

Paradigm Shifts in Shipping Registry Policy Led to Revitalization – Hong Kong Case*

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Abstract

There are needs for ship registers to become business oriented but maintain the quality of fleet. To meet these two objectives, Hong Kong Shipping Register (HKSR) was re-engineered in 1999. An autonomous HKSR was established before the handover of the sovereignty of Hong Kong to China in 1997. When the newly established HKSR began operation, it fell to merely 5.5 million tons in late 1997. In May 2009, the registered tonnage was 41 million tons and the HKSR achieved significant growth of 7.5 times of that in 1997. The study through interviews analyses the paradigm shifts in the shipping registry policy in Hong Kong which led to a successful revitalization of the registered tonnage. External factors of the shipping community and internal factors of the administration in Hong Kong became major drives of the revitalization of the HKSR. The paradigm shifts include a new page of dialogue in formulation of policy of shipping registry with the stakeholders, structural change of quality and survey mechanism in HKSR, restructure of the consultative platforms in connection to enhancement of customer satisfaction, involvement of diplomatic assistance from Beijing and in-depth re-engineering of the bureaucratic system in the shipping registry in Hong Kong.

Key Words : Paradigm shift; Shipping registry policy; Revitalization; Hong Kong

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I. Introduction

Most newly industrialized countries or places, such as South Korea, Singapore, Malaysia, Taiwan and Hong Kong put a high priority on shipping development as an essential element towards their trade and economic development and their foreign trade has grown more rapidly than that of the developed countries (Frankel 1989). Shipping development is one of the important factors of the trade and economic development in Hong Kong. The Hong Kong Shipping Register (HKSR) was established for more than 140 years but Hong Kong registered ships had to be registered under the British Shipping Register prior to 1997. Before the handover of the sovereignty of Hong Kong to China in 1997, an autonomous HKSR was established in 1990 and a new set of law for the HKSR is required. In May 2009, the statistics show that the Hong Kong registered tonnage dramatically reached 41 million tons and the HKSR achieved a significant growth of 7.5 times between 1997 and 2009. No study was conducted to analyse the causes of the significant growth of registered tonnage in the HKSR and paradigm shifts, if any, in the process of its revitalization. The objectives of the study are to identify the paradigm shifts in the formation and growth of the autonomous HKSR; and to investigate the success factors of its revitalization.

II. Methodology

A study which adopts qualitative analysis can be carried out in a rigorous and structured manner (Woodburn, 2007). It is suitable for some areas of maritime research to choose qualitative methodology as one of their alternatives in research, e.g., port policy, shipping policy, shipping taxation policy or seafaring experiences (Vining and Boardman, 2008; Qiu, 2008; McLellan, 2006; Marlow and Mitroussi, 2008; Mack 2007; Everett, 2007). A qualitative approach is used in the examination of the cause of delays in expanding coal export infrastructure and the number of regulatory regimes directly impacting on the facility and operation (Everett, 2007).

The study uses qualitative methodology with the assistance of interviews. The study builds upon a review of public information such as official statistics and policy statements of Marine Department, Maritime Industry Council, Hong Kong Government, Department of Justice, International Maritime Organisation and US Coast Guard. It has been supplemented by analysis of the process of formation and development of the HKSR using original data collected from the public and private sector. The analysis provides insight into the changes of the HKSR. The study adopts qualitative in-depth interviews with 11 senior and middle managers in the public and private sector of the shipping industry in Hong Kong. The study finds and analyses the evidence of paradigm shift and success factors in the formation, growth and revitalization of the HKSR.

The paper, which analyzes policy response of intra-European short sea shipping, UK coastal shipping, urban/river transport and global container shipping, employs a qualitative approach (Barid, 2005). Maritime researchers appear to be discovering that seafaring experiences, particularly the human element, are difficult to explore and represent with statistics and tables, and therefore qualitative methods are needed (Mack, 2007).

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In a study of a case company, 19 in-depth interviews in a service company were included (Olsson and Karlsson, 2003). Four interviewees were selected for a study which was complemented by other information from industry journals and company archives (Penaloza, Brooks, Marche, 2007). In other examples: one company was used to illustrate how the e-business planning model was applied

in a practical context (Tang, Burridge and Ang, 2003); and only one automotive component supplier, Trico, and its strategic supply base were involved in another study (Esain, 2000). The study examines the source of law on the HKSAR due to the handover of the sovereignty from Britain to China. It further finds and analyzes the evidence of paradigm shift and success factors in the formation, growth and revitalization of the HKSAR.

The source of law in changing ship registration and related legislations after the handover of Hong Kong to China in 1997 is the Sino-British Joint Declaration on the Question of Hong Kong (HKSAR Government, 2009) and the Basic Law of the Hong Kong Special Administrative Region (Chinese Government, 1990).

After years of negotiation between China and the U.K., the Joint Declaration was signed in 1984. It sets out, among other things, the basic policies of the People's Republic of China (PRC) regarding Hong Kong. Under the principle of 'one country, two systems', the socialist system and policies shall not be practiced in the Hong Kong Special Administrative Region (HKSAR) and Hong Kong's previous capitalist system and life-style shall remain unchanged for 50 years. The Joint Declaration provides that these basic policies will be stipulated in the Basic Law of the HKSAR.

III. Paradigm Shifts started in the Revamping of the Law of Shipping Registry

Traditionally shipowners chose a ship register for the convenience of shipping operations, e.g. with minimal interference from flag state. However, with more stringent requirements of quality shipping (e.g. ISM Code, ISPS Code, STCW), shipowners now realize the importance of quality registers. Apart from the role of regulator, ship registers are expected to assist shipowners' shipping operations in various aspects .

The Hong Kong Government had the legislative power to revamp the law of ship registration based on the Joint Declaration and it was definitely too late to plan for revamping until the Basic Law was put into effect on July 1, 1997.

Foreign and local shipowners in Hong Kong wanted to know how the laws of ship registration would be changed well in advance of the handover so that they had sufficient time to plan to stay or not. Insofar as to the previous systems of shipping management and regulation of Hong Kong, the Joint Declaration states that the Hong Kong maintains its previous systems of shipping management and shipping regulation, including the system for regulating conditions of seamen. The specific functions and responsibilities of the Hong Kong Government in the field of shipping are defined by the Hong Kong Government on its own. Private shipping businesses and shipping-related businesses and private container terminals in Hong Kong may continue to operate freely (Sino-British Joint Declaration 1984). It is vital for Hong Kong to change the law of ship registration well before 1997 in order to lay down the foundation of the shipping register in Hong Kong.

The revision of the shipping law in Hong Kong in 1997 is an overhaul due to political reasons and there is no other option. The revision of the shipping register in Hong Kong becomes a natural process of change under the blanket cover of the major overhaul of all legislations prior to the handover. Revising the law of shipping register is the first paradigm shift. The HKSR had been established and running for 150 years in 1997. Hong Kong, which was a British colony until 1997, wished to have a smooth transition of the shipping register on the return of sovereignty to China on July 1, 1997. Prior to 1997, a ship had to be registered on the British Shipping Register in the name of Port of Hong Kong if a Hong Kong shipowner wanted to register his ship in Hong Kong. Despite the different attempts to formulate and establish an autonomous shipping register in Hong Kong, the British Government did not support the idea. It means the HKSR before 1997 had to follow exactly with the British Shipping Register. The system of the British Shipping Register was rather rigid and inflexible due to its long maritime tradition and the transitional period to 1997 provided an excellent opportunity for change.

The name ‘Hong Kong Shipping Register’ was used when it was under the British regime until 1990. The name was retained when it became the ‘autonomous HKSR’ under the Chinese regime after 1990. Before the autonomous Hong Kong

Shipping Registry was planned and established, a Steering Committee chaired by the then Economic Services Branch of the Government of Hong Kong, including people from the local shipping industry and Marine Department was set up. The tasks of the Steering Committee were never easy as all the shipping rules and regulations in relation to the shipping register and other shipping issues had to be examined and amended to international standard. The HKSR inherited the good and bad practices of the British Shipping Registry. It was found that the principal hindrance to shipowners were the traditional requirements on manning of British nationality, in particular employment of British senior officers, use of British-made equipment, and antiquated legal procedures regarding registration, ship surveys and ship mortgages. The new shipping law, covering registration of ships, surveys, quality control, safety, charges, etc., was enacted on December 3, 1990. The Hong Kong Government with the shipping community in Hong Kong tried their best in formulating an updated shipping register but nobody knew in advance whether the newly created HKSR continued to attract shipowners registering their tonnage in Hong Kong. The work of revising the details of the shipping regulations of Hong Kong and inserting new sections here and there continued thereafter. The job of localising the British shipping law in Hong Kong was more or less complete by 1997-1998. It seemed that the issues of the shipping register were resolved early on and the Hong Kong Government waited for the handover in 1997. Unfortunately it was not the case and serious problems occurred threatening the survival of the HKSR well before 1997.

IV. Crisis of the HKSR approaching the handover

The gross tonnage under the Hong Kong flag was 6.3 million tons in 1990 (see Table 1: Registered Gross Tonnage from December 1990 to February 2009 in the HKSR), when the newly established HKSR began operation. It did not rise above 10 million tons during the entire period from 1990 to 1997 though there was an incentive of capping the registration fee and tonnage charge for large ships (Richardson 1992). But the worst time was around November 1997 in which

the gross tonnage fell to merely 5.5 million tons. The Policy Bureau of the Hong Kong Government was seriously concerned, and tried to find the causes of the fall. The reasons for the rapid decline in the registered tonnage were multiple and complex. Possible causes included the lack of political confidence in China, the HKSR and the worry about a lack of quality control in the shipping register after Hong Kong's return to China. The withdrawal of tonnage from P&O alone cut the tonnage in the HKSR by 1.2 million tons before 1997.

Before successfully resolving the worries of the Hong Kong shipping industry, a serious internal problem arose in Marine Department. The issue related to the survey staffs in Marine Department who were extremely concerned about the loss of authority in conducting surveys of ships while they were being used to carry out audit inspections of all ships registered in Hong Kong. Surveyors of Marine Department opined that they had more authority if they played the role of surveyor instead of 'auditor'. They felt that the quality of the Hong Kong registered ship might be under threat if the survey work was delegated to third parties like Classification Societies while surveyors of Marine Department only performed the audit function. The survey staffs of Marine Department also worried that they might have no role to play in relation to the HKSR and this would later lead to substantial loss of jobs. What they had observed was the significant decline of the tonnage registered in Hong Kong and it seemed to them that the new HKSR had not turned the tide around in attracting more domestic and foreign tonnage joining it. The senior management of Marine Department found that it was not straight forward to convince the survey staffs of the merits of the new system of audit inspection. Marine Department did not give up the newly established autonomous HKSR and thought of re-engineering the structure of the HKSR.

V. Re-engineering of the HKSR in 1998

The autonomous HKSR commenced to operate on December 3, 1990. The abrupt and continual decline of the registered tonnage in Hong Kong to a record low of 5.5 million tons posed a real threat to the entire establishment of the

HKSR in 1997. To counter this, Marine Department decided to carry out an in-depth re-engineering exercise in 1998. Many possible issues could be included in the re-engineering exercise, e.g. growth of tonnage, amount of revenue, quality of tonnage, incentives to attract more tonnage or size of the HKSR in the world league, but it was not easy to determine which ones should be the top priorities for the future of the HKSR. In a study based upon Lloyd's of London casualty records, a risk factor that had significant and independent effect upon the likelihood of a bulk carrier foundering was related to the ship's flag of registration (Roberts and Marlow, 2002). One of the requirements of the re-engineering is that Hong Kong did not want to see its 'newly' established shipping registry to be associated with any statistics of major casualties. The evidence presented against flags of convenience in terms of vessel safety appears overwhelmingly deleterious. The International Transport Workers' Federation indicates in their 'Flag of Convenience Campaign Report' for 1998 that of the worst 20 flags both in terms of absolute numbers of vessels and absolute tonnage lost in 1998, ten are flags of convenience (Alderton and Winchester, 2002). On the other hand it is important to distinguish between the shipping registries which offer the necessary guarantees in terms of quality and safety and those which do not. It is a mistake to label closed registers intrinsically safe and abiding by international regulations, and flags of convenience as unsafe and dangerous (Llacer, 2003). Hong Kong did not want to be in the group of 20 flags above purely because of the pressure of growth in tonnage and whatever tonnage was offered. It meant that the quality of the tonnage registered could not be compromised due to the growth of the registered tonnage in the HKSR. Having said that, Marine Department was not sure that the registered tonnage would grow if more incentives were provided for domestic and international shipowners.

Study finds that more incentives in the shipping policy on national shipping did not progressively increase the tonnage of the shipping registry in Taiwan and deregulation of the maritime transport market basically had no impact to shipping carriers (Chiu, 2007). It seems that providing incentives is not a guarantee of more tonnage in the HKSR in long term. One of the strategies, which Hong Kong can consider, is to attract tonnage which adopts either the Greek shipping policy or

management-intensive shipping policy described by Goss. The strategy assists to recruit long term quality shipowners and/or ship operators into the HKSR (Goss, 2008). Marine Department decided to maintain quality of the fleet in the HKSR regardless the growth of the HKSR increased or decreased.

The senior management of Marine Department took a different approach in this important project. A paradigm shift in formulating a new policy in the HKSR was attempted. The concept of a brand new idea, namely Flag State Quality Control (FSQC), was considered. The senior management of Marine Department this time involved the middle management and front line staffs at the beginning of the re-engineering exercise and they owned the problem and also proposed alternatives to the problems. The responsibility for action was delegated to the survey staff of Marine Department. They were asked to identify possible issues in connection to the survey of ships and look for appropriate solutions. It was not a straight forward problem because the team had to strike a fine balance between maintaining the quality of ships registered with the HKSR up to international standards and at the same time reducing the costs of surveys for shipowners who compete for business worldwide. Shipping community is alarmed if a shipping registry reaches a situation of the Panamanian Shipping Registry which at one stage kept a high casualty rate, worsened by the absence of procedures for the investigation of casualties, and the alarming situation related to Port State Control (Llacer, 2004). The team finally solved the issues of the survey of the registered tonnage in Hong Kong by outsourcing surveys to the Classification Societies, which had a much wider worldwide network as well as expertise. The survey staff of Marine Department remained responsible for the monitoring of the quality of the registered ships on the HKSR. A study reveals that the shipping industry is a relatively safe industry but there is a possible over-inspection of vessels. The effect of inspections varies across ship types and the prevention of incidents with high economic costs can be improved by a coordinated approach of all types of inspections that are performed which allows the decrease of unnecessary inspections. More emphasis should be placed by a shipping registry on the rectification and follow-up of deficiencies and the implementation of the ISM code (Bijwaard and Knapp, 2009). Hong Kong took the issue of over-inspection

into consideration when it formulated the mechanism of the FSQC Programme.

The basic principle behind the FSQC is that the Register takes up an overall monitoring role on all the aspects and stakeholders affecting the quality of Hong Kong registered ships. The original scope of ship registry focuses on the flag State inspection only, without much association to the performance of related organizations, e.g. management companies .

The concept of the FSQC Programme was first formulated among shipping registers worldwide by Marine Department which later creatively devised another concept, namely the Pre-registration Quality Control Programme (PRQC), which targets second hand ships wanting to join the HKSR. Marine Department was determined to uphold and maintain a high level of quality in the HKSR including the FSQC Programme (MD, 2008). It has implemented the FSQC system since 1999 to monitor and upkeep the quality of Hong Kong registered cargo ships. It aims to discharge the obligations under the international maritime conventions vested to a signatory state. The FSQC system consists of quality assessment, quality assurance inspections, and monitoring the performance of Recognised Organisations. The PRQC serves as a gatekeeper against a substandard ship which applies for registration to the HKSR. It was introduced in 2004 to ensure ships joining the HKSR are complying with all applicable safety and pollution prevention standards of the relevant international conventions at the time of entry. On receiving notice that a ship has applied to join the Register, Marine Department assesses the condition of the vessel taking into account the ship age, ship type, number of Port State Control detentions, number of Port State Control deficiencies, existing flag, existing classification society and accident records of the ship, etc. to determine if the ship warrants a PRQC inspection. All critical deficiencies detected during the inspection must be rectified before the Certificate of Registration can be issued. If the condition of a ship is found unacceptable, registration will be refused (MD). The two programmes contributed a great deal towards directly revitalizing the HKSR without sacrificing quality and safety.

Relying on quality of the fleet in the HKSR cannot be the only success factor of the HKSR and Marine Department started to further the relationship with the private sector.

VI. Partnership between the government and private sector

Marine Department was often caught between the provision of quality service and the shipping industry which wanted to lower the charges in relation to the shipping register. It was found that it was vital to keep continual dialogue going between Marine Department, shipowners, the relevant staff at the working level of the shipping companies and other stakeholders of the shipping industry in Hong Kong. The methodology of collecting feedback and opinions used by Marine Department included regular interviews and questionnaire surveys.

Initiatives which are successful are originally started by Marine Department which is prepared to involve a certain amount of trial and error. An initiative might originally be worked out by the senior management of Marine Department and then promoted in various events for the stakeholders of the shipping industry.

Staffs of Marine Department have to make ample time to receive input from the shipping industry in Hong Kong for improvement and amendments.

In 1997, Hong Kong Shipowners Association submitted a formal proposal to the Hong Kong Government on the question of fees of the HKSR. The Economic Services Bureau, HKSAR, and Marine Department reviewed the proposal in relation to the level of fees, the ship surveying procedure and other related areas.

Other relevant units in the Hong Kong Government were involved in order to expedite the process of revision and enhancement of the HKSR. The Finance Bureau which was responsible for setting Government fees and charges was also involved. The objective was to streamline the fee structure, to reduce the cost burden to shipowners and to increase the competitiveness and attraction of our shipping register (Ip, 1997). Other departments joined in to make way for changes. The Services Advisory Committee of the Trade Development Council and the Hong Kong Shipowners Association worked together promoting Hong Kong as a ship management centre on different occasions. After strengthening the cooperation with the private sector and different government departments in Hong Kong, Hong Kong also encountered problems in diplomatic arena.

The issue of a Hong Kong registered ship trading between Hong Kong and Taiwan after 1997 demonstrates a good example of constructive synergy between

the government and private sector in the shipping industry. The unification of Taiwan with the PRC is a sensitive political issue in China and Taiwan. The four pacts signed between China and Taiwan on November 4, 2008 signified the normalisation of cross-strait contacts by restoring the ‘three links’ - postal, transport and trade - cut nearly six decades ago between China and Taiwan (Ho, 2008). Prior to 1997, a ship of the HKSR which flew the British flag encountered no difficulty politically in calling at the ports of Taiwan or a ship flying the flag of Taiwan calling at the port of Hong Kong. After the handover in 1997, a ship of the HKSR which flew the Chinese flag and HKSAR flag were not permitted to enter any port of Taiwan and nobody at that time could be sure when the three links were connected. It was a devastating impact to ships of the HKSR which could not continue to participate in the Hong Kong - Taiwan trade, which is worth more than 150 billion Hong Kong dollars a year. Contact through official channels between China and Taiwan was not frequent and it might take a long time if official talk was engaged. Mainland China appeared unwilling to start any official exchange in the government-to-government mode based on its ‘one China’ principle. It also refused negotiation through Strait Exchange Foundation (SEF) and Association for Relations Across the Taiwan Straits (ARATS) mode before Taiwan had acknowledged the ‘1992 common understanding’ based on the interpretation of the Mainland China. At first, Taiwan was unwilling to contact the mainland Chinese authorities by official forms. The SEF, which was a private foundation, was established by Taiwan government in March 1991 as a window for interacting with the Mainland China. Mainland China also set up the ARATS in December 1991 in order to conduct negotiations and dialogue with Taiwan. In addition, the WTO mode was unworkable because mainland China had refused to discuss with Taiwan any issue in an international forum (Chang, Lin and Bao, 2006). The problem was not encountered before by the governments of the three places, i.e., China, Taiwan and Hong Kong. Only a shift from the old paradigm might break the deadlock. The shipping community in Hong Kong proactively played an important role as a bridge between China, Taiwan and Hong Kong.

Finally the governments of China, Taiwan and Hong Kong all agreed that the Hong Kong Shipowners Association could act as a non-government organisation

in talking to Taiwan about the issue of calling at Taiwanese ports by Hong Kong registered ships and vice versa. Finally an agreement was reached ensuring the shipping links continued between Hong Kong and Taiwan after the transition in 1997. The agreement guarantees that Hong Kong registered ships can continue to call at Taiwanese ports freely and vice versa, and it ensures that Hong Kong registered ships can continue to participate in the Hong Kong - Taiwan trade (Ip, 1997).

The organisational enhancement of Marine Department together with the improvement of the HKSR was positively received by the shipping community in Hong Kong. Shipowners in Hong Kong voted with their feet demonstrating the competitiveness of the HKSR. The positive impact on the shipping community in respect of the HKSR was the improved competitiveness of the shipping industry in Hong Kong. The competitiveness was improved due to the facts that there were appropriate tonnage charges and fees; efficient services from Marine Department; responsible administration and regular dialogue among stakeholders. The result was increased business in Hong Kong from shipping companies based in China, Japan and Korea. The negative impact was not at first immediately obvious; the fast growing tonnage of the HKSR attracted more attention from some international labour unions such as the International Transport Workers' Federation. Quality of the HKSR is frequently a concern for existing as well as potential shipowners.

VII. Quality of the HKSR

The term 'flag of convenience' emerged in the practice of international shipping during the mid-1940s, when several countries, principally Panama, Liberia and Honduras, began to grant their flag to any foreign merchant ship for a specified payment, confining themselves merely to registering it (Egiyan, 1990). Open registry is different from a flag of convenience. For almost four decades, the expansion of open registries' shipping and the growing interest of several countries to increase the tonnage registered under their flags have allowed for

the creation of new maritime nations. These registries, which are also known as commercial registries, have allowed easy registration access and transfer of ships owned and controlled by non-citizens, low taxation, manning rules that are free of nationality requirements and other facilitations conducing to lower management costs. These characteristics contrast with the traditional registries' requirements of ships to be owned, and/or managed, and to a certain extent manned by nationals of the flag-state (Corres and Pallis, 2008). Hong Kong does not want the HKSR to be classified as a flag of convenience.

The Flag State Audit 2003 (Winchester and Alderton, 2003) develops a method of measuring the regulatory capacity of flag states. In overall terms, flag states are grouped into four bands, from 'high' to 'poor', according to the extent and effectiveness of their regulatory regimes. The HKSR was ranked by the audit as 'good' in 2003. In the Audit, it was found that current flag state practice enabled vessels registered the freedom to define a regulatory environment in any way they see fit. A study by Corres and Pallis (2008) extends the assessment allowing for an in-depth empirical assessment of flags performance. In the 'Excellent' flag-state category of the global flag state performance of commercial flags, Hong Kong is one of the three shipping registers together with Bermuda and Liberia that are graded excellent (Corres and Pallis 2008, Table 6). As to the port state control performance of commercial flags, Hong Kong is top of the 'Excellent' flag-state category together with the Isle of Man, Liberia and Marshall Islands (Corres and Pallis 2008, Table 11)..

It is not easy to keep the average age of a shipping register down when the total tonnage is progressively increasing. The average ship's age of the HKSR is 16.90 years when it had its record low in 1997. Fortunately the average ship's age became younger, i.e., 15.64 years when the tonnage of the HKSR revised the falling trend and began to grow in 1998. The HKSR is successful in recruiting younger tonnage into the Register and the average ship's age is more or less steady in a range of 11.2 years to 11.6 years in 2005 to 2008 (see Table 2). In October 2008, the oldest in age, i.e., 12.64 years is the category of general cargo ship; the bulk carrier is in second place at an average age of 11.47 years; container ship is in third place at an average age of 10.06 years; and tanker is in the last

place at an average age of 8.22 years. A fleet of younger age does not necessarily maintain a relatively good performance in quality management and detention rate of port state control reflects better the quality of performance in a shipping register.

The detention rate of a shipping register over a relatively long period of time is a valuable performance indicator in the quality of ship management in the shipping register. The detention rate of the HKSR is lower than the average detention rate under the Paris Memorandum of Understanding (Paris MOU) between 1997 and 2007. The smallest gap occurred in 2004 where the HKSR is in the midst of continued growth in tonnage. The detention rate of the HKSR improves in 2006 and 2007 and it maintains a gap below the average detention rate of the Paris MOU (see Table 3). The difference of the detention rate of the HKSR is even greater from the average detention rate of the Tokyo Memorandum of Understanding (Tokyo MOU) from 1997 to 2007. It is a clear indication that the quality of the HKSR is relatively good. Regular inspections of Hong Kong registered ships are carried out. About 10% of the total Hong Kong registered tonnage was inspected under the Programme of FSQC in 1999. The rate of inspection came down to half at around 5% in 2003/04 because quality ships in the HKSR could be identified through the deployment of the list of deficiency under the Tokyo MOU and Paris MOU. In order to provide incentive for shipowners who have better quality tonnage, a scheme of reducing annual tonnage charge is established. With an aim to encourage a long term and stable registration under the HKSR and to promote the HKSR as a quality shipping register, an annual tonnage charge reduction scheme for Hong Kong registered ships was effective as of February 1, 2006. Under the scheme, for every two years that a ship is continuously registered with the HKSR and provided that the ship has no detention record under any port State control regime during such period, the registered owner of the ship is able to enjoy a six-month annual tonnage charge reduction for the following year (MD, 2008, Section 1.12).

When compared with the FOC, national flags usually give an impression as bureaucratic but not user-friendly. However, user-friendliness does not necessarily conflict with proper control on ship quality. The Hong Kong experience

demonstrates that the user-friendliness can be achieved without compromising proper and effective controls on ships. There are critical success factors which brought the HKSR forward.

VIII. Critical Success Factors of the HKSR

One of the success factors of the ‘new’ HKSR is the determination of Marine Department to revamp the ‘old’ HKSR. The challenge was to change the whole system of the tonnage charge so that it was in accordance with international practice, whereby an entry fee was charged according to the gross tonnage of a ship when she entered and an annual fee levied thereafter. But in the U.K. Shipping Register, a tonnage charge was only levied at registration of the vessel. There was no annual tonnage charge under the British registration system. The change in the tonnage charge coupled with the fee for a survey of the ship would have serious effects on the propensity of shipowners to fly the Hong Kong flag.

Survey fee was another hurdle in the HKSR which Marine Department had to overcome in order to attract domestic and foreign tonnage joining the HKSR. The survey fee was about US\$26,000 to US\$39,000 for an average sized ship when the ship joined the HKSR. Shipowners were negative about the high survey fee together with the annual tonnage fee and informed Marine Department that they were prepared to leave the HKSR when it commenced operation. Marine Department had little room to maneuver because the law which incorporated the regulations of the survey fee and the annual tonnage fee had been drafted and were ready for approval and enactment .

Marine Department did not extensively involve other important stakeholders of the HKSR, e.g., shipowners. But it realised that the issues were vital to the success of the HKSR and swiftly reacted to the serious concerns of the shipping industry on the survey fee and annual tonnage charge by adjusting its strategy and looking for a possible solution from the shipping industry before launching the HKSR on December 3, 1990. One of the issues directly related to the procedure of legislation in Hong Kong. According to traditional practice in the Hong Kong Government,

the stakeholders of the shipping industry had only been informed about the charges under the new fees structure; they had seldom been consulted during the drafting of the fees regulations. In this case the ultimatum from the local shipping industry was that the costs had to match those of international benchmarks if their tonnage was to continue to stay with the HKSR. It was extremely difficult for the Government to make any changes to the legislation of registration at this late stage just before the launching of the Shipping Register in December 1990. A paradigm shift was imminent and an innovative idea was urgently needed to break the standstill between the Government and the shipping industry. Marine Department came up with a ‘new’ service, namely the audit inspection, which would only cost shipowners around US\$6,400 for an average ship instead of the US\$26,000 to US\$39,000 survey fee of entry. In the audit inspection, survey work on the registered ships was delegated to Classification Societies and the surveyors of Marine Department became auditor. The introduction of the audit inspection for entry to the shipping register could cope with the requirements for registration while taking note of the concerns of the shipping industry.

Another success factor of the HKSR directly connected to the paradigm shift in taxation which is an issue of concern to Hong Kong shipowners. Apart from the registration charge and annual tonnage charge on a Hong Kong registered ship, she is subject to profit tax or tonnage tax. Income derived from the operation of ships within Hong Kong or from voyages commencing from Hong Kong waters is generally chargeable to tax under the Inland Revenue Ordinance. Double taxation arises when two or more tax jurisdictions overlap with each other in levying the tax charge, as a consequence the same item of income or profit may be subject to tax in each jurisdiction (MD, 2008, Section 1.16). It was difficult to justify a proposal of reducing taxation for the shipping industry while there was no positive sign that the revenue of the Hong Kong Government might increase due to more tonnage registering in the HKSR. The Hong Kong Shipowners Association put forward a submission to the Hong Kong Government concerning the freight tax imposed by some overseas countries which puts Hong Kong registered ships in a disadvantageous position. Hong Kong Government was convinced and finally agreed and the Finance Bureau examined the issue of taxation of shipping in the

context of the Government's review of profits tax so as to create a level playing field for Hong Kong shipowners (Ip, 1997). A double taxation agreement may either be a comprehensive one covering various incomes including transport income or be limited to transport income only covering shipping income or both airline and shipping income. The Hong Kong Government negotiated with a number of its close trading partners, who did not have reciprocal exemption provisions in their domestic tax laws (MD, 2008, Section 1.16). The Central Government is supportive to the growth of the HKSR.

Beijing indirectly became a drive on the development of the HKSR. The Central Chinese Government's 11th Five-Year Plan 2006-2010 (Chinese Government, 2006) gave unequivocal support to the development of Hong Kong's logistics industry and the maintaining of its position as an international maritime centre. In response, the government in Hong Kong set up a Focus Group on Maritime, Logistics and Infrastructure to consider and develop strategic proposals and policies which could be adopted to meet these objectives. In January 2007, the Focus Group issued a report (HKSAR Government, 2007), arguing that Hong Kong should make appropriate adjustments to its existing policies and measures, so as to provide an infrastructure conducive to the development of the logistics industry and improve its business environment in order to enhance the competitiveness of the whole industry. In respect of taxation, the Focus Group made two broad recommendations namely to introduce a tonnage tax system and increase the number of tax treaties that Hong Kong has concluded with other countries (KPMG, 2007). The Hong Kong Government actively negotiated and concluded avoidance of double taxation agreements with other trading partners HKSAR 2007. On February 11, 2009, the Hong Kong Government bilaterally signed Double Taxation Avoidance Agreements with twelve countries (DoJ, 2009).

The Focus Group on Maritime, Logistics and Infrastructure also proposed to consider making reference to overseas practice to make tonnage tax as an alternative to the profits tax currently imposed on vessels. The Hong Kong Government needed to further assess the feasibility and implications of the proposal and to consult the industry on the impacts of Tonnage Tax on the

policy to attract shipowners to register in Hong Kong and the current tax system (HKSAR Government, 2007). Tonnage tax is a special tax regime that many countries have introduced to provide a more straightforward and preferential calculation of the taxable profits of shipping companies. Broadly, under a tonnage tax regime, shipping companies will determine their income according to the net tonnage per qualifying ship multiplied by a fixed amount. Thereafter, the normal corporate tax rate will be applied on this income to arrive at the shipping company's tax liability. The method of tonnage tax is simpler in that it does not require the exact assessable income and deductible expenses to be ascertained. Tonnage tax is not a separate type of tax, but is essentially an alternative way of computing tax liabilities for shipping companies. It is usually optional and shipping companies can elect whether or not to be subject to the tonnage tax regime. Countries like Denmark, Germany, India, Ireland, Italy, Netherlands, Norway, the UK and the US have already adopted a similar approach in tonnage tax (KMPG, 2007). Chinese shipping companies look for international shipping register with high quality so that they can have another international platform to register their tonnage.

The flagging out of Chinese shipping companies in the Mainland to the HKSAR is a critical impetus in the growth of the HKSAR. Chinese flagging out started in the 1950s, in a relatively small scale, due to western embargo policies. Chinese trade was carried by joint venture companies set up with socialist partners such as Poland, Czechoslovakia and Albania, and later seized trading opportunities with countries China had not as yet established diplomatic relations. Flagging out took massive dimensions and momentum after the open-door policy in 1978 under the consequences of taxation, profitability and operational considerations (Haralambides and Yang, 2003).

One major factor for the success was a shift in paradigm in the culture of customer service within Marine Department. A project of re-engineering for improving customer service in a government department could be conducted from time to time while shifting its paradigm in the culture of customer service is completely another issue. There is an apparent change in the attitude towards customer service in Marine Department. After careful consideration, a one-

stop-shop approach in the registry of shipping was adopted and implemented in Marine Department as previously there had been more than one section of Marine Department which was involved in registering a ship in Hong Kong. A one-stop-shop service allows shipowners to process ship registration, applications for manning certificates and seafarers' licenses, survey arrangements and radio station licenses at one location in Marine Department. Another major change is that the staffs of the HKSR in Marine Department provided a service for shipowners outside office hours or during holidays, if requested (MD, 2007). An office in Marine Department could handle or assist with all the issues of registry of a ship after the implementation of the one-stop-shop approach. The change of working pattern in Marine Department is one of the success factors in the growth of the HKSR and a critical shift in paradigm in a government department.

Apart from the issues of quality, regulations, charges and communication, in recent years Marine Department has been successful in the simplification of procedures as well as the maintenance of the role of Marine Department in the control of the quality of registered ships under the HKSR. Among the stakeholders in the private shipping sector, Marine Department also relied on the consultative committees, which represent wide coverage in different sectors of the shipping industry in Hong Kong, for feedback and advice. Task Forces were formed under the Maritime Industry Council. The Hong Kong Shipowners Association also had various committees taking care of different issues in the shipping industry and the Hong Kong Shipowners Association invited from time to time the participation of Marine Department on specific issues of concern to the shipping industry. Marine Department continued to enhance the HKSR by taking a number of measures to make the HKSR more user-friendly. These included the introduction of bilingual certificates, the publication of a user handbook, and the use of the Internet to disseminate information. Hong Kong under the Basic Law does not have jurisdiction in foreign affairs and Beijing assists Hong Kong shipowners when their ships require diplomatic assistance outside Hong Kong and China.

Diplomatic assistance in emergency (MD, 2007) offered to shipowners is one of the important factors in choice of shipping register. The Hong Kong Government

obtained the support of the Central Government when diplomatic assistance is required overseas. The Ministry of Foreign Affairs agreed to assist and issued an instruction for PRC embassies and consulate offices overseas to provide consular assistance for Hong Kong registered ships when required (Ip, 1997). International shipping faces many potential threats arising from both ‘normal’ crime and terrorism due to the fact that merchant shipping is highly vulnerable (King, 2005). The piracy attacks against merchant shipping off the coast of Somalia are under the spot light internationally. The London-based International Maritime Bureau said more than 100 vessels had been attacked in the coast of Somalia in 2008 and 14 ships were held for ransom in January 2009, including Saudi supertanker ‘Sirius Star’ and the ‘Faina’, a Ukrainian cargo vessel carrying 32 military tanks. In response to the issue of safety of seafarers and cargoes on board Chinese merchant ships, a Chinese naval fleet arrived on January 6, 2009 in the waters of the Gulf of Aden off Somalia to carry out the first escort mission against pirates (People’s Daily, 2009a). Soon after its arrival, the fleet conducted its first escort service for four Chinese merchant vessels, including one from Hong Kong (People’s Daily, 2009b). The Hong Kong Government does not have the capacity to provide the coverage in protecting its Hong Kong registered ship overseas.

IX. Conclusion

The gross tonnage under the Hong Kong flag was 6.3 million tons in 1990 when the newly established HKSR began operation and it fell to merely 5.5 million tons in November 1997. On May 2009, the registered tonnage was 41 million tons in the HKSR. The study through interviews analyses the paradigm shift in the shipping registry policy in Hong Kong which led to a successful revitalization of the registered tonnage. The paradigm shifts included the revision of the law of shipping register which required the approval and assistance of the Central Government in Beijing prior to the handover in 1997; the formulation of a new policy for the HKSR which involved the interests of different stakeholders; the new approach in reaching an agreement for Hong Kong registered ships which

call at Taiwanese ports which was a highly unpredictable task in the political arena between China and Taiwan; the breakage of the standstill between the Government and the shipping industry by coming up with audit inspection system; the changes in the policy of taxation for Hong Kong registered ships which was a sensitive issue relating to income of Hong Kong Government; and the significant change of attitude in the culture of customer service within Marine Department which is definitely one of the corner stones of the revitalization. Statistics demonstrated to the shipping industry and the Hong Kong Government that the quality of ships registered in the HKSR has not been compromised despite its continual growth in last decade.*

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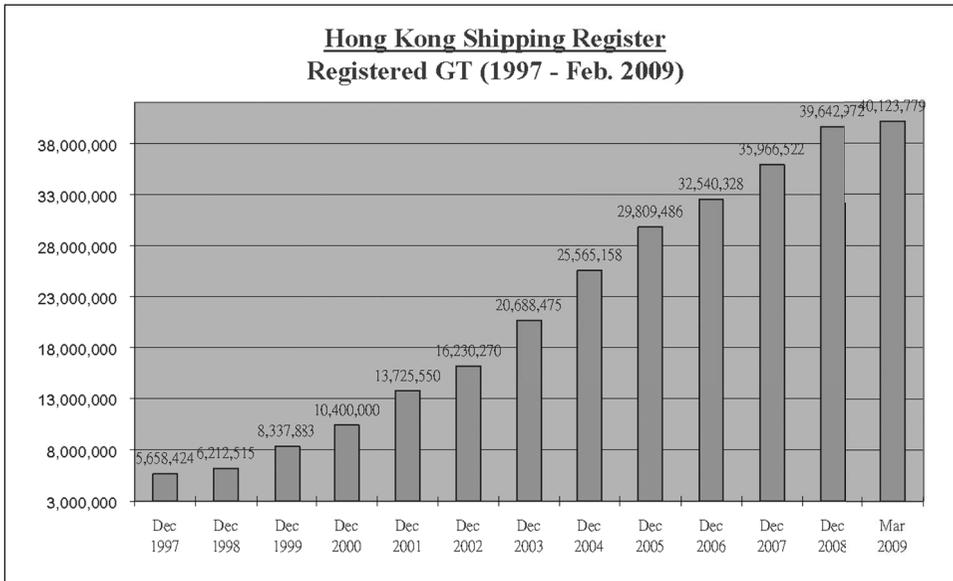
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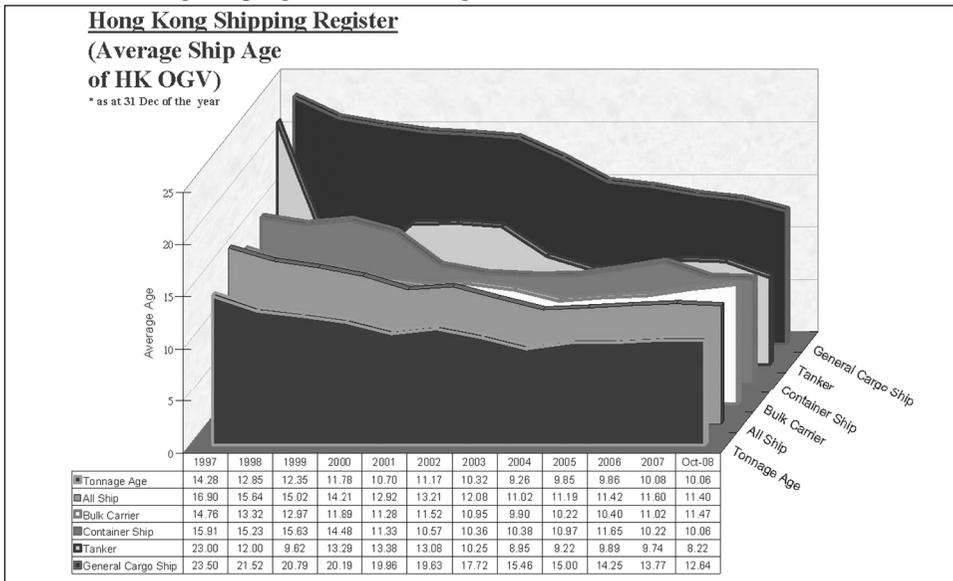
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<Table 1> Registered Gross Tonnage from December 1990 to February 2009 in the HKSAR



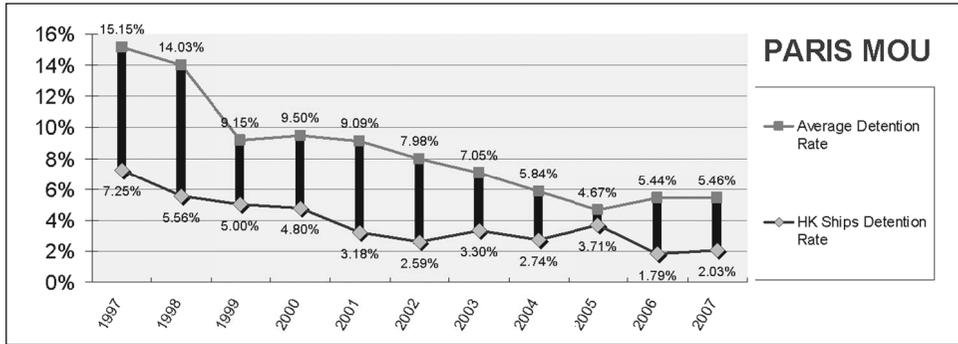
Source: Marine Department

<Table 2> Average Ship Age of Ocean Going Vessels of the HKSAR

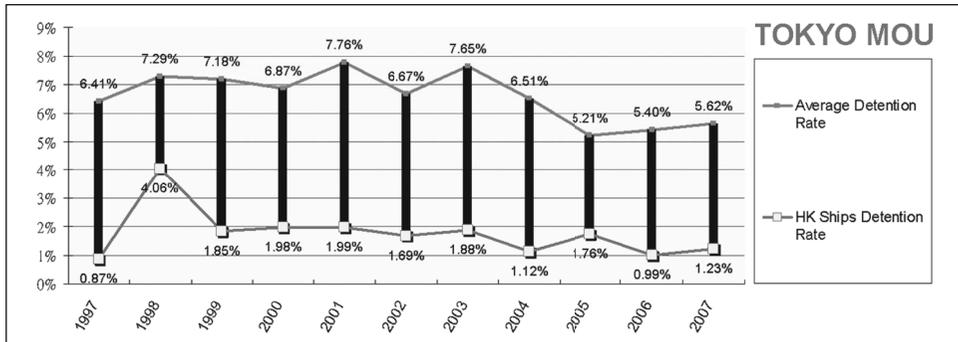


Source: Marine Department

<Table 3> Average Detention Rate and Detention Rate of Hong Kong Registered Ships in Paris MOU & Tokyo MOU in 1997-2007



Source: Marine Department



Source: Marine Department