

EXPLORING THE NORTHERN DIMENSION



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Arctic shipping needs anti-avoidance rules to mitigate environmental disasters

Global warming will accelerate the melting of ice and release some of the Arctic territories for shipping. On the one hand, it will have a positive impact on world trade but on the other hand, the risk of ship accidents and environmental disasters will increase. In the period from 2010 to 2019, 512 ship accidents in Arctic Circle Waters were reported, not without damage to the environment. However, today's legal structure of the shipping industry makes it virtually impossible to make the ultimate owners of ships liable and responsible for environmental costs. There is no international regulation that would pressure the shipping industry to increase its corporate responsibility and to take more sustainable decisions of using clean fuels, improving environmental friendliness of ships, or recycling old ships.

- **Recommendation 1.** To improve availability and transparency of ultimate beneficial ownership data in the shipping industry.
- **Recommendation 2.** To develop mechanisms to hold the ship's ultimate beneficial owners liable for maritime incidents such as oil spills.
- **Recommendation 3.** To design anti-avoidance rules applicable to the use of flags of convenience and last-voyage flags (in the spirit of anti-tax avoidance rules).



Who evades regulation?

The evasion of regulations is a major problem in the global shipping industry. Ship companies are legally organized in such a way that they can easily avoid responsibility for the catastrophes that they cause. 90% of ships in the world are registered as a single ship subsidiary, which makes it impossible to hold the ultimate owner of a ship liable.

A further example of the circumvention of regulations and the need to meet environmental standards is the registration of the so-called flag of convenience, where one can buy the flag of the country under which the ship will sail. Panama, Marshall Islands and Liberia are the leading flags of registration followed by Hong Kong SAR and Singapore.

Palau is an island with a population below 20,000 inhabitants and a capital city below 300 inhabitants. Its ship registry represents less than 0.001% of the world fleet, but 59.5% of last-voyage flags in 2019.
(Vuillemey, 2020)

Another issue is the use of old ships. Instead of being recycled, the ships change their names, owners and get the so called last-voyage flag (most frequently by Panama, Liberia, Comoros, Palau and St. Kitts & Nevis), and then the obsolete ship is simply dropped in a remote harbor of a developing country. The majority of abandoned ships end up in ports of Bangladesh, India and Pakistan, where they constitute a major environmental risk.

Why is better regulation needed?

The need to comply with regulations and environmental standards plays a critical role in all activities in the Arctic. It is a unique place on the planet due to its natural characteristics that are necessary to protect and preserve. The region is remote and its emergency infrastructure is very limited, which combined with extreme weather conditions makes the problem of a potential ship disaster especially acute.

Such incidents incur high ecological, economic, and social costs for the Arctic. These costs may amount to billions of US dollars in terms of clean-up costs, equipment loss,

lost fishing and tourism income, wreck removal, fines, reputational damage, impact on health and well-being of indigenous populations, and incalculable damage to wild nature. One major oil spill can kill hundreds of thousands of seabirds and is detectable in marine mammals, invertebrate and shellfish even several years after the spill. This makes enforceability of and compliance with strict maritime regulations inevitable.

| | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | Total |
|---|------|------|------|------|------|------|------|------|------|------|-------|
| Machinery damage/failure | 16 | 12 | 13 | 20 | 27 | 45 | 32 | 46 | 23 | 14 | 248 |
| Wrecked/stranded (grounded) | 9 | 9 | 8 | 10 | 14 | 6 | 11 | 9 | 7 | 6 | 89 |
| Fire/explosion | 6 | 6 | 1 | 4 | 2 | 4 | 1 | 3 | 6 | 8 | 41 |
| Collision (involving vessels) | 10 | 4 | 4 | 2 | | 3 | 2 | 4 | 2 | 3 | 34 |
| Contact (e.g. harbor wall) | 4 | 1 | 3 | 6 | 4 | 5 | 1 | 1 | | 1 | 26 |
| Hull damage (holed, cracks etc.) | 2 | 2 | 1 | 2 | 1 | 1 | 2 | 2 | | | 13 |
| Foundered (sunk) | | 3 | 1 | 1 | 2 | | 1 | | 1 | 1 | 10 |
| Labor dispute | | | | | | | 1 | | | | 1 |
| Miscellaneous | 4 | 2 | 6 | 5 | 5 | 6 | 4 | 6 | 4 | 8 | 50 |
| Total | 51 | 39 | 37 | 50 | 55 | 70 | 55 | 71 | 43 | 41 | 512 |

Table 1: Casualties (shipping incidents), including total losses in Arctic Circle Waters, 2010-2019. AGCS Safety and Shipping Review 2020, p. 33.

Solution: anti-avoidance rules

Regulation of vessels sailing under flags of convenience is one of the unresolved challenges in the current international legislation on the Arctic. In 2017, about 50% of vessels operating in the Arctic were flagged by Panama, Hong Kong, Liberia, Marshall Islands, Malta, Singapore, Bahamas, Netherlands, and Cyprus. Therefore, the adoption of legally binding rules in the Arctic implies that negotiations need to be made with many non-Arctic states as well.

The Polar Code, which is the main set of international rules providing for safe ship operation and environmental protection in the Arctic, very much relies upon flag states to enforce standards. However, certain states are lax about enforcing rules and allow beneficial owners to relatively easily and inexpensively cover their true identities and avoid being subject to strict regulations ex-ante and liability ex-post.

Anti-avoidance rules in the spirit of anti-tax avoidance rules applicable to the use of flags of convenience could be a potential solution. Its two most important aspects would be the improvement of data availability on beneficial owners in the shipping industry, and the development of mechanisms for making beneficial owners liable for maritime incidents.



The adoption and development of such provisions require concerted action by the international community, especially the Arctic states. A common position on the question would allow the introduction of rules whose violation would prohibit ships from entering the Arctic waters and contribute to the sustainable development of the North.

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