

2nd session

**“Russian International Ship Register:  
organizational and tax aspects”**

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## “Russian International Ship Register: organizational and tax aspects”

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On the 20th December, 2005 the Russian Federal Law No.168-FZ on Amendments to Certain Russian Legislative Acts Relating to the Establishment of the Russian International Ship Register was adopted. The Law came into force on the 23rd January, 2006.

The adoption of this Law has become the most significant event in the legal regulation of the Russian Federation merchant shipping since the introduction of RF Merchant Shipping Code enforced on 1st May, 1999.

The FL draft Explanatory Note stated that the goal of establishing the Russian International Ship Register was to provide for economic and organizational conditions of functioning Register-based Russian ships granted by all advantages of “flag of convenience”.

The Explanatory Note offered the following reasons for adopting such a law:

Under contemporary market conditions Russia’s shipping companies undergo serious economic difficulties in the competitive struggle in the world transport services market. Over the last 10 years (1995-2004) the merchant navy under the Russian flag has declined (from an overall deadweight of 9.5 million tons in 1995 to 2.6 million in 2004) and foreign currency earnings from international sea shipping have also reduced from 508.7 mln USD in 1995 to 200 mln USD in 2004. Ships withdrawal in offshore zones started in 1992 and is ongoing at this time. In 1992 the share of ships under foreign flags amounted to 18.4% of the total Russia’s tonnage, but at the beginning of 2005 this share amounted to about 58%. Unless this trend is stopped no sea vessels under the Russian flag will be left by 2010.

One of reasons for the crisis amongst Russian shipping companies is the high tax share of transport services cost, particularly comparing to the “convenience flag” countries (such as Liberia, Marshall Islands, Bahamas Islands, Cambodia, etc.). Among others it doesn’t allow ship owners to reproduce fixed assets which results in the reduction of Russian Navy. Out of 211 ships which were built for Russian ship owners in 1992-2004 over 90% operate under the foreign flag.

This can be explained by two main reasons:

- rejection of foreign banks granting ship building credits to ship owners to accept as pledge ships under the Russian flag;
- high custom duties when registering ships both built and purchased abroad.

To ensure a favourable investment climate in the industry and retrieval of ships under the Russian flag the government support is required which will stimulate the fleet revitalization including by indirect methods based on cost-free solutions. One of such methods is the establishment of the Russian International Register.

In view of the Russian legislators the establishment of the International Ship Register will contribute to addressing the following issues:

- involvement in the Russian registration of new-built Russian ships currently putting out to “flags of convenience”;
- involvement in the Russian registration of the ships owned by Russian shipping companies and operating under foreign flags;
- involvement in the Russian registration of foreign ships whose operation requires a Russian flag;
- revitalization of national shipbuilding and ship-repairing sectors;
- acquisition of ship registration dues income by the national budget.

The analysis of the foreign experience illustrates that over the past decades many leading maritime states have been establishing International Ship Registers to hold ships under national flags.

Among the countries which opened such Registers are Norway, Denmark, Great Britain and the Netherlands. This was the measure which prevented national fleets exodus under “flags of convenience”, projected in 70-90-s and entailing the reduction of the total tonnage of EC member countries’ ships from 32 percent of the world tonnage to 14 percent.

The key feature of such International Registers is the ban for cargo transportation between national ports.

This positive practice was adopted by Russian Federal Law No.168-FZ dated 20th December, 2005.

The Russian International Register Law stipulates for imposing upon registered ships a special tax regime providing economic conditions similar to those in foreign countries where such International Registers have been created, with respect to such ships operation.

The ships which are exclusively used for international shipment can be entered into the Russian International Register. The Register provides for two types of ships registration:

- 1- for Russian ships owned by Russian legal entities and citizens of Russian Federation;
- 2- for foreign ships chartered by Russian freighters under bareboat charter contracts.

At the same time the Register provides no restrictions regarding ages of the ships .

The tax regime for ships included in the Russian International Register envisages the payment of state registration duty and its annual validity extension fee. So, a new special tax regime has been introduced for previously not existed tax entity which is the ship listed in the Register. At the same time the ship owner does not have to pay the following taxes relating to such ship operation:

- income tax,
- VAT (including ship imports),
- transport tax,
- property tax.

The ships listed in the Russian International Register are exempt from customs duty. The estimate of the state registration duty amount was based on the level of weight-average tonnage rates of three countries: Liberia, Cyprus and Malta in which 96% of foreign Russian Navy are registered.

Though the Law title has such words as “on Amendments... Relating to the Establishment of the Russian International Ship Register” no separate Legislative Act was adopted with respect to the Register. The Russian International Ship Register “was created” through introducing amendments and additions to the following Russian Federation Laws:

- Merchant Shipping Code,
- Tax Code and
- Customs Tariff Law.

The ship registration in the Russian International Ship Register is to be confirmed on the yearly basis. The procedure for confirmation of ships registration is specified by Regulations for Ships Registration and Rights for Ships in Sea Trading Ports.

The Law proceeded with the following regulatory acts:

1. RF Government Instruction No.583-r dated 25th April, 2006 on Approval of the List of Sea Trading Ports whose Captains Perform Registration of Ships in the Russian International Ship Register.

2. RF Ministry of Transport Order No.87 dated 21st July, 2006 on Approval of Regulations for Ships Registration and Rights for Ships in Sea Trading Ports.

3. RF Government Instruction No.1116-r dated 13th August, 2006 on Entitlement of RF Ministry of Transport on behalf of RF Government to Exercise Actions Relating to Authorization of Foreign Classification Societies – Members of International Association of Classification Societies with Powers of Inspecting Ships Registered in the Russian International Ship Register.

Indicated Regulations for Ships Registration in Sea Trading Ports stipulate for accessible and easy for Russian original and disponent ship owners procedure for registration of ships in the Register including the re-registration of ships listed in the Russian State Register of Ships or Russian Bareboat Charter Register. Specifically, the re-registration of the foreign ship chartered by the Russian disponent ship owner under bareboat charter from the Bareboat Charter Register to the Russian Interna-

tional Ship Register requires neither executing a new bareboat charter nor obtaining a new permit for sailing under RF National Flag.

It is fair to say that the Law No.168-FZ dated 20th December, 2005 provided necessary conditions for functioning the Russian International Ship Register. Along with this, the Law is being implemented very slowly. The main reasons for this slowdown include:

1- obviously ineffective phraseology of basic provisions of the Law entailing their different interpretation by tax and customs authorities;

2- missing Law enforcement instructions to executive authorities;

3- RF Federal Customs Service's denial of a possibility to use customs duty exemption, which is stipulated by the Law, by ship owners without adoption of the Decree by RF Government.

Currently neither tax nor customs authorities have adopted any regulatory act to implement the Law. For instance no official interpretation has been provided, no practice (including legal) has been developed and, correspondingly, no consequences of terminating registration prior to 10-year registration for both Russian ships (purchased by Russian ship owners in Russia or abroad or re-registered from the Russian State Register of Ships) and foreign ships chartered under bareboat charter are evident.

Due to this **uncertainty** the Law has not started working yet and Russian shipping companies beware of enlisting the ships into the Russian International Ship Register. As of the 1st January, 2007 only few ships had been entered the Register in southern Russian ports: 1 vessel - in Novorossiysk port, 0 - in Tuapse port and 17 ships – in Taganrog port. Notably, these registrations were made as the re-registrations of Russian ships previously registered in the State Register of Ships and foreign ships under Russian flag previously registered in the Bareboat Charter Register.

This Russian ship owners' careful policy relating to the registration of their ships in the Russian International Ship Register seems to be the most sensible at present.

The current situation will probably improve in 2007 through the following efforts of Russian authorities:

1. Adoption of RF Government Decree discussed since September 2006 on customs duty exemption in regard to ships included into the Russian International Ship Register.

2. Issue of the Regulatory Act by RF Federal Tax Service which clarifies the procedure for ship owner tax exemption specified by the Law.

3. Issue of the Regulatory Act by RF Federal Customs Service which clarifies the procedure for ship owner exemption from customs duties specified by the Law.

It is presumed that the implementation of the indicated activities will allow to address the objectives of the Federal Law No.168-FZ and to balance tax and organizational conditions of Russian ship owners' business with their foreign colleagues' conditions which will enable the Russian companies to sustain a severe competition in the international shipping market with no change in the Russian Flag or Russian ships "citizenship".

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