately staffed to handle the workload. There are also many outdated regulations that require updating or repeal. The White Paper was the first step for government to focus on these problems and engage with the industry in order to find solutions. The policy statement called for the creation of a maritime safety authority as an option to satisfactorily deal with revisions of legislations⁶³. This led to the birth of the South African Maritime Authority (SAMSA) in 1998.

5.2.2 Draft Maritime Transport Policy, 2008

In early 2005, the South African government established a working group through the DOT, called the South African Ships Register Advisory Group. This was created to identify obstacles which make the SASR uncompetitive, and to come up with solutions for this situation. The members of the South African Ships Register Advisory Group are the Department of Justice, the Department of Labour, the Department of Immigration, SAMSA, the Association of Shipping Lines, the Association of Ships Agents and Brokers of South Africa, the Container Liner Operators Forum and the Maritime Law Associations⁶⁴. It was identified that a national maritime policy in line with international standards would make shipowners sufficiently comfortable to consider flying the South African flag. To this end the Draft White Paper on South African Maritime Transport Policy was circulated in 2008. The ambitious goal set out in

⁶³ White Paper on National Transport 1996, p.69.

⁶⁴ Norton, T. 2011. Rebuilding the South African Flagged Fleet. *Nautical Institute Online*, 8 September. <http://www.nautinst.co.za/papers/norton.pdf> [Accessed: 08 June.2015].

the Maritime Transport Policy of 2008 was to become one of the world's top 35 maritime nations by 2014 through aggressive promotion of a SASR.

While the White Paper of 1996 only briefly touched on cabotage options, the White Paper of 2008 took a more drastic approach to encourage regimes to promote and protect South African shipowners.

It emphasises that domestic and regional inter-port cargo should be transported through coastal shipping, because it is more economical than transporting cargo by road ⁶⁵. However, regional and domestic cargo which is carried by sea is transported on foreign-owned vessels. It was therefore identified that the free trade area in the SADC and a number of bilateral trade agreements with most 'New Partnership for Africa's Development' (NEPAD) countries provides a platform for instating protectionism for an African-owned ship ⁶⁶.

The main objective of the policy is to ensure a level playing field for South African shipowners and operators as well as for foreign-owned vessels in order to attract both domestic and foreign investment ⁶⁷. In order to promote ship registration in South Africa, the policy identifies the following issues which needs to be attended to in order make the SASR competitive:

- Fiscal allowances and other developmental incentive and support given to industry by authorities;
- Security and facility afforded by the South African ship registration and mortgage provision on the Merchant Shipping Act 57 of 1951; and
- Cabotage and related policy regimes ⁶⁸.

One of the major policy statements is that the National Treasury will finalise the implementation of a tonnage tax regime in order to reduce the cost of doing business in South Africa. The first step in this direction was taken in July 2008, when the National Treasury circulated the South African Tonnage Tax Proposal for public comments. The proposal outlined concerns that South Africa's exports are transported on foreign-owned ships and that ships transporting South Africa's commodities create wealth for the country where the ship is

⁶⁵ Draft Maritime Transport Policy, 2008. Section 3.3.2.1.

⁶⁶ Ibid. Section 3.3.2.3.

⁶⁷ Ibid. Section 3.4.1.2.

⁶⁸ Ibid. Section 3.4.1.3.

registered. It therefore represents an opportunity cost for South Africa and justifies the intention of introducing a tonnage tax regime.

The proposed tonnage tax regime was based on the “Dutch Model”. This model essentially levies a fixed rate according to the size of the ship and days operated during an accounting period without taking into account the company’s business income ⁶⁹.

The proposal of the tonnage tax regime was the first major effort of the National Treasury to bring South Africa’s taxation law in line with standards in other countries. As previously noted, levying of tax is one of the fundamental reasons for a shipowner to choose the country of registration.

The policy highlights the problem of unfavourable ranking of mortgage claims in terms of the Admiralty Jurisdiction Regulation Act 105 of 1983 together with the choice of law applicable to ships’ mortgages. However, the policy fails to make any statement on how this problem can be resolved. Offshore lending has been identified as another problem. Because there is no local ship finance available in South Africa, there might be risk associated with the shortcomings of mortgage, inhibiting investment in this area.

Overall, the Maritime Transport Policy outlines the problem of why there are no ships flying the South African flag, but very little is offered regarding ways to counteract this problem. By 2014, the policy had failed to achieve its goal of South Africa becoming one of the world’s top 35⁷⁰ maritime nations as no merchant ship was yet flying the South African flag.

5.2.3 Green Paper on South African Maritime Transport Policy, 2015

The Green Paper is a policy document which aims to incorporate the mandate from the White Paper on National Transport Policy of 1996 by providing a framework for the development of the maritime transport sector. The policy considers the South African National Development Plan and recognises the stipulations under the African Union’s Maritime Transport charter. Moreover, the policy sees significant growth for South Africa through successful trade with its main trading partners.

⁶⁹ SOUTH AFRICA. DEPARTMENT: NATIONAL TREASURY. (2008) *Request for Public Comments – The South African Tonnage Tax Proposal*. [Online] 18 July. Available from: http://www.treasury.gov.za/comm_media/press/2008/2008071803.pdf. [Accessed: 15.09.2015].

⁷⁰ Draft Maritime Transport Policy, 2008. Section 3.4.4.1.

The policy highlights the financing hurdle that currently no commercial banks in South Africa offer industrial ship financing and insurance. Moreover, exchange control restrictions prohibit the granting of USD-denominated finances. Therefore it is factually impossible for a South African shipowning company to obtain equitable finance of a long-term nature to finance the acquisition of a ship. The policy states that the DOT, in collaboration with the Department of Trade and Industry and the National Treasury, will investigate the feasibility of and a possible model for establishing a national ship-financing capacity. In addition, it recommends that the National Treasury should consider lifting the exchange control restrictions with regard to ships' financing.⁷¹

South Africa's drive to carry its bulk exports was further analysed in a case study which established that an investment of between eight and ten billion rand would be needed in order for South Africa to carry less than 15 per cent of iron ore exports from South Africa to Beilun. The current oversupply of ships in the market and the uncertainty of the backhaul cargo would make it difficult for this venture to generate a profit. It is therefore seen as not commercially viable to acquire a national fleet in order to generate employment for seafarers and to ship South Africa's exports on a national fleet. Instead, the policy focuses on measures such as tonnage tax and removing other restrictive conditions in order to undertake a joint venture agreement with selected trading partners. This would require an agreement with players in the mining industry who would be committed to dedicate their cargo to South African-flagged vessels in order to achieve economies of scale.

The policy does not see a benefit for South Africa to participate in shipowning in the liner-shipping segment. Because the initial investment for South Africa to start-up a shipowning company would virtually be unaffordable. However, consideration is given to freight forwarding, and for entrepreneurs, to enter as a non-vessel-owning common carrier and issue their own bill of lading. Those South African liner cargos would still be carried on foreign owned vessels but the business transaction would be controlled by a South African company.

The ranking of mortgage claims after those of creditors supplying "ship necessities" seems to be an ongoing debate for which no solution could be suggested in the policy. The policy statement however underlines that the DOT will engage with the Department of Justice in order

⁷¹ Green Paper South African Maritime Transport Policy 2015. Item 60 Policy Statement on Financing for Shipping.

to remove this legal obstacle which is seen as a hindrance to the growth of ship acquisition in South Africa⁷².

The policy addresses the problem of shipping companies being taxed on the same basis as other South African industries versus a thriving maritime register allowing for a tonnage tax regime or levying no tax at all. However, this problem has been eliminated with the implementation of Act No. 43 of 2014: the Taxation Laws Amendment Act, 2014.

Grindrod Limited has been identified in the policy as the only South African-owned company which owned vessels. In 2012 it owned about 20 vessels, had 17 vessels on long-term charter and operated about 35 vessels through its subsidiaries Island View Shipping and Unicorn Shipping. The policy encourages the DOT and the Department of Mineral Resources to collaborate with South African-owned shipping companies in order to facilitate a new joint venture between mining houses and South African owned-shipping companies.

The policy suggests that the DOT undertake a feasibility study of selling South Africa's exports, in particular raw materials, on CIF terms in order to promote and develop the South African maritime industry. South Africa's exports are mainly sold FOB and therefore the country loses income from freight and insurance to foreign companies. To encourage selling on CIF terms will be a challenge for the industry, as the majority of South Africa's mineral exports are sold to China. China has immense power in the market and favours its own national shipping companies, which can supply shipping at a very low cost. A CIF policy therefore needs to be implemented which is likely to need subsidies from government to be able to compete with the Chinese market. Because China has greater buying power on ship space, it will be difficult to meet a CIF price which will not be too high for the purchaser, who may look for suppliers of raw material elsewhere.

Another key aspect is that the SASR is inefficiently administered. The long timeframe to process an application will not encourage shipowners to choose to fly the South African flag. The policy therefore suggests that the DOT should carry out a benchmarking study to compare practice of ship registration globally.

In conclusion, the policy identifies the need for a package to be established that will make the SASR attractive to international shipowners. Hence, it is far more likely that foreign investors will shift their flag than the ownership.

⁷² Ibid. Item 63. Policy Statement on mortgage ranking.

Policy recommendations such as the Green Paper 2015, White Paper 1996 and the Draft Maritime Policy of 2008 have been discussed above. The discussion will now shift towards legislative changes that came about in order to enact these policy recommendations.

5.3 Legislative changes to implement policy recommendations.

5.3.1 Ship Registration Act, 1998 (SRA)

One of the challenges taken up in the White Paper was the modernisation of the South African shipowner and registration policies. This resulted in the implementation of the SRA, No 58 of 1998 which updated the administration and law relating the SASR to the current international standard. It was acceded by parliament in 2003. The new Act removes the inflexible parochial approach of the 19th century and is based on modern English ship ownership law ⁷³. The SRA, 1996 allows for South African-owned ships and ships on bareboat charter to South African nationals to fly the South African flag ⁷⁴. The Act defines a “South African-owned ship” as follows:

- (b) any other ship, other than a fishing vessel, that—
 - (i) is wholly owned by one or more South African nationals;
 - (ii) is owned by three or more persons as joint owners of the ship, where the majority of those persons are South African nationals; or
 - (iii) is owned by two or more persons as owners in common, where the majority of the shares in the ship are owned by South African nationals ⁷⁵.

This section appears to be nationalistic as the majority of shares must be owned by South African nationals. However, upon examining who is a “South African national”, the requirement seems to be less strict. Hence a South African national is defined as follows, in section 1 of the Act:

- “South African national” means—
 - (a) a South African citizen in terms of the South African Citizenship Act, 1995 (Act No. 88 of 1995);
 - (b) a body corporate established in terms of a law of the Republic with a place of business in the Republic;
 - (c) a trust in which—
 - (i) the majority of trustees having the controlling power at any given time are South African nationals referred to in paragraphs (a) and (b); and
 - (ii) a majority of the beneficial interests are held by such South African

⁷³HARE, J. (2002) Maritime Law Update South Africa 2002. *Ports & Ships*. [Online] Available from: http://ports.co.za/legalnews/article_2002_12_31_0732.html. [Accessed: 20.09.2015].

⁷⁴ Ship Registration Act, 1998. Section 16(a)(b).

⁷⁵ Ship Registration Act, 1998. Section 1(4)(b).

nationals; and
(d) the Government of the Republic

Subsection (b) diminishes the requirements in section 4 which seemed to make the SASR a closed register. Hence it considers a body corporate with place of business in South Africa as a South African national⁷⁶. The Act therefore allows for foreign joint venture ownership of South African-registered vessels on condition that the majority of shares in the vessel are owned by South African nationals. The beneficial ownership of the vessel can therefore be located elsewhere, which gives the opportunity to foreign-owned companies to open a subsidiary office in South Africa for the pure purpose of registering any ship within the group in South Africa. The allowing of minority foreign ownership might infringe on the ITF requirements of a genuine link and could therefore make the South African register a FOC, the reason being that the link between the ownership of the vessel and the South African register is weak. It merely requires that the owner has a registered company with a place of business in South Africa. However, the SASR should not be regarded as a FOC, as South Africa is a member of the IMO and is committed to administer the register according to international standards.

However, the modernisation of the SRA did not attract any merchant vessels into the register. In the White Paper, 1996, the South African government identified that the development of a merchant fleet flying the South African flag holds great potential for economic growth. Therefore the SASR Advisory Group was formed to identify and remove impediments to the registration of ships in South Africa⁷⁷.

5.3.2 Taxation Laws Amendment Act, 2014 (Act No. 43 of 2014)

On 20 January 2015 the President assented to the Taxation Laws Amendment Act, 2014 (Act no. 43 of 2014). The approval of the Taxation Laws Amendment Act forms a milestone in the development of making the SASR competitive in that the international trend is to reduce taxation for shipping companies through tonnage tax or a total tax exemption. The taxation on the tonnage is calculated by measuring the tonnage of the ship and is not based on the company's profit, which essentially amounts to a smaller fee. In contrast, South African

⁷⁶ HELLENIC SHIPPING NEW. 2013. *South Africa: Creating an attractive Ship's Registry – the draft South African Maritime Policy*. [Online] 07.12.2013. Available at: <http://www.hellenicshippingnews.com/3ce0304b-f8bc-452a-815e-13d7cf9fc3c3/> [Accessed: 30 September 2015].

⁷⁷ Norton, T. 2011. Rebuilding the South African Flagged Fleet. *Nautical Institute Online*, 8 September. <http://www.nautinst.co.za/papers/norton.pdf> [Accessed: 08 June.2015].

shipping companies were subject to a corporate income tax rate of 28 per cent which makes the SASR uncompetitive and is cited as one of the main reasons why the SASR does not have merchant ships in its register⁷⁸. Against this background, government has assented to the Taxation Laws Amendment Act, 2014 to provide tax relief for international shipping companies⁷⁹. In order for a shipping company to qualify for this tax relief, the company must be a resident and hold at least one or more vessels which are designed for international transport of goods and passengers for reward and that are flagged in South Africa in terms of the SRA, 1998. One of the main changes of the Taxation Amendment Act is the amendment of section 9D of the Income Tax Act, 1962 to the effect that the receipt and accruals derived by the international shipping company from the operation of a South African ship will be exempt from income tax⁸⁰. However as a result of the capital gains and income tax exemption, the South African-flagged ship will no longer be depreciable. Furthermore, dividends paid by a qualifying shipping company will not be subject to dividend tax if the dividend is derived from the operation of the South African international transport ship. The international shipping company will be exempt from withholding tax on interest if the interest is paid to a foreign lender in respect of a debt used to fund the construction or improvement of the South African-flagged international transport ship. In addition to this, officers and crew are exempt from tax on their salaries, irrespective of the number of days spent abroad. The previous conditions for this exemption were that they had to be outside South Africa for more than 183 days⁸¹.

Legislative changes that were instituted to implement policy recommendations to rebuild the SASR such as the Taxation Laws Amendment Act 2014 and SRA 1998 have been addressed. The formation of SAMSA which was set up to administer the SASR will be looked at. In addition, the focus of Operation Phakisa on SASR as an economic growth point for South Africa will be discussed.

⁷⁸ Pinch, A. and Radloff W. 2013. Proposed changes to the South African international shipping tax regime. TaxManSA Online, 1 November. <http://taxmansa.co.za/proposed-south-african-international-shipping-tax-regime/> [accessed: 15 March.2016].

⁷⁹ Taxation Laws Amendment Act, 2014. Government Gazette, 20 January 2015. Available at: http://www.gov.za/sites/www.gov.za/files/38405_Act43of2014TaxLawsAmend_20Jan.pdf. [Accessed on: 03.06.2015].

⁸⁰ Taxation Law Amendment Act, 2014. Section 12(1)(b).

⁸¹ LEXISNEXIS. (2013) *Explanatory Memorandum on Taxation Laws Amendment Bill, 2013*. [Online] 24 October. Available from: <http://www.mylexisnexis.co.za.ezproxy.ukzn.ac.za:2048/Index.aspx>. [Accessed on: 03.06.2015].

5.4 The establishment of the South African Maritime Safety Authority (SAMSA)

As mentioned, the Port State Control was unable to fulfil its duties, which resulted in SAMSA being established on 1 April 1998 in terms of the SAMSA Act 5 of 1998.

The responsibility of SAMSA is to ensure that ships calling at South African ports are adequately operated and maintained. This is done by ensuring that all international regulations on safety, pollution prevention and the training certification on watchkeeping of crew are adhered to by the vessel operators. SAMSA will also be administrating the SASR.

While the main objective for shipowners is to save costs when choosing a flag state, the quality of the register and the adherence to the standard set by the IMO are also playing a vital role in this choice.

Together with the South African government, SAMSA has prioritised a programme of action to reverse the trend of a declining merchant fleet in South Africa since the mid-1990s.

5.5 Operation Phakisa

The breakthrough came with Operation Phakisa which is a “Big Fast Result Methodology”⁸² in which government aims to implement policies and programmes faster, better and more efficiently. The Presidency was introduced to this methodology during a state visit to Malaysia in 2013. With the support of the Malaysian government, South Africa adopted this methodology, which is a results-driven approach setting clear plans and targets with ongoing monitoring of progress and making these results public.

Operation Phakisa is designed to find solutions to address South Africa’s problems of poverty, inequality and unemployment among other challenges. Four critical areas were identified, one of which is the marine transport and manufacturing sector. A joint task team (called the MTM lab) from government, private sector, labour and academia has been formed to focus on the opportunity for South Africa to develop a maritime transport and manufacturing industry. This team has identified that a national ship registry for local ownership of merchant vessels is a key area of significant growth.

In order to rebuild the South African flag, the MTM lab wants to support the local registry through incentives and legislation using South African-flagged ships for cargo and coastal

⁸² DEPARTMENT: PLANNING, MONITORING AND EVALUATION REPUBLIC OF SOUTH AFRICA. *OPERATION PHAKISA*. Available from: <http://www.operationphakisa.gov.za/Pages/Home.aspx>. [Accessed: 08.08.2015].

operation based on UNCTAD and African Maritime Charter guidelines⁸³. The main focus will be on South African minerals of which 40 per cent will be allocated to South African-flagged ships and manned by South African seafarers. The MTM lab aims to finalise a cabotage policy to protect coastwise cargo which will include the supply and operation of offshore support vessels.

There have been several initiatives used by Operation Phakisa to establish partnerships with other shipping companies. On the opening day of Operation Phakisa⁸⁴ it was announced by the Presidency that the South African government and the South Korean bulk carrier *Polaris Shipping* had entered into a memorandum of understanding to establish a national shipping company. This memorandum involves that Polaris brings ships into South African waters and registering them under the SASR. It is apparently already planned that three vessels will go on the SASR⁸⁵. However, to date, not one Polaris-owned ship has been registered in South Africa.

5.6 Current developments

A breakthrough occurred on 20 August 2015 when Operation Phakisa delivered the first bulk carrier, the *Cape Orchid*, into the SASR– the first merchant vessel to be registered since 1985⁸⁶. Only a couple of weeks later followed the *Cape Enterprise*. The *Cape Orchid* and *Cape Enterprise* are owned by Vuka Marine which is a joint venture between a South African BEE-empowered company, K-Line Shipping and Pilipino Fairmont and is registered in Port Elizabeth. This is the first non-government South African-flagged ship which has taken local cadets on board in over a decade⁸⁷. It is important that the registration of the *Cape Orchid* and

⁸³ TRANSNET. 2015. *Operation Phakisa Presentation Invest in South Africa Ocean Economy Seminar 6-7 July, South Africa House London, United Kingdom*. [Online]. Available at: <http://www.fbicommunications.com/downloads/Transnet%20Operation%20Phakisa%20Invest%20in%20SA%20Seminar%20July%202015.pdf> [Accessed: 20.08.2015].

⁸⁴ OPERATION PHAKISA. 2014. *Open Day Operation Phakisa Maritime Transport and Manufacturing Posters, 2014*. [Online]. Available at: <http://www.operationphakisa.gov.za/operations/oel/mtm/Marine%20Transport%20Documents/Marine%20Manufacturing/Open%20Day%20Operation%20Phakisa%20Marine%20Transport%20and%20Manufacturing%20Posters%20%202014.pdf> [Accessed 08 June 2015].

⁸⁵ Cole, B. 2014. Shipping to grow thousands of jobs. *Daily News Online*, 16 October. <http://www.iol.co.za/dailynews/news/shipping-to-grow-thousands-of-jobs-1.1765813#.VPdTKPmUc8I> [Accessed: 03 March 2015].

⁸⁶ Wyngaardt van, M. 2015 Cape Orchid merchant vessel arrives in Saldanha for Kumba Iron Ore. *Engineering News Online*, 25 September. <http://www.engineeringnews.co.za/article/cape-orchid-merchant-vessel-arrives-in-saldanha-for-kumba-iron-ore-2015-09-25> [Accessed: 20 October 2015].

⁸⁷ ANGLO AMERICAN. 2015. *Meet the Cape Orchid*. [Online] Available at: <http://southafrica.angloamerican.com/our-stories/meet-the-cape-orchid.aspx> [Accessed: 02 October 2015].

Cape Enterprise are not an isolated matter, in order to drive job creation in the seafaring industry.

Although, to date, no restrictions are yet in place to protect shipping of South Africa's exports on South African-flagged ships, the *Cape Orchid* has sailed a laden voyage ex-Saldhana Bay in September, 2015. Norman Mabizima, the Chief Executive Officer, of Kumba Iron Ore, stated in an interview that he is proud of Anglo American and Kumba Iron Ore as the first customers of the *Cape Orchid*⁸⁸. It is strong partnerships such as these, between South African mining companies and South African shipowning companies, which will unlock further potential for the SASR to grow.

5.7 Conclusion

The assessment in this chapter shows that over the past two decades, several policies have been implemented with the aim of rebuilding the South African flag. Those policies often emphasise the same objectives but have done little to set these objectives into practice. However, the success shown with the registration of the *Cape Orchid* and *Cape Enterprise* shows that the most important aspect for the South African flag resurrection is cooperation between the government and the private sector. The door must remain open for foreign shipowners to register their fleets in South Africa. Alone, South Africa will not be able to add enough vessels to its register to ultimately change the market's behaviour of selling South Africa's exports FOB instead of CIF. It is therefore important that further initiatives are taken to promote the SASR in order for the *Cape Orchid* and *Cape Enterprise* not to remain an isolated case of success. The following chapter will analyse policies and protectionism measures practised in the Philippines, which ultimately led them to become a strong maritime nation.

⁸⁸ Ibid.

CHAPTER 6 Case study Philippines: The link between BCR and cargo reservation measures

6.1 Background

The South African government, through Operation Phakisa, aims to allocate 40 per cent of the country's minerals exports for shipment on the back of South African-flagged vessels as a way of stimulating the resurgence of the South African merchant fleet ⁸⁹. The question arises how this can be put into practice considering that currently there are only two merchant ships flying the South African flag. It may therefore be useful to look at the Philippine register, considering that they have been one of the pioneers of BCR in the 1970s. Furthermore, the Philippines' main exports are different from those of South Africa and restrictions on coastal trade therefore supported a somewhat different domestic maritime industry. After discussing in this chapter how the Philippine register works and the protections in place for the domestic shipping industry, the following chapter will analyse the feasibility of such measures and whether they would be practical in the South African context.

6.2 Brief overview of the Philippine maritime industry

UNCTAD's maritime review of 2014 ranks the Philippines as the 32nd maritime country among the top 35 registration flags ⁹⁰. The Philippines has two registers, namely the national register and the overseas register⁹¹. In the national register, only vessels which are wholly owned by Philippine nationals or corporations with place of business in the Philippines and controlled by Philippines citizens are included⁹². This is in contrast to the overseas register, which is mostly composed of bareboat chartered vessels. The term overseas register emanates from the Overseas Shipping Act 1955 which was subsequently amended by the Presidential Decree No. 866 which allows for the temporary registration of foreign-owned vessel under [time] charter or lease to Philippine nationals for use in the coastwise trade subject to certain

⁸⁹ SAMSA. (2015) *State of South Africa's Maritime Industry Transport Portfolio Committee*. [Online] 8 May. Available from: <http://pmg-assets.s3-website-eu-west-1.amazonaws.com/docs/120508sami-edit.pdf>. [Accessed: 12.12.2015].

⁹⁰ UNCTAD. (2014) *Review of Maritime Transport*. [Online] Available from: <http://unctad.org/en/pages/PublicationWebflyer.aspx?publicationid=1068>. [Accessed: 01.08.2015], p.45.

⁹¹ REPUBLIC OF THE PHILIPPINES. MARINA. *The Philippines: "Your Home Ship Registry"*. Available from: http://marina.gov.ph/overseas/oso_shipregistry_brochure.pdf. [Accessed: 01.12.2015].

⁹² MALALUAN, S. *An Analysis of Bareboat Chartering Program of the Philippines*. (Master thesis, World Maritime University, 1998).

conditions⁹³. Moreover, it allows the chartered vessel to be used in overseas trade subject to permission of the Maritime Industry Authority⁹⁴. A vessel in the overseas register enjoys the same privileges, rights and protection and is subject to the obligation and duties as a vessel under the national register⁹⁵. In 2013 the national merchant fleet consisted of 9,573 vessels of 1,578,508⁹⁶ gross registered tonnage (GRT) excluding fishing vessels. The Philippine overseas registry (or BCR) consisted of 116 vessels of 2,940,804⁹⁷ gross registered tonnage with an average age of 11 years⁹⁸. The large amount of registered vessel under the national register results from the vast amount of passenger vessels which got a small GRT. Whereas about 60 per cent of the total overseas registered fleets consists of bulk carriers and general cargo ships. Therefore the overseas register supersedes the national register in terms of GRT. Overseas shipping companies contributed about Philippine Peso (PHP) 60 million (about USD 1.3 million) for 4.5 per cent withholding tax to the Bureau of Internal Revenue and PHP 8.2 million (about USD 179,000) in fees to Maritime Industry Authority (MARINA)⁹⁹. MARINA administers the Philippine ship registers. It regularly upgrades and updates standards on safety, level of service and environmental sustainability in order to keep on par with international standards and practice through strict implementation and enforcement. Furthermore, MARINA is engaged with the assessment and ratification of international conventions which are enforced by way of MARINA circulars.

6.3 Policy on BCR in the Philippines

BCR in the Philippines is governed by the Philippines' Presidential Decree No. 760 which was issued in 1975, which marks the point of inception of BCR in the Philippines. However, at that time, it was limited to temporary registration of foreign-owned ships to Pilipino nationals. For this purpose, Pilipino nationals were citizens or corporations established under the legislation of the Philippines, of which 60 per cent of beneficial owners needed to be Pilipino nationals.

⁹³ Philippine: Presidential Decree No. 760. Section 1.

⁹⁴ Philippine: Presidential Decree No. 760. Section 2.

⁹⁵ MALALUAN, S. *An Analysis of Bareboat Chartering Program of the Philippines*. (Master thesis, World Maritime University, 1998), p. 10.

⁹⁶ REPUBLIC OF THE PHILIPPINES. PHILIPPINE STATISTIC AUTHORITY. (2013) 2013 PY Transportation Statistic. Available from: <https://psa.gov.ph/content/transportation>. [Accessed: 26.06.2015].

⁹⁷ Ibid.

⁹⁸ THE PHILIPPINE MARITIME INDUSTRY: PROSPECTS AND CHALLENGES IN 2013 AND BEYOND. Available at: http://marina.gov.ph/reports/other_reports/Philippine%20Maritime%20Industry.Prospects%20and%20Challenges.pdf. [Accessed: 08.08.2015].

⁹⁹ Ibid.

The vessel had to be manned with Pilipino crew and could only be engaged in domestic trade. However, in 1990 the period of charter under BRC was limited to not more than five years.¹⁰⁰. Initially, the reason behind this initiative was to provide an alternative means of ship acquisition to replace the uneconomical and aging fleet to counter the lack of available financing¹⁰¹.

In 1976 Presidential Decree No. 760 was amended by Presidential Decree No. 866, allowing the use of foreign-owned vessels in overseas trade. The latter decree was issued because the Philippine government recognised the need to expand their legal framework in order to modernise the overseas fleet and to increase foreign exchange earnings and maritime employment. Initially BCR was only allowed until 1990, but this was extended until 1999 through Presidential Decree No. 1771. In September 1997 a further extension was granted until 2009¹⁰². Finally in 2007 time constraints were lifted, which made the lease effective indefinitely¹⁰³. These time limits caused a decrease in the bareboat chartered fleet of seven per cent from 2000 to 2007. The register did not provide security for the charterer because the programme's life was always dependent on the political will of the government in power.

The registration process to bareboat-charter a ship in the domestic register was extremely slow, taking up to 52 working days to complete. According to a recent study by the World Bank International Finance Corporation, waiting time costs the shipping companies about PHP 700,000 (about USD 15,281)¹⁰⁴ daily and lost opportunities of about PHP 30 million (about USD 600,000) per ship. This is a considerable drawback for shipowners or bareboat charterers who intended to register their fleet in the Philippines given that the international norm for this kind of registration is one day.

As a means of redress the Philippines introduced Special Processing Window/Express Lane (SPWEL)¹⁰⁵ through MARINA. This was pilot-tested in February 2014. SPWEL is a two-stage processing window/lane for application of bareboat charter ships for use in domestic shipping in the Philippine register¹⁰⁶, which aims to cut the processing time to nine working days. This

¹⁰⁰ Philippine: Presidential Decree No. 760, Section 1.

¹⁰¹ MALALUAN, S. *An Analysis of Bareboat Chartering Program of the Philippines*. (Master thesis, World Maritime University, 1998).

¹⁰² Philippine: Executive Order No. 438.

¹⁰³ Philippine: Executive Order No. 667.

¹⁰⁴ Based on a rate of exchange of 0.022 as at 9 August 2015.

¹⁰⁵ Philippine: MARINA No. 2014-02.

¹⁰⁶ Pablo, R. 2015. MARINA sets up permanent fast lane for vessel import permits. *Portcalls Asia Online*, 4 January. <http://www.portcalls.com/marina-sets-up-permanent-fast-lane-for-vessel-import-permits/> [Accessed: 08 August 2015].

will come with a cost to the applicant as the processing fees of SPWEL are 20 per cent more than the prescribed fees ¹⁰⁷.

6.4 Cabotage restriction of the Philippines

The cabotage law in the Philippine restricts the maritime transportation of goods and passengers to Philippine registered vessels¹⁰⁸. Cabotage restrictions are often seen by the exporters and importers as trade barriers, because they deprive these operators from access to a cheaper freight rate which could be achieved in an open market. However, the protection of domestic trade has a huge impact for the Philippine economy. The 2012 gross value added to the maritime transport industry was 0.24 per cent of the gross domestic product ¹⁰⁹. This was achieved as a result of the largely domestically operated fleet, as shown in Table 1 below, extracted from the Philippine Statistics Authority. It shows that cargo-carrying vessels have the highest share in gross-tonnage and account for 55 per cent of the total. The total amount of domestic cargo throughput was 77,961,028 metric ton in 2013 ¹¹⁰. If this cargo had been transported on foreign-registered vessels, it would have compromised the contribution to the gross domestic product.

Table 1: Number and Tonnage of Domestics Operating Merchant Fleet 2013

	Number	Gross Tonnage
Passenger	5,734	454,879
Cargo	2,813	1,466,964
Tanker	245	240,329
Special purpose ship	20	1,610
Miscellaneous ship	63	20,185
Other and tug, dredger, yacht	699	83,568
TOTAL MERCHANT FLEET	9,574	2,267,475

Source: Philippine Statistic Authority (2013) ¹¹¹

¹⁰⁷ Ibid

¹⁰⁸ Raul, J. 2013. Review of Cabotage Law. *Inquirer.Net Online*, 3 March. <http://business.inquirer.net/134599/review-of-cabotage-law> [Accessed: 21 December 2015].

¹⁰⁹ Llanto, M. and Navarro, M. 2012. Relaxing the Cabotage Restrictions in Maritime Transport. *Philippine Institute for Development Studies*. <http://www.pids.gov.ph/files/outreach/Llanto-Navarro-Cabotage.pdf> [Accessed: 26 July 2015].

¹¹⁰ REPUBLIC OF THE PHILIPPINES. PHILIPPINE STATISTIC AUTHORITY. (2013) 2013 PY Transportation Statistic. Available from: <https://psa.gov.ph/content/transportation>. [Accessed: 26.06.2015].

¹¹¹ Ibid.

6.5 Cabotage policy in the Philippines

The cabotage principle in the Philippines is linked to the Jones Act of 1920 ¹¹² which was adopted when the Philippines were still under colonial control of the US. The cabotage restrictions in the Philippines are governed by two laws, namely the Republic Act 1937 ¹¹³ (otherwise known as the Tariff and Customs Code of the Philippines) and the Republic Act 9295 (otherwise known as the Domestic Shipping Development Act of 2004).

The Republic Act 1937 translates the cabotage principle into law under the provisions quoted below, which stipulate that the basic requirements for a vessel to engage in coastal trade are that it must hold a Certificate of Philippine Registry and a licence issued annually.

Section 810: A Certificate of the Philippine registry confers upon the vessel the right to engage, consistently with law, in the Philippine coastwise trade...

Section 902: The right to engage in the Philippine coastwise trade is limited to vessels carrying a Certificate of the Philippine registry; and

Section 903: All vessels engaging in coastwise trade must be duly licensed annually ¹¹⁴.

The undermentioned quotation from section 1009 of Republic Act 1937 liberalises the cabotage restriction by allowing foreign vessels to engage in coastwise trans-shipment or transport of passengers if they are going to be exported or imported from the Philippines:

Section 1009: Clearance of Foreign Vessels To and From Coastwise Ports — Passengers or articles arriving from abroad upon a foreign vessel may be carried by the same vessel through any port of entry to the port of destination in the Philippines or articles intended for export may be carried in a foreign vessel through a Philippine port. Upon such reasonable condition as he may impose, the Commissioner [of Customs] may clear foreign vessels for any port and authorize the conveyance therein of either articles or passengers brought from abroad upon such vessels; and he may likewise, upon such conditions as he may impose, allow a foreign vessel to take cargo and passengers at any port and convey the same, upon such vessel to a foreign port.

¹¹² Section 27 of the Jones Act deals with cabotage and requires that all goods transported by water between US ports be carried on US flagships.

¹¹³ Sections 810, 902, 903 and 1009 of the Republic Act 1937 restrict the operation of foreign vessels on domestic trade routes.

¹¹⁴ Philippines: Republic Act 1937.

In 1997 however, the Department of Justice held that this provision may not be construed as authority to allow a foreign vessel to engage in domestic trade, even if the final destination for the cargo was outside the Philippines ¹¹⁵.

In 2004 cabotage provisions were further deregulated by signing the Republic Act 9295 into law. It introduced reforms such as liberalising passenger rates, introducing incentives to modernise the domestic fleet, ship safety standards, ship classification and compulsory insurance coverage of passengers and cargos. However, the law reiterated and strengthened the cabotage restrictions in Sections 5 and 6 of Chapter 3 of the Republic Act 9295 ¹¹⁶ as follows:

Section 5: Authority to operate — No franchise, certificate, or any other form of authorization for the carriage of cargo or passenger, or both, in the domestic trade, shall be granted except to domestic shipowners or operators.

Section 6: Foreign Vessels Engaged in Trade and Commerce in Philippine Territorial Waters — No foreign vessels shall be allowed to transport passengers or cargo between ports or places within the Philippine territorial waters, except upon the grant of Special Permit by the MARINA when no domestic vessel is available or suitable to provide the needed shipping service and public interest warrants the same.

Although Section 6 relaxed the cabotage restriction in special circumstances by issuing special permits, this largely depended on the discretion of the acting bureaucrats. Section 6 therefore created uncertainty in the shipping industry since although bureaucrats had the power to support liberalisation, they simultaneously had the power to frustrate it ¹¹⁷.

6.6 Impact of cabotage restriction in the Philippines on shipping costs

Llanto and Navarro (2012) analyse the impact of cabotage restriction in the Philippines. They initially draw attention to the very high cost of the domestic shipping service. According to an advocacy paper of the Joint Foreign Chambers of Commerce in the Philippines, the cost to ship a container on the domestic service from Manila to Cagayan de Ora was 43 per cent higher than to ship a container from Manila to Cagayan de Oro via Kaohsiung on a foreign service¹¹⁸. The reason for the high cost was the lack of competition which weakened the incentive to

¹¹⁵ Llanto, M. and Navarro, M. 2012. Relaxing the Cabotage Restrictions in Maritime Transport. *Philippine Institute for Development Studies*. <http://www.pids.gov.ph/files/outreach/Llanto-Navarro-Cabotage.pdf> [Accessed: 26 July 2015].

¹¹⁶ Ibid.

¹¹⁷ REPUBLIC OF THE PHILIPPINES. PHILIPPINE STATISTIC AUTHORITY. (2013) 2013 PY Transportation Statistic. Available from: <https://psa.gov.ph/content/transportation>. [Accessed: 26.06.2015].

¹¹⁸ Llanto, M. and Navarro, M. 2012. Relaxing the Cabotage Restrictions in Maritime Transport. *Philippine Institute for Development Studies*. <http://www.pids.gov.ph/files/outreach/Llanto-Navarro-Cabotage.pdf> [Accessed: 26 July 2015].

modernise the fleet. In the case of the Philippines, this has resulted in an aged domestic fleet with an average age of 18 to 20 years, while smaller vessels being used increase the turnaround time and therefore the cost per tonne-mile ¹¹⁹.

The lifting of cabotage restrictions in the Philippines has been topical for over a decade. The lack of competitiveness of the domestic maritime service makes it harder for exporters to compete internationally and is therefore hindering economic progress ¹²⁰. Although Republic Act 9295 offers incentives to shipping companies to modernise their fleets, since the Act's inception in 2004 there has been no change and the domestic fleet remains outdated. Nevertheless, cabotage restriction is the backbone of the merchant fleet under the Pilipino register and has generated employment for thousands of Pilipino, not just as seafarers but also in ancillary industries. There is great concern that strong competition might bring local operators to the ground which could result in closure of Pilipino shipping companies and loss of employment. In this regard MARINA refers to the disaster when Indonesia allowed local foreigners to engage in coastwise transportation, which nearly led to the collapse of the local shipping industry. The Indonesian government had to avert the effect by immediately restoring the restrictions ¹²¹.

6.7 Current development

On 21 July 2015, the Philippine government approved Republic Act 10668. This Act allows foreign vessels to transport and co-load foreign cargo's for domestic trans-shipment and other purposes ¹²². This turn of events is important for Philippine exporters in the mining sector to compete in international trade. The majority of nickel mines are based on the Southern Island while the only port at which foreign carriers are allowed to call is on the Northern Island. In practice, a foreign bulk carrier can now call at Cagayan de Oro directly in order for the exporter to avoid trans-shipment cost.

In the signing ceremony in Malacanang, President Aquino stated that:

allowing foreign vessels from a port outside the Philippines to carry cargo to their domestic port of final destination will make the export and import of products faster and cheaper and

¹¹⁹ Ibid.

¹²⁰ THE MANILA TIMES. (2015) *Embrace open seas policy, relax cabotage*. [Online] 10 June. Available from: <http://www.manilatimes.net/embrace-open-seas-policy-relax-cabotage/190931/>. [Accessed: 26.06.2015].

¹²¹ Palabirca, R. 2013. Review of Cabotage Law. *INQUIRER.net. Online*, 26 July. <http://business.inquirer.net/134599/review-of-cabotage-law>. [Accessed: 26 July.2015].

¹²² Philippines: Republic Act 10668.

lead to a more vibrant market. Stakeholder from consumer to businessmen, will be able to save money ¹²³.

Previously foreign ships were only allowed to export or import cargo from the port of Manila which is heavily congested. As an added benefit, the new liberalised cabotage regime will therefore ease the congestion in Manila and enhance the economic activity in other areas. There are concerns from the local shipping industry that they will not be able to compete with foreign carriers and that the Philippines may risk losing its domestic fleet. In 2014 Primo Rivera¹²⁴ was quoted in an article in which he outlined that domestic shipping is subject to numerous taxes such as a dry-docking tax of 12 per cent, corporate income tax of 12 per cent and value-added tax of 12 per cent, whereas foreign shipping lines are only subject to three per cent common carriers' tax and 2.5 per cent gross billing tax ¹²⁵. Rivera predictions are that domestic shipping lines will now register their fleets in other jurisdictions in order to enjoy the same benefits. Moreover, the lifting of cabotage will increase the dependency on foreign companies which imposes a considerable drain on the balance of payments. It was already weakened when the Philippines government opened the waters to ships based in the other BIMP-EAGA¹²⁶ countries in 2000 ¹²⁷. The knock-on effect of lifting cabotage will therefore have unforeseeable consequences for the Philippine economy.

6.8 Conclusion

Like South Africa, the Philippines is one of the world's richly endowed countries in terms of mineral resources, which are predominantly exported in bulk carriers¹²⁸. Therefore it is unsurprising that the majority of the fleet under BCR in the Philippines consists of bulk carriers. One of the benefits of BCR is the ability of the charter to participate in cabotage and domestic

¹²³ PHILIPPINE DAILY INQUIRER. (2015) *Key shipping reform*. [Online] 28 July Available from: <http://www.investphilippines.info/arangkada/key-shipping-reform/>. [Accessed: 07.08.2015].

¹²⁴ Primo Rivera is the Philippine Interisland Shipping Association President.

¹²⁵ Almonte, L. 2014. Lifting of cabotage to kill PH shipping industry, say local liners. *PortCalls Asia Online*, 12 January. <http://www.portcalls.com/lifting-of-cabotage-to-kill-ph-shipping-industry-say-local-liners/#> [Accessed: 07 August 2015].

¹²⁶ Brunei-Indonesia-Malaysia-Philippines East-Asian Growth Area.

¹²⁷ Krinks, P. 2002. *The Economy of the Philippines: Elites, Inequalities and Economic Restructuring*. [Online]. London: Routledge. Available at: https://books.google.co.za/books?id=wm2IAgAAQBAJ&pg=PA205&lpg=PA205&dq=philippines+easier+registration+of+bareboat+chartered+fleet&source=bl&ots=wt4qhvdCQ_&sig=un2Li8F-r8Sn00x0r1yah7UZnIo&hl=en&sa=X&ved=0CD8Q6AEwB2oVChMIqKw492WxwIVgZYUCh3bkgPu#v=onepage&q=bareboat&f=false [Accessed: 07 August 2015].

¹²⁸ REPUBLIC OF THE PHILIPPINES. PHILIPPINE STATISTIC AUTHORITY. Philippine Economic-Environmental and Natural Resources Accounting. Available from: <http://nap.psa.gov.ph/peenra/results/mineral/default.asp>. [Accessed: 22.12.2015].

trade. This means that a bareboat-chartered vessel enjoys the same benefits and privileges as a locally registered vessel. This scenario is unlikely to continue into the future as liberalisation of cabotage law has opened Philippine waters to foreign-owned vessels. The current environment is globalised and is one in which open market practices benefit the consumer the most. In the case of the consumer of shipping services, the exporter can now export her cargo for less on a foreign-owned vessel. The question therefore arises whether the drive of the MARINA to make registration in the Philippines easier was in fact in vain. For most bareboat charterers, the need to register their fleets in the Philippines will likely fall away. This in turn will mean a significant decrease in tonnage and an accompanying decrease in the collection of tonnage tax and registration itself. It is still too early to analyse the outcome of this liberalisation of cabotage law in the Philippines. Such consideration goes beyond the scope of this thesis. However, the next chapter addresses the following questions. How is South Africa going to increase its merchant fleet? How will it achieve its goal of exporting 40 per cent of South Africa's minerals on South African-flagged ships? Is it feasible for South Africa to consider cabotage as an option considering the problems accorded in the Philippines?

CHAPTER 7 The Philippines model and its application in the South African context

7.1 Background

The assistance of governments to the maritime industry is not a new phenomenon and is common practice in most maritime nations¹²⁹. Maritime subsidies date back to the 17th and 18th centuries, when a strong merchant fleet meant a lot of boats that could be commandeered by government during times of war. In the 1830s, the British Crown granted lucrative contracts for postal deliveries, which benefited Britain's Cunard lines¹³⁰. In the early 1900s, both America and Japan offered easy finance to national shipowners in form of cut-price government loans¹³¹. Currently, shipping subsidies are used for their knock-on effect on industry as a whole rather than for military reasons. The preceding chapter examined how the Philippines became a strong maritime nation, mainly through the assistance of government subsidies and protectionism policies. This chapter will discuss whether similar measures are a way for South Africa to rebuild its merchant fleet. Therefore this chapter examines whether state intervention measures adopted in the Philippines are likely to succeed in South Africa.

7.2 Financial aid

The most frequently offered aid by maritime nations to develop and maintain their merchant fleet is in the form of government loans for the building of new vessels. These grants are beneficial to a local economy if the ship is built in the country. Ship building is a labour-intensive task not only for the shipyards but also for suppliers providing the shipyards. For instance, China's policy provides for protection of the construction of ships and expansion of shipyards through subsidies, resulting in Chinese ships costing on average about 7.3 per cent less than China's rivals¹³². However, for South Africa, such a capital intensive venture will be difficult to finance considering that South Africa's interest rate¹³³ is extremely high compared

¹²⁹ THE ECONOMIST. 2015. *Tilted Maritime*. [Online] 9 August. Available at: <http://www.economist.com/news/finance-and-economics/21611109-new-techniques-show-damage-done-subsidies-heart-global> [Accessed: 19 October 2015].

¹³⁰ Ibid.

¹³¹ Ibid.

¹³² THE ECONOMIST. 2015. *Tilted Maritime*. [Online] 9 August. Available at: <http://www.economist.com/news/finance-and-economics/21611109-new-techniques-show-damage-done-subsidies-heart-global> [Accessed: 19 October 2015].

¹³³ Prime lending rate is 9.5 per cent as at 15 October 2015.

to interest rates of traditional maritime countries. This combined with the exchange control restriction and unavailability of South African financing institutions makes it difficult for a prospective South African shipowner to acquire a vessel in South Africa. Therefore this option does not seem to be feasible for South Africa.

7.3 Cargo reservation and export inducement policies

The South African policies, as reflected in the Green Paper of 2015, emphasise that South Africa must control its exports and that these must be shipped on South African-registered vessels. The *Cape Orchid* is the first merchant vessel flying the South African flag under BCR. More vessels are expected to join the flag as BRC registrations. In order to protect the young merchant fleet and to encourage new entrants, the policies have emphasised that vessels flying the South African flag must be protected and that there must be an incentive for vessel owners to choose the South African flag.

As indicated in the previous chapters which looked at state intervention in the Philippine maritime economy, there are several different methods for the state to intervene in order to develop a national merchant fleet. This can be done through restrictive measures in international shipping – also referred to as “flag discrimination”¹³⁴. Flag discrimination can be defined as an intervention by the government to restrict the freedom of trade to choose the vessel on which cargo may be carried¹³⁵. This can be achieved through cargo reservation laws. Cargo reservation requires that part of the country’s exports must be transported only on ships flying the national flag. It can be imposed unilaterally, if national ships are given exclusive rights to carry cargo passing through the country’s ports, or on the basis of bilateral or multilateral agreements through cargo-sharing agreements with partner countries¹³⁶. The latter involves the government of two or more countries which may decide that each national fleet is granted a significant amount of cargo arising from common trade¹³⁷. For South Africa, a prospective partner would be China as most of South Africa’s mineral exports are transported

¹³⁴ Ademuni-Odeke. 1984. *Protectionism and the Future of International Shipping*. Dordrecht: Martinus Nijhoff Publishers, 103.

¹³⁵ Ibid.

¹³⁶ Fink, C. 2002. Trade in International Maritime Services: How Much Does Policy Matter? *The World Bank Economic Review*. <http://wber.oxfordjournals.org/content/16/1/81.short> [Accessed: 15 March 2016].

¹³⁷ Sübidey, T. 2010. *Economic Liberalization and Turkey*. [Online]. London: Routledge. Available at: <https://books.google.co.za/books?id=OSLJBQAAQBAJ&printsec=frontcover&dq=S%C3%BCbidey+togan&hl=en&sa=X&ved=0CBoQ6AEwAGoVChMI2orNkdHJyAIVCVgUCh0QvwrmR#v=onepage&q=S%C3%BCbidey%20togan&f=false> [Accessed: 17 October 2015].

to China. The South African government has several strategic agreements signed with China which aim to strengthen bilateral relations and trade cooperation to create sustainable investment opportunities for both countries. However, considering that China is shipping South Africa's exports on Chinese-owned ships, there needs to be a strong cost incentive for the Chinese importer to forego the opportunity to transport on Chinese-flagged vessels. Incentives therefore need to be offered that the purchase price will be lower if the cargo is shipped on South African-flagged vessels. This could be achieved through state aid for ocean-born trade in order to protect and develop South Africa's merchant fleet while it is in an infant stage.

One of the most effective ways to assist the promotion of foreign trade on South African-flagged vessels is through incentives and/or inducements¹³⁸. These mechanisms were used in the Philippines through Presidential Decree No. 806 of 3 October 1975. The legislation states that government shall take all necessary steps, including provision of direct incentive to Philippine flag vessels and nation shipping lines, in order to ensure that they carry a substantial amount of Philippine exports. Moreover, the legislation states that Philippine-owned or controlled vessels, or chartered national vessels must have at least equal shares of cargo transported in international trade between the Philippines and another country. Nevertheless, if Philippine-flagged vessels cannot carry the cargo, then the opportunity will be given firstly to carry the balance of the cargo to shipping lines with which the country has a bilateral trade agreement.

Such legislation would not be beneficial for South Africa in the short term as South Africa firstly needs to establish a merchant fleet. With only two vessels¹³⁹ in its register, it would be impossible to enforce 50 per cent of its exports on South African-flagged vessels. However, in the long run, after more owners follow suit, it might be worth considering cargo reservation measures.

In addition to its cargo reservation laws, the Philippines government has also introduced substantial tax incentives. Philippines exporters are able to deduct 150 per cent of overseas freight expenses and charges incurred in the Philippine ports from their taxable income provided that the cargo is carried on Philippine-flagged vessels¹⁴⁰.

¹³⁸ Ademuni-Odeke. 1984. *Protectionism and the Future of International Shipping*. Dordrecht: Martinus Nijhoff Publishers, 103.

¹³⁹ *Cape Orchid* and *Cape Enterprise*

¹⁴⁰ Philippines: Presidential Decree No. 667, 5 March 1975.

Similar tax incentives would be beneficial to stimulate the growth of a South African merchant fleet. The exporter would be able to reduce the product price if the cargo would be carried on South African-flagged vessels, taking into consideration the tax benefit. Thus the predominately Chinese importer, who currently controls the choice of carrier for South Africa's mineral exports, will see the benefit of choosing a South African flagged vessel. Moreover, this will enable the South African exporter to consider selling the product on CIF terms instead of FOB terms which will in turn benefit South Africa in that the freight revenue is not lost to a foreign country. Therefore implementation of flag discrimination and preference seem especially needed if South Africa seeks to counter the effects of importing South Africa's products on FOB terms.

7.4 Cabotage restrictions

Cabotage restrictions have been adopted by the Philippines through the Republic Act of 1937¹⁴¹ and the Domestic Shipping Development Act of 2004. Cabotage restrictions have been part of contemporary maritime discourse in South Africa and the African Continent as a whole with a running theme aimed at protecting the local merchant fleet. South Africa's policies have already emphasized the further exploration of cabotage options for further policy implementation. This discourse comes in various form, but more noticeable is the African Maritime Transport Charter, 2012. The Charter advocate for the development of an African fleet through the establishment of a regional and continental cabotage regime. The Charter contains a clause which states that: "The establishment of national and regional maritime cabotage shipping lines should be encouraged in order to promote intra-Africa trade and facilitate the economics and socio-economic integration of the continent".

The Green Paper, 2015 recognises the African Maritime Transporter Charter. It suggests possible cabotage options will not only be considered by the South Africa government for South Africa's coastal waters, but also for the African continent as a whole.

To have cabotage restrictions limited to South African coastal waters would most likely not be feasible, as economies of scale would not be achieved to have a fully laden service between South African ports¹⁴². However, if cabotage restrictions are applied across the African

¹⁴¹ Section 810, 902, 903 and 1009 restrict the operation of foreign vessels on domestic trade routes.

¹⁴² SOUTH AFRICA. DEPARTMENT OF TRANSPORT. (2011) *Part 4: Proposal and Recommendations*. [Online] 28 July. P. 18. Available from: http://www.transport.gov.za/Portals/0/Maritime/Part%204_Final_280711yf.pdf. [Accessed: 20.10.2015].

continent, then on certain trade lanes, economies of scale would be achieved and would make a merchant fleet owned by individual African countries viable. For South Africa, this will pertain in particular to the coastal and trans-shipment trade to the east and west coasts of Southern Africa. Many imports from China are trans-shipped in South Africa with final destinations in Tanzania, Kenya, Mozambique, Namibia and Angola. However, the challenges faced on these routes are that the majority of cargo is containerised and the routes are predominantly controlled by foreign liner shipping operators¹⁴³. It may therefore be difficult to compete with these multinationals as the cost of acquiring and maintaining ships will be very high. It was identified in the South Africa Maritime Industry Conference of 2012 that coastal countries on the African continent should dedicate a specialised fund for coastal shipping operators at a subsidised rate to allow for cabotage¹⁴⁴. Moreover, the Conference also proposed that the African Union (AU) should adopt cabotage laws such as the Jones Law whereby 40 per cent of all cargos carried in the US are allocated to US ships.

However, restricting Africa's coastal trade to African-owned vessels will move away from the international trend in liberalising trade in order to provide a more cost-efficient trade. Research by the World Economic Forum has concluded that cabotage restrictions damage the local economy and burden business and consumers with significant cost owing to the lack of competition and which forces international import/export businesses to use high-cost logistics suppliers with inefficient trans-shipment operations¹⁴⁵. The danger with cabotage restrictions on the African continent, in particular for South Africa, is that the cargo owner might divert to different routes and trans-ship the cargo outside Africa in order to avoid cabotage restriction. South Africa is a trans-shipment hub for its neighbouring countries and the port facilities would face a significant decline of cargo if trans-shipments were to fall away. As noted in the Philippine case study, this could result in cargo owners looking for different trade routes with higher productivity and greater cost efficiencies¹⁴⁶. Moreover, Liner Shipping Companies would not give away this trade either, if they were not allowed to trade along the African

¹⁴³ SOUTH AFRICA. SAMSA. (2012) *Coastal Shipping in Africa: Prospects & Challenges*. Cape Town: SAMIC 6 July. Available from: <http://www.samsa.org.za/sites/samsa.org.za/files/COASTAL%20SHIPPING%20IN%20AFRICA-Admaral%20Ombo.pdf>. [Accessed at: 21.10.2015].

¹⁴⁴ SOUTH AFRICA MARITIME INDUSTRY CONFERENCE. (2012) *Delivering on South Africa's Maritime Agenda – A Call for Action*. [Online] Available from: http://samic.samsa.org.za/sites/samic.samsa.org.za/files/samic_report_final.pdf. [Accessed: 24.11.2015].

¹⁴⁵ Marle van, G. 2013. Africa presses for cabotage laws despite Davos warning. *The Load Star Online*, 02 June. <http://theloadstar.co.uk/africa-presses-for-cabotage-laws-despite-davos-warning/> [Accessed: 22 October 2015].

¹⁴⁶ Llanto, M. and Navarro, M. 2012. Relaxing the Cabotage Restrictions in Maritime Transport. *Philippine Institute for Development Studies*. <http://www.pids.gov.ph/files/outreach/Llanto-Navarro-Cabotage.pdf> [Accessed: 26 July 2015].

continent. As a result, they might consider calling certain African ports directly, in particular from China to the east coast of Africa, in order to avoid the cabotage restriction¹⁴⁷. Therefore, cargo which is currently routed along the African coast might fall away and with it, the revenue earned at the trans-shipment ports.

7.5 Conclusion

At this stage, subsidies for ship-building and financing might not be achievable for South Africa owing to the high interest rate and the fact that there are no South African financiers specialising in shipping finance¹⁴⁸. Nor does it appear that cabotage restrictions are a feasible option for South Africa. The implementation of cabotage laws in Southern Africa may work to the detriment of South Africa's trade. Firstly, owing to the high cost of acquiring a liner service and secondly because trans-shipment trade would most likely opt for a different route if the coastal trade was not cost-efficient. Therefore cabotage restrictions as they have been implemented in the Philippines seem not to be an advisable strategy for South Africa to adopt.

The most feasible option to encourage the growth of a South African merchant fleet seems to be through cargo restrictions and incentives for the mineral cargo shipped on South African-flagged vessels. This might encourage South African bulk carriers currently registered under different flags to return to the South African flag.

¹⁴⁷ SOUTH AFRICA. DEPARTMENT OF TRANSPORT. (2011) *Part 4: Proposal and Recommendations*. [Online] 28 July. P. 16. Available from: http://www.transport.gov.za/Portals/0/Maritime/Part%204_Final_280711yf.pdf. [Accessed: 20.10.2015].

¹⁴⁸ Green Paper 2015, Section 54.

CHAPTER 8 Conclusion

8.1 Introduction

The main objective of this thesis was to provide a critical evaluation of whether promotion of BCR in South Africa would rebuild and strengthen the South African merchant fleet and whether this would have a positive knock-on effect on the South African economy as a whole. Literature covered in this thesis was drawn predominantly from various disciplines including maritime law and maritime economics. A case study of the Philippine BCR and cargo protection measures was conducted in order to establish if the Philippines model would be applicable for South Africa. The study makes a theoretical contribution to the literature by filling in the gap in academic studies assessing the impact of BRC on the South African economy. This exploratory study is most relevant when considering the possible economic benefits for the economy in implementing policies to encourage bareboat charterers to register their ships in South Africa. The study has demonstrated a critical need for further research in this area in order to highlight implementation challenges that could hamper economic growth.

The research has clearly illustrated that BCR is the most feasible option that South Africa has for rebuilding the merchant flag. It is very unlikely that a vessel owner will fully register his fleet in South Africa even in circumstances where he would be willing to trade in South Africa. BCR addresses this issue by allowing vessel owners to register their vessel in South Africa and through another preferred flag. BCR also overcomes the ship financing hurdle and exchange control restrictions which otherwise are difficult matters to deal with and to which there are no foreseeable solutions in the near future.

The analysis points to the fact that BCR is a strong option for South Africa. However, more still needs to be done to develop an attractive package that potential foreign bareboat charterers would find encouraging and entice them into cooperative schemes with local South African companies. If this is not done, South Africa will be confined to cargo supply and ship-related services but lack cargo carrying capacity.

8.2 Legal framework

The concept of BCR has challenged the traditional notion that a vessel must be subject to only one register. The SRA includes legislation which deals specifically with BCR. The uptake of BCR in South Africa has therefore been anticipated in various ways through the SRA.

Firstly, the SRA allows for a BCR, as per section 16(c).

In addition, the period of the bareboat charter is not fixed in terms of the SRA of 1998, Section 1(1)(ii). This stands in contrast to other registers which allow for dual registration but fix the period of the bareboat charter to a minimum term of three to five years. One of the benefits of how the SASR is phrased is that it does not prescribe the duration of the bareboat charter. This gives a South African shipowner the option to register his fleet in the SASR. A shipowner can therefore respond to market conditions and adjust his tonnage by bareboat chartering in a vessel for a short term.

Finally, BCR requires differentiation between the public and private functions of the ship register¹⁴⁹ in order to avoid problems associated with the law dealing with mortgage or transfer of ownership. Moreover, this serves to reduce the risk of a flagless ship that is regulated by the jurisdiction of more than one state.

The SASR deals with these challenges in Sections 19(1)(b) and 19(2)(d), which requires the owner's written consent and filing of the primary register's authority in support of the application for registration in South Africa. Section 31(9) prescribes that the private law functions do not apply to ships registered under BCR. Therefore any question arising with regard to the transfer of ownership or mortgage is subject to the law of the state of primary registration. The SRA is in line with the requirements of Article 16 of the United Nations International Convention on Maritime Liens and Mortgages 1993¹⁵⁰ which prescribes that mortgages are subject to the law of primary registration and that written consent needs to be obtained. Section 31(9) is important as it resolves legal uncertainty with respect to the registration of mortgages on the vessel which is subject to the law of more than one jurisdiction. Therefore the interest of the security of lending banks is protected.

¹⁴⁹ Coles, R, and Watt, E, ed. 2009. *Ship Registration: Law and Practice*. [Online]. London: Informa Law, 48. Available at:

https://books.google.co.za/books?id=LWISlNR76WgC&pg=PA363&lpg=PA363&dq=Coles,+R.;+Watt,+E.+Ship+Registration:+Law+and+Practice.&source=bl&ots=urtdMCx6Z7&sig=YpX33yAaa_Ve83Ci0G01KIZE81c&hl=en&sa=X&ved=0CC4Q6AEwBGoVChMizISC2KjyAIVTGkUCH1cNQeI#v=onepage&q=Giuseppe%20di%20Vittorio&f=false [Accessed: 03 March 2015].

¹⁵⁰ This is not yet in force, and South Africa has not yet ratified the convention.

Therefore this study points to the fact that the legal framework should give the necessary assurance to South African nationals to choose the South African flag for their bareboat chartered fleet. Thus the bareboat charterer benefits from securing reduced operational costs when registering a bareboat chartered fleet in South Africa, while protecting the interest of the lending banks.

8.3 Policy implication

Factors influencing the decision of a shipowner to register her bareboat chartered fleet in South Africa are based on profit maximisation and reputability of the flag state. South Africa has ratified a number of IMO and ILO conventions and therefore has established a responsible framework for ship regulation.

With regard to profit maximisation, the ratification of the Taxation Law Amendment Act, 2014 provides a more attractive package for bareboat charterers operating in international shipping, as they are exempt from income tax. This places the SASR on a level playing field with other registers in terms of taxation benefits of the flag state. However, the SASR needs to provide further benefit for a vessel owner to decide to move her fleet from an established register to the SASR. The SASR therefore needs to put policies in place which make it unique and more beneficial to shipowners in comparison to other registers.

The South African government aims to further strengthen the local maritime industry, as outlined by the Minister of Transport in the foreword to the Green Paper, 2015 stating that:

The Department of Transport will continue to evolve policy positions that will create enabling conditions for the maritime industry to play its full role in the socio-economic development of our country and its people, including the rest of the African continent¹⁵¹.

It is therefore a declared policy of the government to accelerate the development and expansion of the South African registered fleet. Recent successes of the *Cape Orchid* and *Cape Enterprise*, with both vessels now flying the South African flag under BCR, shows that the first milestone has been achieved. However, government still needs to ensure that these two vessels do not remain an isolated case and that other bareboat charterers gain confidence in registering their fleets in South Africa.

¹⁵¹ Green Paper South African Maritime Transport Policy 2015. Foreword: Minister of Transport.

8.4 Recommendations for future research

South Africa is the world's biggest exporter of chromium and platinum¹⁵² and therefore the main focus for government should be to attract more dry bulk carriers to its register. This can be achieved through policies which give incentives to exporters to ship South Africa's raw materials on CIF terms on South African-flagged vessels. The more the industries selling terms can shift from FOB to CIF, the more encouraging it would be for a South African shipowning company to register its bareboat chartered fleet in South Africa.

However, these policies should by no means be restricted to CIF terms only, as that could do more harm than good to the South African economy. Such a restriction would result in importers looking for cargo elsewhere, as South African cargo cannot compete with the global market price, owing to the higher price on CIF terms. Therefore government needs to subsidise the price between CIF and FOB, which can be achieved through tax incentives. This study has shown that it may be of benefit for South Africa to implement policies based on the measures implemented under the Philippine Presidential Decree No. 667 of 5 March 1975 which, would encourage exporters and importers to patronise South African-flagged vessels. As outlined above, these measures provide tax incentives which enable the exporter or importer to deduct 150 per cent of overseas freight expense and national port charges incurred from their taxable income if they ship on national vessels¹⁵³. This would encourage the South African mineral exporter to ship her cargo on a South African-flagged vessels, as the tax incentive will enable the exporter to sell the product CIF at a better price than FOB.

These policies might also encourage South African based shipowning companies to register their fleet back in the SASR. There are only a few South African shipowning companies who no longer have their head offices in South Africa¹⁵⁴. However, those companies could register their fleets through bareboat chartering in South Africa, in order to benefit from the amended taxation act.

In the event of further incentives through cargo protectionism, it might be feasible for the South African-based shipowning company to register its bareboat-chartered fleet in South Africa under BCR. Benefits for the company would be that they are enjoying tax benefits of the SASR.

¹⁵² SOUTH AFRICA EXPORT 1957-2015. Available from: <http://www.tradingeconomics.com/south-africa/exports>. [Accessed: 23.12.2015].

¹⁵³ Philippines: Presidential Decree No. 667, 5 March 1975. Section 1.

¹⁵⁴ HELLENIC SHIPPING NEW. 2013. *South Africa: Creating an attractive Ship's Registry – the draft South African Maritime Policy*. [Online] 07.12.2013. Available at: <http://www.hellenicshippingnews.com/3ce0304b-f8bc-452a-815e-13d7cf9fc3c3/> [Accessed: 30 September 2015].

While the mortgage and ownership rights are still subject to the private law of the primary register and are therefore not subjected to unfavourable legislations in South Africa.

The policies may even encourage a South African company to bareboat charter a fleet and register it in South Africa. However, such ventures can be tricky. Therefore, even if further policies are implemented which provide for tax incentives for raw materials exported on South African-owned dry bulk carriers, owners may struggle to find backhaul cargo to South Africa. South Africa on one hand exports raw materials in dry bulk carriers to Asia but on the other hand imports a variety of containerised cargo in container carriers¹⁵⁵. The imbalance of trade could make it difficult for the shipowner to find substantial cargo for the backhaul journey to South Africa. As a result, there will be no chance for the shipowner to make any profit if the backhaul is in ballast. A newly established South African shipowning company will, moreover, find it difficult to compete globally, considering the market supply overhang¹⁵⁶. Hence the surplus of bulk carrier is being topped up by new deliveries while trade is set to decline.¹⁵⁷

The most feasible option is for a South African company to increase its efforts with respect to imports. One way of achieving this would perhaps be through joint venture agreements between local companies and international companies with mutual interests. The BCR company would benefit from tax incentives when carrying cargo out of South Africa and the international shipping company would facilitate cargo for the return leg, which would have otherwise been ballast a leg. Alternatively the government should seek synergy for similar purposes through bilateral agreements with its specific trading partners. These and other methods would not only translate to higher profits, but can also be expanded to include cooperation in other fields related to merchant shipping.

A typical example of private cooperation can be seen in registering of The *Cape Orchid* and *Cape Enterprise*. Both vessels are owned by VUKA Marine which is a joint venture between a South African company, Japanese K-Line Shipping and Fairmont (which is a Filipino company). This is a classic success scenario of what could be achieved through private cooperation between South African companies and other international conglomerates. The registry of the *Cape Orchid* is the first case of such a joint venture in South Africa. The success

¹⁵⁵ SOUTH AFRICA. DEPARTMENT: INTERNATIONAL RELATIONS AND COOPERATION. *China (People's Republic of)*. Available from: <http://www.dirco.gov.za/foreign/bilateral/china.html>. [Accessed: 23.12.2015].

¹⁵⁶ Supply overhang means that there is an over capacity of shipping space in the market.

¹⁵⁷ CLARKSONS RESEARCH. 2015. *Bulkcarrier Investors Search For A Silver Lining*. [Online] 11 December. Available from: <https://clarksonresearch.wordpress.com/category/bulkcarriers/> [Accessed: 23 December.2015].

of VUKA Marine will most likely be the lodestar for similar future endeavours in the South African shipowning industry.

The aforementioned examples are suggestions for South Africa's shipping companies to benefit from the bareboat charter regime in South Africa. This provides a key area for further research to evaluate the full economic potential of this type of arrangement. Therefore, it is recommended that there are further consultations between the private sector and government agencies in pursuit of implementing policies for the growth and development of the SASR.

8.5 Benefits for South Africa in having a bareboat chartered fleet in its register

This study has illustrated that the benefits of having a bareboat chartered fleet are fourfold.

First, South Africa will enjoy economic benefits through increases in revenue in the forms of taxes and other fees and the generation of foreign exchange. Taxes generated from charter hire and remittance from seafarers on South African-flagged vessels will be positive for the economy. Both payments are made in USD and will therefore benefit the balance of payments.

Secondly, it will also provide labour opportunities. However, with the average number of crew employed on board varying between 20 and 30 crew members, South Africa would require a large fleet in order to make a dent in unemployment through seafaring jobs. Nevertheless, having a bareboat chartered fleet on the register will enable South Africa to train cadets – and well-trained, English-speaking seafarers will be hired by vessels of other nations as well.

The third factor is the acquisition of ship management and technical expertise without the financial investment. A bareboat chartered fleet in the SASR will stimulate growth in other maritime sectors.

Finally, a bareboat chartered fleet will give South Africa the means of expanding its merchant fleet and shares of South Africa-flagged vessels in international trade.

However, flagging of a merchant fleet under BCR will not ameliorate the desperate statistics on unemployment. It is not the ship which creates employment but the company managing and supplying the ship which will stimulate the economy and create jobs. Even if South Africa attracts a substantial fleet under BCR through tax incentives, these ships could still theoretically be commercially managed, technically managed, insured, maintained and supplied in different countries.

To summarise, the concept of BCR will assist South Africa in regaining a merchant fleet as the country lacks the capital to stimulate a competitive shipping industry on its own. Nor is the current legislation responsive to full ship registration. South Africa has an effective judicial system and has adopted several international conventions and should therefore not be catalogued as a flag of convenience. A shipowner registering a bareboat chartered fleet will benefit from the tax incentives without being associated with flying the flag of convenience. The thesis has shown that BCR evolves according to the political and economic interests of South Africa and the trends of the shipping industry in general. For South Africa, a national fleet is a key element of economic growth considering that 98 per cent of South Africa's exports are carried by it sea. This is due to South Africa being in the unique position of being one of the world's largest mineral exporting countries. South Africa therefore needs to implement policies which make it mandatory for South African cargo to be transported on South African owned ships in order to encourage ship owners to register their fleet in the South African register. After all, an owners choice of the flag his ship flies is based on profit maximisation. If a ship owners sees the benefits of having an advantage over other carriers to carry South Africa's exports, coupled with the taxation benefits, then South Africa should be able to reverse the trend of having an empty ships register.

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