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# **RUSSIAN SHIPOWNERS IN THE ASIAN-PACIFIC REGION SHOULD OPERATE ACCORDING TO WESTERN STANDARDS**

**by Dmitry Kafanov**

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*The Asian-Pacific region due to a serious economic potential and prospects for market development are called by many experts as "the region of XXI century". Shipping companies of the Russian Far East are faced with paying a part of no small importance in the development of the market of transport carriages on the Asian-Pacific region. The reporter of Maritime News of Russia (MNR) talked to **Dmitry KAFANOV**, President of Inmar Legal Co. Ltd, about strategic prospects for national shipping in the Asian-Pacific region and its legal aspects.*

- **Dmitry Alexandrovich, what is a specific nature of the development of shipping in the Russian Far East, in your opinion?**
- The Far East always was a region with the developed marine transport branch, with large shipping companies. Unfortunately, the national economic crisis of the 90s seriously touched the sphere of marine transport. As a whole, at present the main problems for the Russian shipowners are high taxes, problems with customs clearance of vessels, cargoes as well as administrative barriers, the latter ones, for the most part, are not a problem for a specific branch but for the whole sphere of business...
- **How is the Russian shipping business close to the world standards in this sphere for today?**
- I would say the following – we have many things to strive for. Our strategic goal is establishment of shipping companies and organization of shipping in accordance with the western pattern, with transparent budget and "white" taxation. Many shipowners which want to work legally cannot show their real financial turnover, because in this situation their business makes no sense. But taxation schemes may be considerably optimized with competent legal approach. Unfortunately, many companies work now on the principle of "black market" resulting in negative consequences.
- **How often do you resolve problems of Russian shipowners?**
- Rather often. We have dealt with problems of international maritime law for 6 years and gained certain experience in the sphere of legal security of shipping, "turn-key" establishment of shipping companies, acquisition of vessels (down to search for them abroad), obtaining of license for this activity, development and implementation of investment projects, tax optimization of work of shipping companies. The most Russian shipowners of the Far East have to operate in the Asian-Pacific region where every state has its own laws and legal peculiarities of regulation of shipping and all related matters. Only specialist knows all details and nuances. Practice shows that incompetent actions from the law standpoint cause direct losses to shipowners amounted to million dollars.
- **What do you think of brining the Russian vessels "under flag of convenience"?**
- Positively as a whole. This is one of the lawful ways to make a financial scheme of operation of a company which permits to considerably reduce taxation, optimize payments through establishment of offshore companies. One of the related problems is customs clearance of vessels and equipment for them in the event of their acquisition abroad, since it is necessary to pay rather high customs rates that, certainly, does not promote the development of national shipping. At present, many large national shipping companies have to bring at least a part of their fleet under flag, because usually vessels are built or bought against bank credits. Not every bank gives a large credit for a vessel registered in the Russian Register of Shipping in connection with considerable risks for the bank related to complexity of the legal protection of its interests as a creditor.
- **Today there are many talks of the necessity of establishment of the international shipping register in Russia which permits to give equal rights and correspondingly tax relieves to shipowners under Russian three-color flag and foreign flags....**
- Yes, it would be a way out. The more so, many countries have successfully followed that way.
- **The problem of operation under flag has recently become very pressing from the point of view of observance of seamen's rights, timely payments of salaries and social guarantees for seagoing personnel...**

- You are absolutely right. Such problem is actually available. At that, not only seamen suffers objectively but shipowners. For example, such disputes are judicially considered, as this takes place, in spite of formal legal circumstances, an award is passed, as a rule, in favor of seamen, which permits to secure rights of seagoing personnel, however, it may cause serious losses to a company-shipowner. Take for example: a vessel is given to bareboat charter, i.e. a lease contract without crew. Seamen are employed by a foreign charterer and courts in the event of claims on the part of the crew take recourse against the Russian shipowner which does not bear a relation to employment of seamen. If we talk of the matters of seamen's rights protection, we can say that work of marine trade unions is rather weak now.
- **How often does you company work in arbitration courts and protect the interests of Russian shipowners?**
- The world practice shows that legal companies are classified into two common specializations: the companies which carry out general consulting and the companies which deal with protection of rights in court; for example, so called barristers in the Anglo-Saxon legal model. Our company works in accordance with the first variant, though we and our partners have to appear in court rather often. The Russian reality has also fault – many law offices offer to defend shipowners' rights in court but nobody thinks that thanks to competent legal consultation many claims could be avoided at all.... We follow that way and believe that a civilized market of legal services in the sphere of shipping should be such exactly.
- **How often do Russian shipowners defend their rights in foreign arbitration courts?**
- Yes, according our data, rather often. There are very important details here. The foreign arbitration court differs essentially from the Russian arbitration court. As an instance, peculiarities of the Chinese judicial practice are so that a foreign company cannot essentially win a claim in their court, even with a strong legal support. In the Republic of Korea, for example, it is very easy to arrest a vessel, that is an effective measure of influence upon the shipowner. But in Russia to achieve arrest of a vessel is very difficult, though in preparation of the Merchant Shipping Code there were proposals to introduce a simplified system of arrest of vessels, however, in final adoption the proposals were not taken into account.
- **Have you ever defended the interests of shipping companies because of accidents at sea?**
- Yes, we had a number of cases when we defended our clients' interests after collision of vessels; in one case there was collision with a foreign military vessel, however, we in spite of all difficulties could seek compensation for the Russian shipowner.
- **How are administrative problems of shipowners resolved?**
- As a rule, the case in point is correct execution of documents by customs authorities, borders service and other control structures which in their activity are often guided by subordinate acts, departmental instructions which are not always in strict compliance with the effective legislation resulting in time loss. But these are external problems. Russian shipowners have internal problems, first of all this is deficit of competent management, management of shipping companies. Consequence of rough errors in management of the fleet is loss of vessels and their crews. Now in Russia and the Far East there are not many competent marine managers or, as they are called in the West, ship managers. Such specialists have appeared just after the crisis of shipping abroad in the 70-80s. At present, many managers in Russian shipping companies are former operators without additional education who have no system approach to arrangement of operation of the company. The result is violation of rules of navigation safety, many shipping companies fulfill formal requirements only but do not perform the real work such as instruction of crews, their training, regular certification etc. This is one side of the matter. The other one resides in the fact that, as a whole, many shipowners have no complex management of the company's whole activity, and this is an obligatory condition of their normal operation.
- **In general, are there many things lacking for Russian shipping companies in the Far East to naturally fit into the common structure of shipping in the Asian-Pacific region?**
- Yes, to my mind, many things should happen evolutionally. From strategic standpoint we now need, as I previously said, changes in approaches to management of shipping companies. Also shipping companies need rather considerable investments which is connected with a necessity of replacement and development of the fleet. In general, financing of shipping is a rather specific branch and in Russia there are no special financial institutions operating in this sphere, therefore Russian shipowners most commonly receive money abroad, In

principle, it is necessary 10-15 years for the Russian shipping market to begin to operate according to rules of the western market.

— **What do you think of the problem of ageing of the Russian fleet?**

— Yes, now the most vessels of Russian private shipowners are very worn-out; there is a problem of ageing of the fleet, the system of its operation leaves something to be desired. But shipping business is a part of the national economy which is not brought out of the crisis for the time being. For example, if at present to prohibit operating the vessels older than 20-25 years, this means a final destruction of the whole branch. A different matter, it is necessary to strictly observe the requirements of safety navigation, to provide competent ship management. Generally, in strategic prospect, time should pass to bring everything back to normal, there should be improvement of the economy and transport sphere. Though we now have positive examples, I am talking of large national shipping companies in the Far East of Russia which has reached the level of the western market of sea transportations and are example for other Far-Eastern shipowners. Their absolute advantage resides in the fact that they can more readily minimize expenses, obtain credits for the development and building of the fleet, they have traditionally more material resources and rich personnel potential.

— **What can you say of the operation of ports of the Russian Far East?**

— There is a number of problems here. The problem is especially acute concerning groundless delays and bureaucratic hold-ups in clearance of cargoes when various authorities require different documents during logistics of cargoes. Port dues in some ports of the Far East are high, what forces many shipowners to choose other ports. By the way, the port of Vladivostok is an example. Because of peculiarities of customs legislation there are problems with bunkering of vessels.

— **What, in addition to the tax reform and liberalization of customs sphere, can the state do for the development of the national shipping?**

— The development of projects in the sphere of state-private partnership is promising. Generally, in modern conditions the need of greater use of social contacts between the state and business, the state and citizens is growing. New global threats such as terrorism, ecological threats and others count in favor of the above said. A practical result of the expansion of contacts between the state and business should be the development of mechanisms of state-private partnership as guarantees of protection of interests and security of safety of business and citizens. The idea is simple: the similar agreements determine conditions of work of private companies, applicable tax schemes, customs and financial conditions, rules of work of companies and arrangements between them and the state. With the help of such projects the management of state property by private companies is organized, joint participation of the state and business in investment projects is carried out, agreements between the state structures and private companies related to some rules of doing business are concluded. An example may be the agreement between the relevant administration of the Ministry of Finances and specific shipping company that a certain taxation scheme will be applied in respect to the company. Such practice is in the USA tax system in determination of conditions of transfer pricing, and in France the projects of state-private partnership have assumed the form of steady administrative contracts.

— **What do you think, can such initiatives be really implemented in the sphere of national transport?**

— Certainly, this matter is much talked about on the highest state level. Projects of concessions for the development of shipping, building of ports and others are promising for Russia. This is correct professional approach to which Russia should strive for successful operation in the market of sea transportations in the Asian-Pacific region. As this takes place, guarantee of normal operation of the branch of sea transport should be distinct legal mechanisms which regulate relations of power and business. Semi-legal schemes of compulsion of business to participation in one or other projects by administrative means, to participation in social processes as well as granting of state preferences only to those companies the interests of which are lobbied by officials should be a thing of the past...