



**DALHOUSIE**  
*University*

**RECENT DEVELOPMENTS IN  
INTERNATIONAL SHIPPING POLICY AND  
THEIR IMPLICATIONS  
FOR CANADA**

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**MARINE AFFAIRS PROGRAM**

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An examination of recent fiscal and other trends and developments in the international shipping policy of developed (principally European) countries, and a preliminary assessment of the possible benefits of adoption of similar initiatives by Canada.



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# CHAPTER 1 – INTRODUCTION

## 1.1 Overview

While globalization is regarded as a comparatively new phenomenon by most commercial sectors, it is certainly not new to the shipping industry. Indeed, globalization trends have been a fact of life for many years in the marine transportation field. It has been exemplified in particular by the emergence of ‘flags of convenience’ and their impact on existing norms for taxation, manning, registration, and so on. For a number of years, most established maritime nations chose (or at least felt obliged) to pursue a ‘laissez-faire’ approach in responding to this trend. However, growing concern regarding the negative consequences on their long-term national shipping interests has led to some important policy initiatives over the past decade; a number of leading maritime countries, particularly those in Europe, have undertaken substantive changes to their national policies to counteract the dominance of open registry vessels in international shipping.

Among the key concerns of traditional maritime nations has been the perceived erosion of shipping knowledge and expertise in their countries. This erosion has been viewed with particular unease in Europe as threatening the continued viability and success of European shipping industries and, ultimately, their stature and influence in international shipping fora. There have also been growing concerns regarding marine safety and damage to the environment, attributed principally to the fact that certain States that offer open registry facilities do not have, and do not appear able or willing to provide, the resources necessary to ensure acceptable safety standards on the ships that fly their flag. The recent incidents involving the tankers *Erika* and *Prestige* have served to validate this concern.

The problem has been viewed as sufficiently serious by a number of European countries to justify substantive mitigating action, directed at encouraging the positioning of effective ownership, management, and to some extent registration of ships in their respective countries, and to stimulate recruitment and training of their nationals. Initiatives have taken some or all of the following forms:

- Fiscal relief, through the introduction of an optional ‘tonnage tax’, where the tax to be paid is based on the tonnage of each (qualifying) vessel irrespective of profit or loss.

- Initiatives to make the national flag registration process simpler and easier, hence cheaper, more appealing and user-friendly, while not sacrificing safety standards.
- Income tax relief for national seafarers serving on national flag ‘qualifying ships’, by treating wages as foreign earnings, and in this way reducing to manageable proportions the differential in costs between most OECD countries and current sources of low cost crewing.
- In certain instances (e.g., the United Kingdom), an accompanying obligation imposed on those companies operating ‘qualifying ships’ under a ‘tonnage tax’ regime, to provide billets for national trainees, an initiative designed to provide an additional stimulus to the expansion of shipping knowledge and expertise.

The concerns that these steps have been designed to address are not new to Canada. Indeed, in the early 1990s, principally in response to perceived issues that were not dissimilar to those being addressed in Europe, and flowing from recommendations made in a 1985 review of international shipping policy, Canada adjusted its tax regime as it applied to international shipping activities, and encouraged the establishment of International Maritime Centres, all with the aim of expanding Canada’s maritime knowledge, expertise and involvement in international shipping. These steps have been evolving over the last decade and now merit examination as to their effectiveness in achieving their original objectives.

In particular, the adoption of a ‘tonnage’ tax approach and other measures by many of Canada’s trading partners raises important questions for Canada with regard to the future direction of its own international marine transportation policies and how they might best be achieved. Accepting that Canada’s policy objective of attracting shipping knowledge and expertise remains, while at the same time recognizing that progress made to date in achieving that objective appears limited, this study is intended to evaluate whether or not it makes sense for Canada to adjust its present approach, and in particular to examine whether Canada should pursue a strategy similar to that being adopted by a number of European countries.

## **1.2 The Aim of the Study**

The principal objective of this study is to conduct a broad review and evaluation of current trends in international (deep-sea) shipping policy, focusing in particular on the rationale and objectives of the recent innovative and far-reaching fiscal and other initiatives taken by certain European countries, with the endorsement of the European Commission.

As part of this evaluation, the study also undertakes to provide an overview of how Canadian deep-sea shipping policy has evolved since the late 1960s and, while somewhat

handicapped by lack of extensive data and information, the study also makes a broad assessment of the policy implementation initiatives adopted by Canada since the mid-1980s.

In reviewing recent international trends, the study examines the rapid and widespread introduction of the new 'tonnage tax' policy, which has to date been adopted by at least nine European countries (Greece, Netherlands, Denmark, Norway, United Kingdom, Ireland, Germany, Spain and Finland). Several others, including France and Belgium, have announced plans to do so. The study also explores the arguments and circumstances that have supported the adoption of this important fiscal initiative, the principal elements of the policy, and the broad parameters (the 'ring fence') that define, in a fiscally manageable way, the limits of application of this tax treatment to shipping and marine transportation-related activities.

The study assesses the early results of these initiatives, so as to evaluate whether or not they are achieving the objectives set for them. Based on these findings, the study offers some preliminary views as to whether adjustments to Canada's current deep-sea shipping policy position appear merited.

### **1.3 What is Not the Aim**

An important caveat should be stressed at the outset. It is not the aim of this study to make any recommendations with regard to the deep-sea shipping policy regime that Canada should adopt, nor, more specifically, to argue for Canadian registry in any form as a principal goal. Its primary objective is to offer insights into the new and far-reaching policy directions being pursued by many, if not most, of Canada's OECD partners, and to provide a broad illustration of what Canada's deep-sea shipping policy regime might look like, were it to adopt similar measures. In this way, hopefully the study can provide 'grist to the mill' in advancing Canada's deep-sea shipping policy thinking.

### **1.4 Broad Methodology**

The quite modest scale of the study has meant that it has had to rely primarily on literature and electronic data and information searches. It has, however, been supported by written exchanges and telephone interviews with selected parties where clarification on important points has been required, particularly in relation to the evolution of the International Maritime Centre concept. The lack of a comprehensive program of consultation with Canadian shipowners and others must inevitably qualify the views and observations presented in this report. In this respect they should not be regarded as final positions, but rather as premises that require further discussion, debate and no doubt



adjustment as ideas are evolved and refined. The study should be read with this consideration in mind.

## **1.5 The Organization of this Report**

Chapter 2 provides a summary of the evolution of Canada's international (deep-sea) shipping policy from the late 1960s to the mid-1980s. In particular, it broadly reviews each of the main studies and reports that have been undertaken since that time, and summarizes the principal findings of each. It endeavours to shed light on the policy preoccupations of the day, and how those policy preoccupations evolved over time.

Chapter 3 provides a summary description of the fiscal and other initiatives that were taken in the 1990s to provide an attractive environment for the owners and operators of international shipping to locate the 'mind and management' of their operations in Canada. In particular, it looks at the efforts made to establish International Maritime Centres, notably in Vancouver, but also in Halifax, Montreal, Toronto and Saint John. The chapter endeavours to shed light on the degree to which the initiatives taken by both federal and provincial governments achieved the objectives set for them.

Chapter 4 offers summary descriptions of international shipping policy developments that have recently occurred in a number of developed countries, particularly in Europe. It broadly reviews the marine transportation policy directions adopted by the European Commission and, in particular, examines the Commission's state aid guidelines, which have essentially provided the framework for the fiscal and other initiatives pursued by Member States. The chapter then reviews the initiatives adopted by certain Member States as well as other non-European states, including the United States. It then provides, by way of a case study, a detailed review of the initiatives adopted by the United Kingdom, including the considerations and circumstances that led to the changes, and the studies and other activities undertaken. The case study summarizes the resulting comprehensive shipping policy, examining the merit or otherwise of moving to a tonnage tax regime, as one element in the implementation of the new shipping policy. The chapter concludes with a broad assessment as to the degree to which the initiative may be seen as successful.

Chapter 5 explores the implications for Canada of these international policy initiatives. It summarizes what may be viewed as its 'de facto' policy position on deep-sea shipping, and the initiatives it has in place as the principal means for implementing that policy. It then examines Canada's policy from a number of perspectives and offers some preliminary views as to whether changes in Canada's policy stance may be merited.

# CHAPTER 2 – A SUMMARY OF THE EVOLUTION OF CANADA’S INTERNATIONAL SHIPPING POLICY

## 2.1 Canada’s Early Involvement in Deep-Sea Shipping

It may come as some surprise to many Canadians, whose appreciation of the evolution of Canadian transportation is generally more focussed on the romantic stories associated with the construction of the trans-continental railways, that their country has had a long history of strong interest, and participation, in deep-sea shipping. Indeed, there have been moments in this evolution that Canada has been in a position to claim to be among the world’s leaders in this important transportation sector. However, these moments have been brief and the nature and scale of Canada’s participation have fluctuated quite widely over the years.

In the early 1800s, Canada’s roots as part of the British Empire led rapidly to its active involvement in international trades, and because of its huge resources of lumber, Canada also became a major participant in the wooden hull shipbuilding industry. This pre-eminent position was not to last, however, and emerging technology in the form of the steel hulled steamship in the middle to late 1800s was to lead to a major downturn, and ultimately the first serious demise of the Canadian shipbuilding and operating industries.

This steady contraction continued until the outbreak of the First World War, at which time there was virtually no Canadian deep-sea merchant marine. Again the war, with its significant demand for shipping, provided the stimulus needed for the next cycle with a new expansion of the Canadian steel industry, and its re-entry into substantive shipbuilding. So there emerged a new Canadian-built and -operated fleet.

At the end of the war, recognizing the large number of Canadian-built and -operated ships, the government decided to maintain the new fleet under public ownership. This decision led to the establishment of the Canadian Government Merchant Marine Limited, which in the early 1920s was operating over 60 ships on a worldwide basis. Again, for a variety of reasons, mainly related to low-cost competition, declining freight rates, significant further advances in ship technology internationally, and a lack of capital to modernize its fleet (despite submissions to government for some form of fiscal or

financial relief), the company was forced to close in 1936. By the outbreak of the Second World War, the Canadian flag deep-sea fleet had again contracted to the point where it constituted little more than about 20 ships operated by three companies: Imperial Oil, Canadian Pacific and the Canadian National Steamship Company.

As with the First World War, the Second World War provided a significant stimulus to Canadian shipbuilding, with the UK placing an order for some 26 ships of about 10,000 dwt. These ships, together with several others from Canada's domestic fleet that were modified for use in international trade, formed the nucleus of a new Canadian flag merchant fleet that, in 1942, was placed under the administration of the publicly owned Park Steamship Company Limited. By the end of the war, this company was operating 150 Canadian-built, Canadian-registered, Canadian-manned ships—the fourth largest merchant fleet in the world.

Immediately after the war, a renewed optimism and enthusiasm pervaded the Canadian shipping industry. As part of this climate of optimism, Park divested most of its ships to private operators, and the government established the Canadian Maritime Commission to oversee the economic health and prosperity of the fleet. Despite this renewed interest and action by the government, circumstances again conspired to place Canadian flag shipping in a difficult commercial situation. These circumstances included continuing evolution in technology, growing disparities in wage levels between developed and developing countries, and international post-war assistance programs that led eventually to the emergence of low-cost registries—the concept of 'flags of convenience'—particularly in Liberia.

In 1949, recognizing the clear inability of Canadian ships to compete internationally, the Commission released a report recommending to the government that a nucleus of ships and shipbuilding be established and maintained, principally for national security reasons. The government chose not to act on this recommendation and instead put in place measures that facilitated transfer of the remaining ships to the British registry. With virtually no conditions enabling Canadian flag vessels to compete effectively, the decline in the Canadian deep-sea fleet continued, so that by 1969 Canadian ocean-going merchant tonnage totalled no more than 70,000 grt, with only four vessels in this fleet exceeding 1000 grt.

Other developments in Canadian transportation policy thinking also had important impacts on Canadian shipping policy development. In particular, the publication of the report of the MacPherson Commission in 1961, and the subsequent *National Transportation Act of 1967*, led to the establishment of the Canadian Transport Commission, and a renewed focus and priority on policy formulation in all modes. The question of the appropriateness of Canada's policy position on deep-sea shipping was raised. Over the course of the next 15 years, a number of studies were undertaken

directed at this question. What follows are synopses of the more important of these studies, so as to shed light on how Canada's shipping policy perspective has evolved since the late 1960s.

## **2.2 Hedlin Menzies Study (December 1970)**

This report, *Canadian Merchant Marine: Analysis of Economic Potential*, was prepared for the newly established Canadian Transport Commission by Hedlin Menzies and Associates Ltd. It examined "the economic feasibility of developing a modern Canadian flag deep-sea merchant fleet." Four objectives were stated at the outset:

1. To identify prototype ships that would result in minimum carrying costs for each major Canadian deep-sea bulk trade.
2. To evaluate the cost of privately owning and operating prototype Canadian ships compared to precisely similar foreign flag ships assumed to be engaged in the same trades.
3. To evaluate the potential benefits and costs to the Canadian economy that would be associated with the operation of privately owned deep-sea Canadian ships.
4. To evaluate the public cost of practical means of encouraging development of privately owned deep-sea Canadian ships, assuming that Canadian ships would operate within a free and competitive shipping environment.

The focus was on bulk cargo trades (liquid and dry) in large vessels ranging from 25,000 to 300,000 dwt. Coastal and Great Lakes shipping were excluded from the study.

Part I of the report provided an overview of changes in Canadian and global shipping from the 1850s to 1970, with emphasis on 'recent' technological developments and the forms of government intervention found worldwide. Part II outlined the 'trade model' framework of analysis; it examined 26 selected trade routes to and from Canada's east and west coasts, correlating this information with commodity, vessel type and vessel costs to suggest 'near-optimum' vessel types for each route. Part III presented an economic evaluation of 'potential' deep-sea Canadian vessels, and the final section, Part IV, discussed policy issues relating to the development of the new fleet, and in particular manpower concerns and possible government assistance programs.

Three major points may be drawn from the report:

1. No clear connection could be made between the establishment of a Canadian deep-sea fleet and Canada's trade and maritime interests. As the report suggested, "Canada's trade flows, shipping rates, ship technology, quality of shipping services

and level of shipping expenditures in Canadian ports would be relatively unaffected by the introduction of Canadian flag ships.”<sup>1</sup>

2. Only bulk-type vessels of 90,000 dwt or over, and exceeding C\$10 million in ‘world capital cost’, were considered by the report to be ‘potentially economic’. Smaller and less costly vessels were deemed either ‘probably uneconomic’, or able to generate ‘only marginal Canadian net benefits.’
3. Citing high operating and tax costs for Canadian vessels, the report suggested that were Canada to proceed with the development of a privately owned deep-sea fleet, “some form of government financial assistance” would be required. Preferred methods suggested included loan guarantees, investment grants and allowances, and government loans.

As the focus was solely on Canadian flag vessels, the report did not look at the costs and benefits offered by other operating options such as Canadian-owned foreign flag vessels. The report did make a clear case that trading interests and shipowning interests were divergent and signalled the start of the long debate on what policy would be in the Canadian public interest.

### **2.3 Study by H. J. Darling (August 1974)**

Again the focus of this study was on the feasibility of operating Canadian flag ships. Commissioned by the Marine Transport Administration of the Department of Transport, *The Elements of an International Shipping Policy for Canada* by H.J. Darling aimed to provide “a brief résumé of the background and issues in any projected development of Canadian flag deep-sea shipping, with emphasis on the policy options available, their relative importance and practicality and the priorities and coordination necessary to initiate an effective and economic policy.” Citing the focus of the study as an examination of the “needs, scope and implementation of an international shipping policy,” it differentiated itself from the economic feasibility questions of the 1970 Hedlin Menzies study.<sup>2</sup>

Darling suggested that there were two opposing views permeating the debate on international shipping in Canada. These were, on the one hand, what he termed the ‘unrealistic’ calls for a Canadian flag fleet that had “no solid basis in concrete Canadian interests”; and on the other, a possibly excessive level of confidence in the workings of a competitive international shipping industry, which tended to create ‘indifference’ towards any need for change in Canada’s laissez-faire shipping policy.

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<sup>1</sup> Hedlin Menzies & Associates Ltd. (1970), *Summary of Canadian Merchant Marine: Analysis of Economic Potential* (Para 23).

<sup>2</sup> Darling, Howard J. (1974), *The Elements of an International Shipping Policy for Canada*, p. 1.

Canadian shipping policy, Darling argued, was poorly conceptualized to begin with, and a re-orientation was needed before any policy could be effective. Specifically, a clear distinction needed to be made between Canada's core *interests* and its *advantages* where shipping was concerned—while a national flag fleet might have represented the latter, its absence was no threat to the former, which was based on trade and the ability to move key commodities.<sup>3</sup>

Citing overseas trends toward nationalism, bilateralism and subsidization, the report suggested that Canada's commitment to laissez-faire principles threatened to make it a "unique case among the world's main trading nations."<sup>4</sup> The report contrasted the more focused and purposeful posture of the United States with a Canadian shipping policy administration characterized by departmental fragmentation.

Darling also stressed that the interests of shipping and shipbuilding were not necessarily identical, and it was inappropriate to strive for policy convergence between the two groups. He also drew attention to the low numbers of Canadian seafarers in deep-sea shipping and observed that this situation offered both advantages and disadvantages in the consideration of policy options for Canada.

Darling suggested that the 'principal interest situations' that merited attention included:

- Canadian resources moved in the bulk trades, e.g., ore and coal.
- The role of Canadian ships in Arctic development.
- The examination of Canadian interests with respect to container consortia, and the impact of their operations on Canada/US port competition
- The consequences of other countries' bilateral policies.
- The position of Canadian ports in the light of modern shipping trends.<sup>5</sup>

The heart of the report lay in Sections VII through X. In particular, Section VII outlined 'general strategies for a deep-sea shipping policy', and contained six key elements:

1. A general policy statement from the government as an 'essential starting point', that also served to "legitimize the responsibility of a Department or Agency for shipping policy."
2. A change in the view of Canadian flag ships from an 'isolated objective' to something 'closely integrated into a general shipping policy.'

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<sup>3</sup> Darling (1974), see in particular pp. 2-3.

<sup>4</sup> Darling (1974), p. iv.

<sup>5</sup> Darling (1974), p. viii.

3. The organization of shipping policy to respond to ‘different kinds of interest situations’ that could arise. This flexibility would allow the promotion of Canadian flag shipping to become an objective if ‘favourable conditions’ were to arise.
4. The use of ‘existing structures’—e.g., third flag shipping, whether Canadian operated or not—‘wherever they offered the most effective means of dealing with particular issues.’
5. A ‘practicable plan’ of assistance that could respond to unique and to common cases, and which could be implemented at the discretion of ‘the shipping authority’.
6. The development of a ‘positive and flexible’ approach to assistance in general, which would enable the government to use assistance tools selectively, i.e., without making them part of a general assistance plan.

The report concluded by suggesting a series of steps in the implementation of an ‘effective’ shipping policy, each of which was intended to respond to a perceived shortcoming in the existing Canadian framework. They were:

1. a positive attitude toward shipping problems, ‘a recognition that they are important in themselves and not merely a troublesome residue of other more important problems;’
2. a consolidation of authority for dealing with shipping policy;
3. effective powers for such an authority; and
4. a readiness to take the initiative in the use of the powers granted.

Finally, eight specific ‘policy recommendations’ were made as follows:

1. Centralize control and administration of international shipping matters; assign effective powers to ‘deal with interest situations and pursue long-term objectives.’
2. Announce a policy stance that defined Canadian interests, sensitized other countries to these interests, and mobilized public opinion.
3. Deal directly with countries ‘whose shipping policies affected their trade with Canada.’
4. Liaise closely with Canadian shipping companies and associations that were active internationally.
5. Provide a policy document to specify the role of Canadian shipping in the exportation of ‘Arctic and other bulk commodity resources.’
6. Provide the shipping authority with a ‘wide choice of methods’ with which to respond to the range of interest situations that could arise.

7. Develop a two-level support program for Canadian flag shipping.
8. Allow 'special methods' of threat response by the shipping authority (perhaps through standing committees) to cover port development, trade, financial assistance, and resource exploitation.<sup>6</sup>

The Darling report may be viewed as a thoughtful and far-sighted study that articulated well the conceptual, policy, and organizational difficulties that were challenging Canada's approach to international shipping at the time. It was also among the earliest to recognize that shipping policy and shipbuilding policy might also be divergent. Summarized briefly, the core messages of the report were: Canada should base its policy on core interests, not advantages; the international context was continuing to change and its implications for Canada could not be accurately predicted; and therefore Canada needed an improved policy and organizational structure to cope with the challenges those changes represented.

## **2.4 The Alcan Shipping Services Report (July 1977)**

This report, *Shipping Options for Canadian International Deep-Sea Trade (Alships Report)*, was prepared for Transport Canada's Research and Development Centre in July 1977. Its objective was the quantification and comparison of "direct benefits and costs which would accrue to the Canadian economy from the carriage of various selected commodities" through four shipping 'Options:' These options formed the cornerstone of the analysis that followed.

- Option 1: Foreign shipping services.
- Option 2: Canadian managed and operated foreign flag ships.
- Option 3: Canadian managed and operated Canadian flag ships with vessels being purchased from the cheapest sources of supply.
- Option 4: Canadian-built, -managed and -operated Canadian flag ships.

For each option, costs and revenues associated with various routes were assessed; the routes were intended as samples "representative of the diversity of Canadian trade." The study specifies that its point was not to present recommendations, but to quantify and compare.

The study unfolded in three phases. Phase 1 saw the compilation of a database of commodities and vessels involved in Canada's deep-sea trade, representing then-current

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<sup>6</sup> Darling, p. 62.



conditions in the field that were considered with projected trends to “select certain commodity/route/vessel combinations.”<sup>7</sup>

Phase 2 addressed the commercial analysis. Each of 23 selected routes was treated as a project; revenue flows, and capital, operating and voyage costs “for each of the four shipping options serving the same project” were calculated.

Phase 3 aggregated the results in terms of a hypothetical Canadian deep-sea fleet, and included a “review of commercial surpluses and shortfalls, vessel capital costs and manning requirements” of such a fleet. It also included an assessment of the “likely effect” of each option on Canada’s balance of payments.

Before its findings were reported in Section 9, the report offered certain disclaimers, including that trade routes were simplified and hypothetical, and that net present values of shipping options were not to be “interpreted as an independent measure of commercial viability but rather as a relative measure among the various scenarios under the same assumptions.”<sup>8</sup> After discussing three critical variables to which shipping options were especially sensitive (estimated market freight rates; vessel cost estimates; loan term assumptions), the report arrived at its comparison of the four options. Eleven broad conclusions were then drawn regarding the relative costs of each of the four options.

1. Transportation service costs are in all cases lower under Option 1 than under Options 3 and 4.
2. The rank of Options in order of increasing cost is: 2, 1, 4, 3.
3. A “non-significant difference” exists between the costs of Options 1 and 2.
4. A “non-significant difference” exists between the costs of Options 3 and 4.
5. Options 3 and 4 show lower costs because of the purchase of vessels from Japanese shipyards.
6. Costs in Options 3 and 4 could be wider apart if the terms of financing were to differ.
7. Reliable conclusions on groups of trade routes could not be drawn because of the “considerable differences” in route characteristics.
8. Seven routes are listed which, if provided with “limited financial assistance,” could offer commercial success.
9. A “more detailed investigation” is recommended to assess the “full commercial implications” of one option or route in relation to another.

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<sup>7</sup> Alcan Shipping Services Ltd. (1977), *Shipping Options for Canadian International Deep-Sea Trade*, Introduction (third page).

<sup>8</sup> Alcan (1977), 9.2

10. The trade routes indicated as the most promising “may not be commercially sound” were lower market freight rates to arise.
11. For the seven routes cited in Item 8 (above), financial assistance from 5-17% of “present transportation cost” would be required for services under Options 3 and 4 to compete with those under Option 1.

This was a technically complex study, involving a large number of variables. Because of data availability problems, the study was forced to make a large number of assumptions. As can be seen from the study that follows, the reliability of its findings, and hence its utility, was seriously open to question.

## **2.5 Shipping Advisory Board (September 1978)**

A further signal of enhanced government interest in deep-sea shipping policy was the establishment, by Cabinet in 1975, of an interdepartmental Shipping Advisory Board (SAB), which was tasked with coordinating current shipping policy activities and developing a framework for future shipping policies. In partial fulfilment of this role, the SAB completed in 1978 a review of the economic evaluation of Canadian deep-sea shipping options and in particular that undertaken by Alcan Shipping (the Alships Report). The resulting report was entitled *An Economic Analysis of Canadian Deep-Sea Shipping Options*.

This SAB report suggested that these studies had “not been comprehensive.”<sup>9</sup> Specifically, the SAB report criticized the “tenuous” methodologies of the Alships Report, and set out to “rework the commercial analysis.”<sup>10</sup> One of the more prominent results of this ‘reworking’ was the reversal of the Alships assertion that its Option 4 (Canadian operations with Canadian-built vessels) would be less costly than Option 3 (Canadian operations with foreign-built vessels). Following a lengthy and detailed exposition of its own methodology, the SAB report presented its central result: that any investment in Canadian flag options “would generate net economic costs.”<sup>11</sup>

The report offered the reasonable premise that “Canada’s international trade interests were best served by an efficient transportation system that provided an adequate supply of services at minimum cost.” In this respect, it generally supported the assumption made in the Alships economic analysis that Canadian shippers faced freight rates that were, and would continue to be, “predominantly determined by competitive forces in the

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<sup>9</sup> Department of Finance (1978), *An Economic Analysis of Canadian Deep-Sea Shipping Options* (Executive Summary), p. 1.

<sup>10</sup> Department of Finance (1978), p. iv

<sup>11</sup> Department of Finance (1978), p. viii

international market.”<sup>12</sup> Furthermore, it contended that employment, foreign exchange considerations, etc., did not justify steps to promote higher cost Canadian flag shipping. While making these observations the report also pointed out that there were those who argued in support of a domestic fleet, contending that Canadian flag shipping was necessary to protect Canada’s trade interests.<sup>13</sup>

The report then proceeded to examine this latter issue around the need for protection. This included analysis of the arguments that trends in deep-sea shipping encouraged “natural monopolies”; that foreign government intervention posed a threat to low-cost shipping; and that bilateralism, cargo reservation or UNCTAD would prove injurious to Canadian interests. The general conclusion of this examination was that such threats were overstated, and that there was every reason to believe that there would be “continued availability of shipping at competitive prices.”<sup>14</sup> The SAB report did acknowledge, though, that “foreign cargo preference policies” represented the most serious threat to Canadian trade.<sup>15</sup>

The two central conclusions of the report were, first, that Canadian flag services could not be operated profitably, and second, that even in the event that foreign cargo preference laws did result in potentially higher costs for Canadian shippers, introduction of Canadian flag shipping would not represent an “appropriate policy response” or an “improvement in the situation.”<sup>16</sup>

Finally, echoing the Darling Report, the SAB authors argued that “a careful distinction had to be made between participation of Canadian flag shipping in deep-sea trades and Canadian control of, and participation in, (foreign flag) deep-sea shipping.”<sup>17</sup> Further, the ability of large Canadian users of dry-bulk tonnage to effectively control their shipping requirements through contracts of affreightment or time-chartered tonnage suggested that these users were better served by the open market. Moreover, the report argued that Canada also had some large independent shipping companies that owned or chartered substantial volumes of tonnage registered under foreign flags. In both points, the message was clear: the SAB considered that Canadian trading interests had little to gain—and possibly much to lose—by the establishment of a Canadian-registered fleet.

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<sup>12</sup> Department of Finance (1978), p. x.

<sup>13</sup> Department of Finance (1978), p. x.

<sup>14</sup> Department of Finance (1978), p. xvii.

<sup>15</sup> Department of Finance (1978), p. xvii.

<sup>16</sup> Department of Finance (1978), p. xvii. The SAB Report did, however, recommend that Canada strongly oppose the UNCTAD code’s cargo sharing provisions.

<sup>17</sup> Department of Finance (1978), p. iii. Emphasis added.

## 2.6 Transport Canada Report TP 2347 (October 1979)

This 1979 report, *Background Paper on Deep-Sea Shipping*, undertaken by the Shipping Policy branch of Transport Canada, was intended as a discussion document to assist in the development of a more formal Canadian deep-sea shipping policy by early 1980. It explored parameters for the development of a deep-sea shipping policy in three main sections entitled *Factors, Trends and Developments in Deep-Sea Shipping*, and *Alternatives*.

The Factors section outlined the patterns and characteristics of Canadian trade. The longstanding Canadian reliance on foreign shipping and the question of Canadian government support for domestic shipping interests were explored, brief mention being made of the attempts in previous reports to “identify and assess developments impinging on international shipping, and their implications for Canadian shipping policy.”<sup>18</sup> Despite its focus on deep-sea shipping, the report also included some observations on domestic and transborder activity, including Arctic shipping.

Liner/tramp traffic was disaggregated, and loosely correlated with cargo types, import sources/export destinations, and value/volume differentiations. Some statistics on Canadian-registered deep-sea vessels (only 4) and Canadian-owned foreign registered vessels (estimated at 86) were provided.

The Trends section dealt primarily with the factors that led to the international oversupply of shipping capacity in the early/mid-1970s, and described two important trends occurring in the late 1970s: UNCTAD/bilateralism and government intervention in other states. The latter was cited as the “most fundamental” of recent developments, particularly in Less Developed Countries (LDCs).

In the third section, Alternatives, three strategic options for the Canadian government were suggested:

1. Minimum Involvement, i.e., “taking no action to encourage Canadian flag shipping; continuing to rely ... on foreign flag shipping; and encouraging as competitive a shipping market as possible.”
2. Full Involvement, i.e., “trying to build ... a merchant marine big enough to carry ... Canada’s offshore trade; providing a full range of measures to Canadian operators; supporting financial and fiscal incentives with cargo reservation policies...; and developing a high level of government participation in the industry in support of an aggressive fleet expansion policy.”

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<sup>18</sup> Transport Canada (1979), *Background Paper on Deep-Sea Shipping*, p. 1.

3. Mid Course, i.e., “encouraging the gradual development of a Canadian flag fleet ... by offering Canadian operators incentives comparable to those available” in other countries; “providing direct support in areas of particular national interest ... or where (there were) discriminatory measures on the part of other governments ...;” and encouraging a competitive shipping market.<sup>19</sup>

After laying out a series of program alternatives pertaining to industry support, Arctic shipping, and financial alternatives, the report moved to its conclusion, which was generally congruent with the Mid-Course strategy outlined above. Revisiting the interplay between Factors and Trends, the report was careful to say that the extent to which Canadian trading and shipping interests were directly affected by (such) developments was impossible to assess with any degree of precision. It concluded that the significant changes in international shipping implied that Canada could no longer continue to rely automatically on market forces to ensure the availability of low-cost shipping.<sup>20</sup>

## **2.7 Transport Canada Report TP 1676 (1980)**

TP 1676, *A Shipping Policy for Canada*, was perhaps the closest that Canada came, in this intensive period of policy review, to laying out a formal deep-sea shipping policy. Its declared purpose was “to set out the main elements of a deep-sea shipping policy for Canada, taking into account recent and anticipated developments in this country and abroad.” Like other documents, it acknowledged Canada’s reliance upon, and benefit from, foreign flag shipping, and the “fundamental changes” that were occurring at the time, and aspired to provide a “comprehensive review” of Canadian shipping policy.<sup>21</sup>

The document first outlined Canada’s shipping interests and global trends. This description was then followed by a discussion of the legislative and institutional framework for Canadian shipping. This section offered commentary on the state of Canadian regulation, for example suggesting that Canada did not “possess extensive legislative or regulatory mechanisms capable of dealing with the kinds of policy issues” that were emerging.<sup>22</sup> The 1974 Darling Report’s critical appraisal of Canada’s “fragmented and contradictory” shipping policy was quoted extensively. The following section on Canadian flag deep-sea shipping revisited the four options of the Alships report, repeating the findings of that paper, namely that the two Canadian flag options (Options 3 and 4) would represent an inefficient use of Canadian resources.

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<sup>19</sup> Transport Canada (1979), pp. 27-28.

<sup>20</sup> Transport Canada (1979), pp. 39-40.

<sup>21</sup> Transport Canada (1980), *A Shipping Policy for Canada*, p. 1.

<sup>22</sup> Transport Canada (1980), pp. 35-36.

The report's conclusions recapped the global trends—foreign government involvement in shipping, reduced competition, changing economics in world shipping—before revisiting possible Canadian 'options.' It argued that it was highly doubtful that Canada could continue to rely on the competitive forces of the international shipping market to supply all the services Canada needed at the lowest possible cost.<sup>23</sup> Preference was expressed for Options 1 and 2 (reliance on foreign-flag shipping and on Canadian-managed foreign flag ships) as opposed to the development of a Canadian flag fleet.

In policy terms, the report offered the following conclusions:

- the “primary objective of Canadian deep-sea shipping policy should be to ensure the continuing availability of adequate and economic shipping services...;”
- “the provision of new tax or financial measures to support the development of a Canadian flag deep-sea fleet” was unwarranted;<sup>24</sup>
- a number of “related measures” should be adopted, given Canada’s intention to continue to rely on the open market; this implied a “more direct and active Government interest in deep-sea shipping” and envisaged “measures to ensure that competitive market conditions (were) not unduly constrained” and that national interests were “promoted and protected;”<sup>25</sup>
- new legislation should be developed to give the government “broad powers” to act where Canadian shipping interests were threatened by the actions of a foreign government or carrier.

Perhaps the key observation here is that the conclusions of this policy document did not examine the merits of Option 2 in relation to Option 1. More particularly, there was no examination of the value and importance of nurturing within Canada an involvement in international deep-sea shipping through the control and ownership of foreign flag ships.

Moreover, the absence of any substantive reference to shipbuilding issues in this deep-sea policy was instructive; as originally stressed by Darling (see 2.3) shipbuilding policy was clearly not seen as part of any policy objective in relation to international shipping, although support for shipbuilding, as part of Canada’s domestic shipping policy through the 25% import duty provision on all foreign built ships imported for use in the Canadian Coasting Trade, was not addressed by the report. The rationale behind this clear policy division between international and domestic shipping will be addressed later in Chapter 5.

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<sup>23</sup> Transport Canada (1980), p. 50

<sup>24</sup> Transport Canada (1980). This conclusion was accompanied by a commitment to review this decision “in the light of changing circumstances” (p. 51).

<sup>25</sup> Transport Canada (1980), p. 51.

Most importantly, this policy document signalled to the nation that the government viewed the public interest as more focused on trade-liberalization and growth than on the maintenance of a shipping industry. The focus for the next few years shifted to examining the merits of adoption of a ‘Defensive Deep-Sea Shipping Policy.’

## **2.8 Transport Canada Report TP 4918E (October 1983)**

*Examination of the Defensive Deep-Sea Shipping Strategy*, prepared as a Working Paper by the Shipping Policy Branch of Transport Canada, constituted the culmination of the government’s efforts to examine how it might implement the 1980 policy pronouncements regarding a defensive deep-sea shipping policy. Its declared intent was to “review the incidence and implications ... of foreign government intervention in ocean shipping”, with the proviso that it was not intended to ‘make judgement’ on the need for new measures. Instead, it timidly pronounced that it was meant to “provide background information on diverse aspects of the issue and to elicit comments and views from all interested parties.”<sup>26</sup>

By way of definition, the report suggested that the primary objective of a defensive strategy was to ensure efficient, low-cost service to Canadian shippers.<sup>27</sup> The strategy’s intention would be:

1. To “defend various Canadian interests from adverse consequences arising from certain actions of some foreign governments ...”
2. To “deter and/or respond to actions taken by foreign governments to restrict shipping and related services, or to promote unfairly their national maritime interests.”<sup>28</sup>

The report was careful to point out that a defensive shipping strategy “would not be promotional,” i.e., it was not “intended to expand Canada’s fleet or to extend Canadian shippers’ control of deep-sea movements beyond what would be obtained by normal competition.”<sup>29</sup>

After a brief exposition of the conditions that might lead to the implementation of such measures, the paper discussed the rationale for and against such a strategy. Examples of foreign interventions were provided, but counter-arguments were also offered. For example, the question was raised as to whether or not foreign intervention had even affected Canadian trade, and it was pointed out that the number of complaints received by

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<sup>26</sup> Transport Canada (1983), *Examination of a Defensive Deep-Sea Shipping Strategy*. Foreword.

<sup>27</sup> Transport Canada (1983), p. 1.

<sup>28</sup> Transport Canada (1983), p. 3.

<sup>29</sup> Transport Canada (1983), p. 3.

the government from domestic shipping interests had been small.<sup>30</sup> The “extremely” diverse view within the Canadian shipping industry was also discussed, with some shippers eschewing the idea of a defensive strategy, and others supporting bilateralism. There were also those who argued that the government should consider the designation of “suitable” foreign flag carriers as Canadian carriers.<sup>31</sup>

The report cited defensive measures taken in other OECD states but, once again, in an observation reminiscent of the 1974 Darling Report, pointed out that the policy for Canadian reaction to foreign intervention in shipping had not been clearly articulated and that a systematic strategy had not been developed for the implementation of a response to the actions of other governments.<sup>32</sup>

After a lengthy exploration of ‘alternative responses’ to foreign interventions—i.e., retaining the status quo, supporting commercial solutions, bilateral negotiation, multi-lateral initiatives—the report delineated a defensive strategy along lines of ‘non-retaliatory/remedial powers and overtly retaliatory powers,’ which were described at length.

The report came to the conclusion that there were two “basic arguments” that made the consideration of defensive legislation “inappropriate” at the time:

1. The “small proportion” of Canadian trade adversely affected by other states’ distortionary practices, and the sense that Canada’s “vital interests” did not seem to be in peril.
2. The possibility that, had actual problems arisen, they could have been “adequately resolved through a more aggressive use of existing powers and bilateral representations to our trading partners.”<sup>33</sup>

Finally, the report recognized that, though the impact of foreign interventions appeared to be limited at the time, there was no guarantee that this would remain the case. This led him to indicate that further examination of the need for a “more responsive, defensive shipping strategy *as a contingency measure*” might be warranted.<sup>34</sup>

## **2.9 Transport Canada Report TP 6347E (April 1985)**

Of all the studies reviewed in this chapter, this report is almost certainly the most important. Not only did it represent the culmination of almost 15 years of intensive

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<sup>30</sup> Transport Canada (1983), p. 10.

<sup>31</sup> Transport Canada (1983), p. 15.

<sup>32</sup> Transport Canada (1983), p. 19.

<sup>33</sup> Transport Canada (1983), p. 35.

<sup>34</sup> Transport Canada (1983), p. 36 (emphasis added).



evolution of policy thinking, but also it is the last substantive examination of policy undertaken by the government in this field. Established in April of 1984, the Task Force on Deep-Sea Shipping was mandated to “evaluate changing conditions in the international shipping market and the possible need for measures to encourage the expansion of the Canadian deep-sea fleet.”<sup>35</sup> Its membership featured representation from shipping interests, government officials, union leaders and academics.

Like previous reports, *The Task Force on Deep-Sea Shipping, Report to the Minister of Transport*, explored the history of Canadian shipping and the current Canadian interest and involvement in this sector, before moving on to an assessment of the ‘changing’ international shipping environment. This exploration included:

- the changes occurring in the nature and scale of demand for international shipping;
- the rise of new economic centres such as Taiwan and South Korea;
- a trend toward specialization in ship design and increased productivity in ocean transportation;
- the continuing growth of ‘flag of convenience’ registries;
- the development of highly subsidized and protected Soviet, satellite and LDC fleets;
- the oft-cited trend toward foreign government intervention.

Analyzing the effect of these changes on Canada, the report first argued that interventions by other states “do not appear to represent a major problem in Canadian trades” and, second, that “the overall trend in ocean shipping has decidedly been towards more, not less, competition.”<sup>36</sup> It is also noteworthy that this report devoted considerable attention to taxation regimes in OECD countries, perhaps representing a shift in Canadian thinking from promoting a merchant marine to alternative methods of protecting Canadian interests.

The report reiterated the importance of Canadian access to competitive shipping markets, and in the chapter entitled *Policy Options Facing Canada*, it argued that the national policy needed to be based “unequivocally on commercial principles as opposed to some broader, undefined national interest.”<sup>37</sup> It was forceful in its explanation of this position, citing the clear “inability of the high income nations to compete without subsidy” and arguing that trends toward crew hiring from LDCs could not “be expected to be reversed in this century.” Lastly, it suggested that for Canada to consider measures to enter

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<sup>35</sup> Transport Canada (1985), *Task Force on Deep-Sea Shipping: Report to the Minister of Transport*, p. iii.

<sup>36</sup> Transport Canada (1985), pp. 25, 29.

<sup>37</sup> Transport Canada (1985), p. 31.

national flag deep-sea shipping, at a time when maritime OECD countries were having great difficulty keeping their fleets from disappearing, did not make economic sense.<sup>38</sup>

The main recommendations of the report relating to Canada's policy posture in relation to deep-sea shipping may be summarized as follows:

- that the federal government not establish a core deep-sea Canadian flag fleet;
- that Canada “encourage and strengthen its expertise and interests in international shipping;”
- that the government create a fiscal environment “conducive to the establishment and maintenance of international ship management activities in Canada”;
- that an advisory board be created to monitor the international shipping environment and that it be provided with “mechanisms enabling it to react” to external influences; and
- that three issues peripheral to the main deep-sea policy debate, be further examined: the availability of Canadian owned vessels in an emergency situation; the promotion of Canadian interests in the field of Arctic shipping; and the review of the impact of economic and technical rules and regulations on the ability of Canadian flag shipowners to compete in international shipping markets.

In the end, the report stands out from its predecessors in its clear differentiation between the relative merits of what, in past studies, have been identified as Options 1 and 2. On the one hand, it offered strong condemnation of a policy of encouraging, by direct operating subsidies, a Canadian flag deep-sea fleet, while, on the other, it provided strong support for Canadian involvement in the management of foreign flag shipping, as the means by which Canada could encourage and strengthen its expertise and interests in international shipping. In the latter case, it recommended important fiscal adjustments that included an endorsement of the creation of ‘International Shipping Corporations’ (ISCs) as the mechanism for achieving these fiscal objectives.

As the implementation of the second and third recommendations of the Task Force form the basis of subsequent analysis in this study, it is worthwhile repeating them in their original language:

**Recommendation 2:** It is recommended that Canada, as a major importing and exporting nation with significant reliance on ocean transportation, encourage and strengthen its expertise and interests in international shipping.

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<sup>38</sup> Transport Canada (1985), p. 41.

**Recommendation 3:** It is recommended that the government create a fiscal environment conducive to the establishment and maintenance of international ship management activities in Canada.

Recognizing that the economic situation in Canada was heavily dependent upon exports, the Task Force believed that it was vital that Canada have a strong base of shipping expertise in order to ensure continued smooth flow of exports. The focus of such expertise would be one of being astute buyers of maritime transportation services, astuteness derived from industry knowledge. Such industry knowledge would also be garnered through the creation of a financial environment that was more attractive to shipping companies. This involved legislation that allowed for the creation of International Shipping Corporations (ISCs). The report recommended that an ISC would be majority owned by Canadian residents, and would be managed in Canada. The ISC would be permitted to own ships that were registered under any flag. As well, if the ISC earned at least 90% of its income from international shipping, it would not be taxed in Canada on its income. It was believed that this would act as a clear signal that successful shipping companies could operate from within Canada.

The manner in which Recommendation 3 was addressed and implemented by the federal government is the focus of Chapter 3.

## **2.10 Summary: Emerging Themes in the Evolution of Canadian Deep-Sea Shipping Policy**

In reviewing the evolution of thinking over the period 1970-1985, certain broad themes emerge.

- Despite a clear and often repeated desire expressed by certain interests in both the public and private sectors to develop a persuasive rationale for encouraging the development of a Canadian flag fleet, no supporting rationale emerged over the period. This was principally because the costs of achieving this objective, mainly in the form of subsidies in one form or another, were seen to outweigh what were considered comparatively modest benefits in the form of balance of payments contributions, employment creation, stimulus to employment in auxiliary services, and strategic defence considerations. However, not addressed among the benefits was the value to be gained by having a nucleus of knowledgeable and experienced sea-going personnel, available to come ashore to fill shore-based positions in commercial shipping operations. This issue will be discussed more fully in Chapters 3 and 5.
- An obvious option to any stimulus to support expanded participation by Canadian-registered ships in international deep-sea trade was to rely on policies and powers designed to ensure the continuance of free and fair competition. A feature of the

period was a number of unilateral, bilateral and multilateral initiatives by various states that would have had a negative impact on the maintenance of a competitive environment. In this respect, the option anticipated careful monitoring of trade practices on Canada's import and export routes, and the introduction of powers to act where restrictions to competition arose. So there emerged a focus on defensive shipping policy options in the early 1980s. It is probably fair to say that international developments since that time (for example, the end of the Soviet Union and the effective abandonment of the United Nations Code of Conduct for Liner Conferences 1982) have tended to reduce, rather than to increase, any threat to competition.

- Another policy dimension that was largely ignored over the period, but came to the fore finally in the Task Force report where it received specific attention and recommended action, was the need for Canada to maintain expert and practical knowledge and experience in the wide range of commercial activities relating to ocean shipping, of which shipowning was but one element. For this to happen, initiatives needed to be taken to encourage development of the necessary commercial environment. If this could not be achieved through the operation of Canadian flag ships, then it needed to be accomplished through encouraging the establishment in Canada of the effective ownership, management and control of foreign flag ships. It was to this end that the Task Force report recommended certain fiscal adjustments and the formation of a joint industry, government and labour Advisory Board. Again these recommendations will be discussed further in Chapters 3 and 5.

## **Acknowledgement**

The assistance of Iain Grant, Dalhousie MMM '03 candidate, in undertaking the background research for this chapter is much appreciated.

# **CHAPTER 3 – CANADA’S INTERNATIONAL MARITIME CENTRE EXPERIENCE**

## **3.1 Introduction**

This chapter begins by examining Canadian fiscal policy in the period before the Task Force on Deep-Sea Shipping reported. This is done in order to set the scene for a full understanding of the efforts that followed its recommendation to set a fiscal climate conducive for owners of deep-sea vessels to create employment in shore-based maritime services industries in Canada. The chapter then goes on to explore the International Maritime Centres initiative, using the Vancouver and Halifax experiences as illustrative of what followed in Canada, but with some documentation of early efforts elsewhere. In order to evaluate the experience with International Shipping Corporations (ISCs), the authors present what is known about ISCs today and draw some conclusions about the implementation of the Task Force recommendations. This will lead into Chapter 4, where European shipping policy and the tonnage tax concept will be explored. It should be noted that the focus of Chapter 3 is entirely on international shipping and it only addresses peripherally any of the fiscal requirements of a Canadian flag fleet or of Canadian providers of domestic shipping operations.

## **3.2 Fiscal Policy Prior to 1985**

As discussed in Chapter 2, prior to the Task Force on Deep-Sea Shipping there were still many in Canada who were interested in the possible development of a deep-sea fleet under Canadian flag. While many studies concluded that conditions were not right for this shipping policy option or that the benefits of the policy option were not sufficient, there were still a few individuals who were convinced that it was merely a matter of offering the right fiscal incentives. It was that belief that led to the Brooks and Marlow study of fiscal incentives.

Unlike other maritime centres, Canada does not grant any exemptions to personal or corporate taxes payable for specific businesses or industries. The United Kingdom (UK) has had a long-standing policy, for example, of supporting non-national owners as a means of encouraging the maritime services industry, among others. A ship owner, domiciled abroad but resident in the UK, may be liable for UK taxes on his earnings and

investments remitted to the UK, but is not liable for taxation on earnings made by companies registered and resident overseas, which are not remitted to the UK. This provision has been crucial in attracting Greek owners, among others, to London. Unlike the UK government, the Canadian government has applied a “mind and management” test that has discouraged this type of arrangement, taxing Canadian corporations on their worldwide income. For an industry where most companies pay little or no tax, this was a barrier to establishing a shipping business in Canada.

In 1983, Canadian fiscal policy (as it applied to shipping) was examined for the federal government in an unpublished report by Brooks and Marlow.<sup>39</sup> Based on the methodology used in fiscal studies for the UK government and reported by Gardner and Marlow,<sup>40</sup> the study evaluated the existing Canadian fiscal climate against that provided in West Germany, Japan, the United Kingdom and the United States. It also examined four variants to the existing Canadian fiscal regime, each offering the hypothetical ship owner a federal government–determined combination of capital cost allowances and vessel purchase incentives superimposed on the existing regime. All combinations were analyzed using two different inflation assumptions and two different rates of return, for three tax positions (full tax, no tax (e.g. sufficient offsetting tax losses), and new entrant). The paper concluded that, if the government wanted to improve the fiscal climate to encourage registration of deep-sea shipping in Canada, it would need to improve the fiscal regime for foreign-built ships and the standardization of safety requirements to international standards so that the capital costs of safety investments were not higher for Canadian owners than for foreign owners. In hindsight, it would have been useful to do the same type of investigation to evaluate the International Shipping Corporation model proposed by the Task Force some 16 months later.

### **3.3 The Deep-Sea Task Force Recommendations on Fiscal Treatment of Shipping**

One of the Task Force recommendations (Recommendation 3), as quoted earlier in Section 2.9, focused on the issue of the fiscal climate for international shipping management in Canada. It was recommended that Canadian tax law be modified in order to create a financial environment that was more attractive to shipping companies, through the implementation of legislation that allowed for the creation of International Shipping Corporations. It was recommended that an ISC would be majority owned by Canadian residents, and would be managed in Canada. The ISC would be permitted to own ships

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<sup>39</sup> Brooks, Mary R. & Peter Marlow (1983), *Canadian Tax Policy and the Shipping Industry: An Evaluation*, unpublished.

<sup>40</sup> Gardner, Bernard & Peter Marlow (1983), *An International Comparison of the Fiscal Treatment of Shipping*, *Journal of Industrial Economics*, 31, 4, 397-415.

registered under any flag. As well, if the ISC earned at least 90% of its income from international shipping, it would not be taxed in Canada on its income. It was believed that this would act as a clear signal that successful shipping companies could operate from within Canada.

The Department of Finance response to the Deep-Sea Task Force was relatively swift in coming to public discussion. To grant an exemption from Canadian income tax for a business enterprise resident in Canada would set a precedent unlikely to be acceptable to the Department. Furthermore, the Department was engaged in discussions on corporate tax restructuring and corporate tax reform, and there was concern about the use of ISCs to avoid taxes. From a tax perspective, the ISC issue was part of a larger debate and it was some time before resolution would be forthcoming.

At the same time, within Transport Canada, there were efforts to establish a Canadian position on the *United Nations Convention on Conditions for the Registration of Ships, 1986*. Until the details of the convention were finalized, it was unlikely that any policy decisions on the treatment of Canadian flag vessels would be made.

Clarkson Gordon undertook an assessment of the ISC model in the context of competing tax regimes and in particular that of the US.<sup>41</sup> The resulting Memorandum from Clarkson Gordon recommended that incorporation in Canada not be required and that the ISC only needed to have a majority of Canadian resident directors. To qualify as an ISC, the recommendation was that 75% of salaries must be paid to Canadian residents.

In September 1988, Transport Canada examined the continuing development in Europe and elsewhere of alternative fiscal arrangements for the shipping industry in a small study by Ruth Abbott of Economic Research. Entitled *Second Vessel Registries: Options Selected by European Nations*,<sup>42</sup> the report provides a brief description of the measures already adopted in Europe, a comparison of international registers and the success factors in attracting tonnage to the new “second registers” established. It did not evaluate the suitability of the second register approach for Canada, although this was also being discussed at the time.

Thus progress on implementation of Recommendation 3 of the Task Force was slow in Ottawa. However, on the west coast of Canada, the industry was gearing up to promote change, and the instrument for that change was the Asia-Pacific Initiative.

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<sup>41</sup> Jonathan Seymour & Associates (1988), *Vancouver: An International Centre for Maritime Commerce Final Report*, Vancouver: Asia Pacific Initiative Transportation Task Force, December 22, Appendix II.

<sup>42</sup> Abbott, Ruth (1988), *Second Vessel Registries: Options Selected by European Nations* (TP 9418E), Ottawa: Transport Canada Economic Research.

### 3.4 The Asia-Pacific Initiative<sup>43</sup>

The Asia-Pacific Initiative (API) was a joint federal-provincial task force with federal funds coming from Western Economic Diversification. It was funded for a three-year period, 1987-1990, to enhance British Columbia and Vancouver as Canada's Pacific centre for trade, commerce and travel. A number of private sector volunteers served through task forces in areas such as international finance, culture and transport.

In 1988, the Transportation Task Force of the API undertook a study that focused on the development of Vancouver as an International Centre for Maritime Commerce. The primary objective of this study was to "create an internationally competitive business environment suitable for the ownership, management and control of ships engaged in international trade; one which will permit Vancouver to achieve its natural potential as a major international centre for maritime commerce."<sup>44</sup>

The study concluded that the primary constraint on Vancouver becoming an international shipping centre was the tax structure applicable to the industry in Canada. Taxation in Canada was much more onerous than in other maritime nations. If the management of international shipping activity resided in Canada, that company's worldwide income would be subject to Canadian taxes, irrespective of source.

The primary recommendation of this study was that the Canadian tax rules with regard to shipping should be changed.

*Vancouver already has the essential attributes to become a centre for management of international maritime operations. To make this happen will require modification of Canadian tax policy to permit the "mind and management" of international shipping ventures to be located anywhere in Canada on a tax-exempt basis.*<sup>45</sup>

Changing the tax laws in this manner, it was argued, would create a major opportunity for development. It was recommended that the tax act be changed in line with the recommendations of the Task Force on Deep-sea Shipping, and the new legislation should incorporate features to attract foreign ship owners and operators. It was argued that ship owning, management and the operation of chartered ships should all fall within the tax exemption. It was also noted that the revenue lost from the tax exemptions would

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<sup>43</sup> This section is based on materials distributed by the Vancouver IMC at the time it was active and personal interviews (May and June 2003) with Jonathan Seymour, who served as Executive Director of the Vancouver IMC from 1993-1998.

<sup>44</sup> Jonathan Seymour & Associates (1988), *Vancouver: An International Centre for Maritime Commerce Final Report*.

<sup>45</sup> Jonathan Seymour & Associates (1988), *Vancouver: An International Centre for Maritime Commerce Final Report*, p. 2.



be small, given the amount of international ship ownership in Canada at that time. As well, it was suggested, the losses would be offset by increases in tax revenue from personal income (arising from the new jobs created) and from the corporate taxes paid by non-ISC businesses in maritime-related activities that would result from the increased economic activity.

In order to facilitate the creation of Vancouver as a major shipping centre, it was also recommended that a Shipping Centre Development Office be created for the 18-24 months immediately following the taxation changes. This office would be responsible for tasks including:

- the production of informative and detailed descriptive material for distribution to the shipping industry, trade commissions, etc.
- maintaining liaison with target groups and candidates
- providing a focal point for enquiries and information flow
- initiating and directing contact between candidates, advisors and the authorities, as appropriate
- in association with Canadian and provincial private and public bodies, initiating and developing international conferences on shipping related matters to be staged in Vancouver.

The purpose of this office would be to establish Vancouver as a shipping centre and, once this had been achieved, the need for the office would diminish, and it was expected that the office would eventually be eliminated.<sup>46</sup>

The funding for the Asia-Pacific Initiative IMC study was provided by the Province of British Columbia. The Province adopted the study and seconded Glen Scobie as additional support for the initiative. Mr. Scobie served as Executive Director of the newly-formed Society for International Maritime Centres (a provincially incorporated not-for-profit corporation with a national board, including one of the authors of this report representing Halifax interests). The purpose of the Society was to gain national support for implementing changes to the legislation. International Maritime Centre Vancouver was a provincial entity, with a provincial board, and was established to promote Vancouver as the destination of choice once legislative changes had been made.

Amendments to the Canada *Income Tax Act (Bill C-18)* received royal assent on December 17, 1991. These amendments meant that a company incorporated in another country, but located in Canada, where all or substantially all of its activities are primarily involved with the movement of international traffic and whose revenues are derived

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<sup>46</sup> Jonathan Seymour & Associates (1988), *Vancouver: An International Centre for Maritime Commerce Final Report*.

totally or at least substantially from the operation of ships in transporting international traffic was considered, for tax purposes, not to be a resident of Canada, but rather to be a resident of its country of incorporation. (This was a rather elegant solution to the problem the Department of Finance faced with respect to establishing a precedent.) This provision did not preclude, however, the possibility that a corporation may also be a resident in a country other than Canada or the country of its incorporation. The changes to the Act, along with subsequent revisions and interpretations, are detailed in Appendix 3.1.

In addition to the amendments to the *Income Tax Act*, Canada enacted minor changes to several other statutory instruments to achieve legislative consistency. These involved the *Coasting Trade Act*, the *Customs Act* and regulations pursuant to the *Customs Tariff*. The result was to make a clear distinction between shipping activities undertaken within Canada and those undertaken internationally, and their respective treatment in Canada for tax, duty and cabotage purposes.<sup>47</sup>

After the passing of the legislation, Vancouver ramped up its marketing efforts. The Province of British Columbia financed a seminar in Hong Kong to extol the virtues of relocating to Vancouver (at a cost of about C\$50,000). In 1993, the Province financed C\$100,000 to support the International Maritime Centre Vancouver office and the newly created office secured a coordinated immigration agreement between the Province of BC and the federal government to establish guidelines to smooth immigration acceptance of key company personnel. This immigration agreement was considered as a critical building block in the success of the Vancouver IMC.

Jonathan Seymour, a maritime consultant, was appointed Executive Director of the Vancouver IMC and the office moved to the Vancouver World Trade Centre when C\$150,000 in additional funding came in 1994. Then Federal Government and Western Economic Diversification provided more support in the amount of C\$150,000 a year for the next three years. According to Jonathan Seymour, about C\$1.4 million was spent over the lifetime of the marketing campaign.

By 1994, the IMC Vancouver argued, in a report to the Department of Foreign Affairs and International Trade:

*Confidentiality prevents full disclosure. Shipping groups that can be named include Teekay Shipping, a Bahamian/Danish/U.S. group which moved the control of its fleet of 60 tankers from California to Vancouver; South Pacific Interline (Swedish); MacMillan Bloedel's shipping arm—Canadian Transport Co; Golden Ocean of Taiwan/U.K.; plus Kent Line, Expedo, Oak*

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<sup>47</sup> Jonathan Seymour & Associates (undated), *Canadian Taxation of International Shipping Corporations*, handout of the International Maritime Centre – Vancouver.

*Steamship and Fairmont. In addition, several Hong Kong companies will relocate additional functions to Vancouver as 1997 approaches.*<sup>48</sup>

The Department of Finance proposed an amendment in 1995 (section 115 (1) (b) (ii)) that was designed to ensure that ships used by international shipping companies that qualified as non-residents were not classified as taxable Canadian property. Thus, capital gains on the sale of those ships would not be taxable within Canada. This amendment was passed in 1998 and applied retroactively from April 26, 1995.<sup>49</sup>

By March 1996, the economic benefits of the Vancouver initiative were published by the Vancouver IMC (the direct quote is in the box on the next page). Today, Statistics Canada notes that these numbers were supplied by the IMC and not verifiable. This does not necessarily mean that the benefits are not real, as will be discussed later in Section 3.6.

In 1998, Section 250(6) was modified to recognize the frequent use of holding companies and single-purpose/single-ship corporations by international shipping companies. Following these changes, where an international company controlled ships through a wholly-owned corporation which itself would qualify as a non-resident, it may be treated as if it were operating the ships themselves in order to establish non-residency for tax purposes. The relationship between the sections of the *Income Tax Act* (and therefore the determination of who qualifies as an ISC) is best explained by Appendix 3.2.

There were also changes advocated by the IMC Vancouver to the customs tariff. ISCs were able to purchase vessels offshore and, as long as they remained in the deep-sea trades, they would not be required to pay the customs duty applicable to vessels in Canadian coasting trades.

In 1998, the IMC Vancouver office was wound down because remaining inquiries were low quality (of questionable value) and somewhat suspicious. By then, the lawyers, accountants and others interested in attracting more companies were seen as quite capable of selling the Vancouver location without government support. To quote Jonathan Seymour (during the course of this research): “The IMC initiative has its own legs. No more promotion is necessary. The concept is still alive, and surviving without government support. The original plan was to grow the Canadian maritime services sector not the Canadian fleet.”

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<sup>48</sup> International Maritime Centre – Vancouver (1994), *International Shipping Corporations Opportunities and Obstacles*, prepared for the Department of Foreign Affairs and International Trade, March 31, p. ii.

<sup>49</sup> Jonathan Seymour & Associates (undated), *Canadian Taxation of International Shipping Corporations*.

## **Economic Benefits of IMC Vancouver**

IMC – Vancouver estimates that the Canada-wide impact as at end-Summer 1996 will be as follows:

- 21 companies controlling
- around 200 ships (or in excess of 300—depending on definition)
- 325-350 direct employees in Canada
- including about 85 new immigrants
- with a payroll of about \$17 million annually
- disbursing about \$30 million in direct business expenses in Canada
- yielding about \$5 million per year of direct federal and provincial taxes (\$1.5+ million for BC)
- new personal wealth brought into Canada as a result of the initiative is estimated to exceed \$1 billion

Between 85 and 90% of this impact accrues in British Columbia.

Note: These estimates were discussed with StatsCan. Based on the results of its 1996 maritime services survey, it was StatsCan's view that these IMC figures are conservative.

*Source: Vancouver IMC undated flyer.*

### **3.5 The Halifax International Maritime Centre<sup>50</sup>**

The Halifax International Maritime Centre initiative had neither the financing nor the head-start of the Vancouver group. In Halifax, an ad hoc group was formed to exploit the opportunity but relied on volunteers, goodwill and student support. The group was chaired by Don Connor of the Halifax World Trade Centre and consisted of representatives of the NS Department of Economic Development, Atlantic Canada Opportunities Agency, the Halifax Port Corporation, the Halifax-Dartmouth Port Development Commission, Dalhousie University, MT&T, the Royal Bank and Deloitte and Touche. Seed funding for student research was provided by the NS Department of Economic Development. Student researchers were used to determine the countries with the largest potential to be attracted to the Halifax IMC, or one of its competitors. (By December 1993, Montreal, Saint John and Toronto all had plans to establish local

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<sup>50</sup> This section is based on two student reports written for Dr. Mary R. Brooks by Brenda MacNeil (December 1993) and Claudia Luddemann (April 1994) plus personal interviews (May and June 2003) with Wade Elliott, who was Policy Analyst with the Halifax-Dartmouth Port Development Commission at the time, and Gillian Wood, who was working with the Priorities and Planning Directorate of the Province of Nova Scotia in 1994.

capacity to attract shipping companies but only Vancouver had actually established the necessary infrastructure to support the marketing effort needed. A profile of efforts to December 1993 by these three other IMCs is detailed in Appendix 3.3.)

In her 1993 report to the Halifax IMC group, Brenda MacNeil identified 14 countries in five geographic regions for further investigation and, if appropriate, targeted marketing activities.<sup>51</sup> Of these, Hong Kong was not viewed as a strong possibility, given the head-start made by Vancouver in approaching them. Investigation resulted in several others being rated as poor targets, while the US Eastern seaboard companies and those from Sweden rated as moderate, and those from Germany and the Netherlands as strong possibilities. A marketing program was designed, and a budget of \$243,800 developed in a report by student Claudia Luddemann. Subsequently, a *Fairplay* database was purchased, a brochure on the Halifax IMC designed and advertising commenced, fronted by the Halifax-Dartmouth Port Development Commission. However, the new provincial Liberal government under the leadership of Dr. John Savage faced a significant fiscal deficit and matching dollars were not there for any ACOA assistance. Efforts moved forward, using mostly in-kind support.

It was about this time that the Europeans began to explore the concept of a tonnage tax, but a few markets still showed promise and interest, Germany in particular. Materials were distributed to a number of companies in Germany. Quite a few calls were fielded from immigration lawyers and three German companies showed some interest. Wade Elliott, Executive Director of the Halifax-Dartmouth Port Development Commission, met with the three on a trip to Germany, and there were follow-up discussions. There were signals that the German government was planning to improve the fiscal situation. Eventually, the window of opportunity closed. The total cash investment in Halifax was estimated by Wade Elliott at less than C\$10,000.

To quote Wade Elliott (during the course of this research):

*The window was closing ... at least for Halifax as more European countries introduced tonnage tax programs and other reforms. There was an affinity [Germans were investing along the South Shore] and there was an outreach from Nova Scotia to Germany. The Canadian tax issue was enough to get an audience, but the lack of critical mass of other marine services, like maritime arbitration, and limited air access made for a tougher sell.*

To conclude, this was a time of fiscal restraint in Nova Scotia and there were insufficient financial resources to move it to the top of the government's priority list. Economic

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<sup>51</sup> MacNeil, Brenda (1993), *Halifax International Maritime Centre Market Research Report: Final Report*, unpublished report, December.

Development initiatives were focused predominantly on attracting call centres, and the promise of the concept was a difficult one to understand and to sell locally. Without a well-financed sales campaign, it proved difficult to convince shipping companies to relocate, particularly if they thought their national government would improve the local fiscal climate.

### **3.6 Beyond the ISC to a Canadian Flagged Deep-Sea Fleet?**

In two studies of conditions necessary for competitive, national flag fleet development, Brooks<sup>52</sup> concluded that three conditions are paramount for any country to encourage this outcome: access to cargo, appropriate fiscal climate, and access to inputs (labour and capital) at global market prices. By the time these studies were released, the Task Force on Deep-Sea Shipping had reported and positioned the Canadian public interest as being firmly in the camp of seeking to ensure adequate service for trading interests rather than one of establishing a core deep-sea fleet. Most important, it recommended the creation of an advisory board to monitor international changes to the industry, and the concept of an International Shipping Corporation as a possible approach to the fiscal change needed to attract the shore-based maritime service component of the deep-sea industry.

While this was not the purpose of the *Income Tax Act* changes and subsequent modifications to other legislation discussed above, by the late 1990s there were those who still wanted the legislation to go further and support a Canadian flagged deep-sea fleet. It must be remembered, however, that the economic benefits of a Canadian flag deep-sea option have not been proven. This raises the question: what would it take to encourage deep-sea flagging in Canada, either as an extension of the ISC model or another approach arising from discussions in Chapter 4? This section presents the “what more” for the ISC model.

In June 1998, Section 17(b) of the *Canada Shipping Act* was altered to remove the pro-Commonwealth discrimination that had been a feature of Canadian flag shipping since the days when Canadian shipping was governed by the British *Merchant Shipping Act of 1854*.<sup>53</sup> The combination of this along with the previously noted changes to the customs tariff on off-shore vessel purchases, and the amendments made for ISCs, meant that two

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<sup>52</sup> Brooks, Mary R. (1984), *Commercial Requirements for a Canadian Fleet* (Research Report No. 10.), Halifax: Canadian Marine Transportation Centre; Brooks, Mary R. (1985), *Fleet Development and the Control of Shipping in Southeast Asia* (Occasional Paper 77). Singapore: Institute of Southeast Asian Studies. Reported for a Canadian audience as Brooks, Mary R. (1985), Ownership and Control in Shipping: Problems of Developing Countries, Toronto: Canadian Transportation Research Forum *Proceedings*, 514-537.

<sup>53</sup> For those interested in early Canadian shipping legislation, the most interesting reading is McDorman, Theodore L. (1983), The History of Shipping Law in Canada: The British Dominance, *Dalhousie Law Journal*, 7, 3, 620-652.

of the three planks necessary for a Canadian flag deep-sea fleet were already in place—ability to operate from Canada without incurring Canadian corporate income tax and the ability of ISCs to purchase non-Canadian vessels for deep-sea use without duty. (Section 17(b) as it is worded in the latest iteration of the *Canada Shipping Act* is located in Appendix 3.1.)

To move Canada beyond the ISC model towards a competitive Canadian deep-sea flag option, the third plank—ability of vessels operating under the Canadian flag to crew from globally competitive sources—would need to be adopted. Crews serving on Canadian flag vessels must have Canada certificates, and such certification is available only to citizens and permanent residents. However, when adjustments to this requirement were mooted in 1998, there was no appetite within the unions or within the walls of Canadian industry associations to grow long-term opportunities for sea jobs by opening up the crewing requirements.

The position of those arguing in favour of this third plank being put in place was summed up by Jonathan Seymour, in a 1998 presentation to the Canadian Transportation Research Forum:

*Canada is no longer a high-cost country when it comes to the supply of qualified labour. Canadian senior officers take positions on foreign ships, where the prevailing wages are often better than domestic pay. Canadian junior officers who do not seek out positions on foreign ships can easily spend 15 or more years accumulating enough watch-keeping time to sit their examinations for senior certificates, because of the lack of opportunity in Canada's domestic trade.*

*Canadian marine schools, such as the Pacific Marine Training Campus (PMTC) of the BC Institute of Technology, have difficulty offering a full range of courses because they cannot get enough students, so they are threatened with closure. The career path, once obvious to Canadian mariners through service on the Lakes or the coast, is no longer an expedient one. As a result, Canada's ability to produce suitably qualified seafarers for the many Canadian shore-based jobs requiring professional sea-going qualifications has been seriously curtailed.*

*Meantime, there is a significant and growing shortage of qualified seafarers worldwide. In a recent speech, Barbara Fletcher, director of the London-based Institute of Chartered Shipbrokers, estimated this shortage could reach 45,000 by the year 2002. She also pointed out the impact this would have on the future recruitment of shore-based personnel with seagoing experience. One result is a sharp rise in the number of employment*

*advertisements in the marine press in Europe and Asia. A second is upward pressure on wages offered to skilled personnel internationally.*<sup>54</sup>

Seymour (1998) supported that the two issues, raised by Brooks and Marlow (1983), continue under the Canadian fiscal climate facing Canadian flagged deep-sea shipping: (1) vessel safety standards are unique and onerous, and inflict sufficient costs so as to make the Canadian flag undesirable; and (2) manning requirements fail to recognize the need for at least partial crewing by foreign nationals, which could be met by less onerous reciprocity agreements, should they be in place.

To quote Jonathan Seymour (during the course of this research):

*[T]he fiscal framework created by the ISC amendments to the Income Tax Act can be used to develop a competitive Canadian flag (engaged wholly in international traffic). All that is required is some minor adjustments at the regulatory level; make it so that there is reciprocity on certificates, or allow non-domestic certificates on Canadian ships trading internationally (e.g., change the manning regulations). Canadian senior officers are internationally competitive; the quest for qualifying sea-time makes Canadian junior officers internationally competitive.*

*Canada doesn't need a second flag, or a tonnage tax regime; the Income Tax Act has already been changed, and the concept of the non-duty paid Canadian ship is contained in existing legislation. What's needed [for Canadian flag deep-sea shipping] are changes to manning and certification. The rest is in place. We need to build on success.*

Therefore, it was not the tax issue but the crewing issue that prevented Canada from growing a duty-free Canadian flag deep-sea fleet via the ISC legislation. Canadians would have to be satisfied with the shore-based maritime services jobs created by the IMC initiative and the very few sea-going jobs created by coasting trade legislation. In the revisions to the *Canada Shipping Act* passed in 2001, but not yet in force, there were no changes made to the requirement to have Canadian citizens or permanent residents when filling positions on Canadian flagged vessels (sections 82 (1) and 88 (1), see Appendix 3.1). There were changes, however, made with respect to the process for recognition/reciprocity on foreign certificates (sections 89 (1) and (2) under *Canada Shipping Act* 2001, compared with section 128 of the Act in force, see Appendix 3.1); it appears that the process may have been somewhat streamlined (and moved from

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<sup>54</sup> Seymour, Jonathan (1998), A Time For Change: An Internationally Competitive Canadian Flag? Pragmatic Reform of the Canada Shipping Act is The Answer, *Proceedings*, Edmonton: Canadian Transportation Research Forum, 170-184 at pp. 171-172.



recognition on a case-by-case basis to reciprocity), but is probably not sufficiently less onerous as to encourage reciprocal government-to-government agreements.

It is quite possible that, going forward, the coasting trade will not supply sufficient numbers of personnel with sea-going experience to sustain the ISC needs for shore-based personnel with this experience. A comprehensive study of this requirement has not yet been undertaken.

### **3.7 Evaluating the Experience**

It has been extremely difficult to evaluate the IMC experience and the establishment of ISCs, particularly as companies in this industry are quite protective of data for competitive reasons and not always willing to be noticed. For that reason, the discrepancies in the data reported in Appendices 3.4–3.8 should not be viewed as unreasonable. Even *Lloyd's List of Shipowners* has difficulties tracking the complex and dynamic web of international shipping companies. In an effort to evaluate the effectiveness of ISC legislation, the Vancouver IMC community has been contacted and asked to provide evidence of economic benefit to Canada. The information provided in Appendices 3.6 and 3.7 is that effort to evaluate whether or not the ISC legislation has achieved its intended purpose, the creation of shore-based jobs in the maritime services industry in support of Canadian trading interests.

By October 1993, four companies were willing to go on record as applying to be ISCs based out of Vancouver—Teekay Shipping, Canadian Transport Company, Valles Steamship Company and South Pacific Interline (according to Appendix 3.4). Nine others were reported as waiting for clarifications on Canadian immigration policy.

Of these, Teekay Shipping relocated to Vancouver first and employed, by the end of 1992, 72 staff in Vancouver. The 2002-03 *Lloyd's List of Shipowners* places Teekay as the operator of 55 vessels totalling 3.2 million grt. The vessels are all tankers or bulk carriers (according to Appendix 3.8). The *Vancouver Sun* reported 101 vessels in 2002, not including the 50 it acquired from Navion, and called Teekay the world's largest bulk shipping company; Teekay's operation has more than 4,100 employees in 12 countries, with 265 of them based in Vancouver.<sup>55</sup> As Teekay is a public company listed on the New York Stock Exchange, a profile of Vancouver's largest ISC is possible, and is presented in Appendix 3.5. There is no doubt that the jobs created by the relocation of Teekay to Canada would not have happened if the legislative changes to support ISCs had not occurred.

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<sup>55</sup> Bellett, Gerry (2002), Teekay Rides Global Wave, *Vancouver Sun*, December 17.

The Canadian Transport Company was a retention rather than a relocation. To meet the conditions for classification as an ISC, it was sold by its parent, MacMillan Bloedel, to a subsidiary company in Barbados in 1992. This meant that 27 jobs were initially retained in Vancouver but that company was subsequently sold and is not now operating as an ISC in Canada (see Appendix 3.6).

South Pacific Interline, a small company, was reported as the third to relocate, employing six people at the time of relocation (according to Appendix 3.4). However, the company was sold to a US-based liner operation and so it has left Vancouver.

Valles Steamship was reported as the fourth to relocate to Vancouver and has stayed, accounting for 18 staff in Vancouver (Appendix 3.7). Likewise, there are a number of other companies including Fairmont Shipping, Oak Maritime (Canada) and Waterfront, operator of methanol tankers for Methanex.<sup>56</sup> While Waterfront and Seaboard are listed in Appendix 3.7 as ISCs operating out of Vancouver, they do not appear in *Lloyd's List of Shipowners 2002-03*. This is because it is not only shipowning companies that can avail themselves of ISC legislation. The legislation is broadly interpreted to cover shipowning, operating and management activities.

According to Lloyd's (Appendix 3.8), Seaspan is primarily active in the tug category, but recently the company has formed Seaspan Container Lines, which has taken delivery of five container vessels of the Panamax size (which are on long-term charter) and is in the process of ordering five Panamax and two post-Panamax containerships. They also own a 17,000 dwt gantry craned bulker. The operation of these vessels employs nine staff in Vancouver, the tugs being employed in the domestic trade and not under ISC legislation.

Not all ISCs are based in Vancouver. Expedo Ship Management, a tanker company, operates out of Mississauga, Ontario. It, along with Kent Line, chose non-Vancouver destinations. As part of the Irving Group of companies, the location of Kent Line in Saint John is a natural, as Saint John is the home base for the Canadian-owned multinational conglomerate.

It is particularly interesting to note that the majority of vessels using the ISC legislation are in the tanker and dry bulk trades. Chris Patten, in a recent study *The Contribution of the Foreign Shipping Community to the UK Economy and the Economic Effects of a Change to the Taxation of the Foreign Shipping Community* commissioned by the Baltic Exchange noted that "Shipowners who pay taxes are not competitive in the tanker and dry cargo trades and, in the long run, would be forced out of the business."<sup>57</sup>

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<sup>56</sup> Methanex is the world's foremost producer and marketer of methanol, with roughly 25% global market share for that product.

<sup>57</sup> As reported by Anonymous (2002), London's Taxing Question, *Lloyd's Shipping Economist*, November, 7-10 at p. 10.

Perhaps the most important point here is whether or not shore-based jobs can be grown without access to sea-going work experience. Some positions in the shipping industry do not need a sea-going background but some do. For example, with respect to maritime service functions, some of these are best filled by ex-seagoing personnel, such as coastal pilots or harbour masters, positions such as those involved in vessel operations, nautical oversight (marine) and engineering. For others, they could benefit from some practical time at sea (stevedores, average adjusters, etc.), but it is not absolutely necessary. The marketers and accountants can be grown shoreside.

The Deep-Sea Task Force called for the creation of shore-based jobs in the maritime services industry in support of Canadian trading interests. The benefits of the Vancouver location—political stability (important to many in Hong Kong prior to 1997), inexpensive office space, friendly immigration policies—attracted international deep-sea shipping operations to Canada. Whether more can be attracted is a difficult question to answer. Canada is not a “front of mind” location in shipping circles.

If one is to judge the success of the IMC initiative, the outcome should be measured against the initial Asia-Pacific initiative goals of between 6 and 12 companies controlling 200 ships and employing 800 people directly. Appendix 3.7 shows that two of three of these have been met. If success is measured against the objectives of the Report of the Deep-Sea Task Force, the success could be regarded as more modest.

Today, there are those who are ardent supporters of the ISC concept and those frustrated that the changes did not go further and create a Canadian flag deep-sea option. While some may be disappointed with the number of jobs created, it must be remembered that these employees pay Canadian income taxes and create indirect jobs that also pay Canadian income taxes. This would not have happened without the changes made to the legislation.

They also have an interest in seeing their businesses grow. If that can happen in Canada, there will continue to be the benefit of more shore-based employment. There is no indication that Canada should backtrack on existing legislation, but whether to move towards changing crewing requirements is a question open for debate. Some believe that more back office work would move here if such changes were made; however, the “economic benefits” case has still not been proved for a Canadian flag deep-sea fleet.

## **Acknowledgement**

The assistance of Neal Hewitt, Dalhousie MBA/LLB '05 candidate, in undertaking the background research for this chapter is much appreciated.

## **Appendix 3.1**

### **Relevant Changes to the Income Tax Act and the Canada Shipping Act**

#### **Income Tax Act Changes, 1991**

The Canada *Income Tax Act* was amended in 1991 in an effort to encourage international shipping companies to locate their operations in Canada. The key sections, 81(1)(c), 115(1)(b)(ii), and 250(6), are included in this appendix. These changes in Canadian taxation law provided tax relief to international shipping companies operating from a Canadian base. They no longer had to pay tax in Canada on all of their worldwide earnings. As well, these changes impose no restrictions upon shipping companies with regards to flag, registry or crew nationality and allow shipping companies who qualify to be deemed non-resident for taxation purposes, and therefore not subject to Canadian tax on foreign income.

There are, however, three conditions that must be met in order for companies to qualify to be considered non-resident for tax purposes:<sup>58</sup>

**1. The company must be incorporated outside of Canada.**

In order to qualify as a non-resident a company must be incorporated in a country other than Canada. By definition, companies incorporated within Canada are considered residents and as such will have their entire world income taxed within Canada. A company that is incorporated outside of Canada may control operations within Canada through a branch office. If a company does set up a branch office, and meets the other conditions, none of its income from international shipping will be taxed within Canada.

**2. The company must be an operator of ships.**

In order to avoid paying taxes on its earnings within Canada, the foreign company must be a *bona fide* operator of ships. Otherwise, it will not be protected and will have to pay taxes in Canada. In determining if a company is a *bona fide* operator of ships, Revenue Canada specified that companies that exclusively engaged in the following were not *bona fide* operators:

- Companies that own ships which are bareboat chartered to others
- Companies that carry out shipbroking activities on behalf of others
- Companies that carry out third party ship management activities.

A number of tests for making this determination are provided in Section 250(6).

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<sup>58</sup> Jonathan Seymour & Associates (undated), *Canadian Taxation of International Shipping Corporations*, handout of the International Maritime Centre - Vancouver.

### **3. These ships must be used in international traffic.**

In order to qualify, the company's ships must be engaged in the transportation of goods or passengers either between Canada and a foreign country or between two foreign countries.

## **Relevant Sections of the Income Tax Act as of 2003**

### **Section 81: Amounts not included in income.**

- (1) These shall not be included in computing the income of a taxpayer for a taxation year...
- (c) The income for the year of a non-resident person earned in Canada from the operation of a ship or aircraft in international traffic, if the country where that person resided grants substantially similar relief for the year to a person resident while in Canada,<sup>59</sup>

### **Section 115: Non-resident's taxable income in Canada.**

- (1) For the purposes of this Act, the taxable income earned in Canada for a taxation year of a person who at no time in the year is resident in Canada is the amount, if any, by which the amount that would be the non-resident person's income for the year under section 3 if...
- (b) the only taxable capital gains and allowable capital losses referred to in paragraph 3(b) were taxable capital gains and allowable capital losses from dispositions taxable Canadian properties (other than treaty-protected properties)<sup>60</sup>

### **Section 250: Residence of international shipping corporation.**

- (6) For the purposes of this Act, a corporation that was incorporated or otherwise formed under the laws of a country other than Canada or of a state, province or other political subdivision of such a country shall be deemed to be resident in that country throughout a taxation year and not be resident in Canada at any time in the year, where:
- (a) the corporation
- (i) has as its principal business in the year the operation of ships that are used primarily in transporting passengers or goods in international traffic (determined on the assumption that the corporation is non-resident and that, except where paragraph (c) of the definition "international traffic" in subsection 248(1) applies, any port or other place on the Great Lakes or St. Lawrence River is in Canada), or

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<sup>59</sup> Canada *Income Tax Act*

<sup>60</sup> Canada *Income Tax Act*

- (ii) holds throughout the year shares of one or more other corporations, each of which
  - (A) is a subsidiary wholly-owned corporation of the corporation as defined by subsection 87(1.4), and
  - (B) is deemed by this subsection to be resident in a country other than Canada throughout the year,
 and at no time in the year is the total of the cost amounts to the corporation of all those shares less than 50% of the total of the cost amounts to it of all its property;
- (b) all or substantially all of the corporation's gross revenue for the year consists of
  - (i) gross revenue from the operation of ships in transporting passengers or goods in that international traffic,
  - (ii) dividends from one or more other corporations each of which
    - (A) is a subsidiary wholly-owned corporation of the corporation, as defined by subsection 87(1.4), and
    - (B) is deemed by this subsection to be resident in a country other than Canada throughout each of its taxation years that began after February 1991 and before the last time at which it paid any of those dividends, or
  - (iii) a combination of amounts described in subparagraph 250(6)(b)(i) or 250(6)(b)(ii); and
- (c) the corporation was not granted articles of continuance in Canada before the end of the year.<sup>61</sup>

### **Clarification of Section 250**

Discussions between the Revenue Canada and International Maritime Centre – Vancouver resulted in the following clarifications regarding the operation of ships:<sup>62</sup>

1. A corporation would be considered for taxation purposes to be engaged in the operation of ships when it:
  - Owns and crews ships and arranges passengers or cargo for its own account;
  - Charters out ships that it owns and has crewed to another party;
  - Charters in ships with crew from another party, but has for a specified period or number of voyages the right and responsibility to arrange passengers or cargo for its own account;

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<sup>61</sup> Canada *Income Tax Act*

<sup>62</sup> Jonathan Seymour & Associates (undated), *Canadian Taxation of International Shipping Corporations*, handout of the International Maritime Centre - Vancouver.

- Charters in ships from another party, crews the ship itself and arranges passengers or cargo to transport on the ships for its own account;
  - Charters in ships from another party, then crews them and charters them out to another party; or
  - Engages in any combination of the above activities.
2. Furthermore, a corporation engaged in the operation of ships can be regarded as being involved in a number of discrete activities:
- Raising capital and debt financing
  - Overseeing new construction, acquisition and dispositions;
  - Crewing and catering;
  - Performing repairs and maintenance;
  - Arranging insurance;
  - Marketing;
  - Negotiating charters;
  - Arranging voyages and soliciting passengers or cargo; or
  - Stevedoring.

All of the above activities will be treated as the operation of ships when undertaken as part of an integrated business that is carried on in the same company for its own account. However, these activities will not be treated as the operation of ships if carried on separately from the activities listed in 1.

3. If any of the activities listed in paragraph 2 were established and used for the company's own ships, with its services provided to other third party companies only on the odd occasion that the company did not require them for its own use, these revenues would still be treated as revenues from the company's operation of ships. However, if the services to third parties are of such magnitude an/or regularity so as to constitute a separate business, they would not be considered as revenues from the operation of ships.
4. Revenue Canada has also confirmed that other income sources may also qualify as income from the operation of ships. For example, interest income on funds employed or risked in the shipping business will qualify, whereas interest income on funds in excess of the shipping business requirements would not qualify. As another example, bareboat charter income may qualify as income from the operation of a ship where the vessel was purchased or chartered in for use in the company's own integrated shipping business but, due to a change in circumstances, it is judged prudent to bareboat charter it out with the intention of, as soon as reasonable in the circumstances, crewing it and using it in the company's integrated shipping business.

**Canada Shipping Act, Section 17 as changed in 1998  
(to remove the “Commonwealth” provision)<sup>63</sup>**

17. Unless they are registered in a foreign country, the following ships may be registered under this Part:
- (a) a ship that is owned only by qualified persons and that does not exceed 15 tons gross tonnage;
  - (b) a ship that is owned by a corporation incorporated under the laws of a country other than Canada if one of the following is acting with respect to all matters relating to the ship, namely,
    - (i) a subsidiary of the corporation that is incorporated under the laws of Canada or a province,
    - (ii) an employee or director in Canada of any branch office of the corporation that is carrying on business in Canada, or
    - (iii) a ship management company incorporated under the laws of Canada or a province; and
  - (c) a ship that is in the exclusive possession of a qualified person under a financing agreement under which the person will acquire ownership on completion of the agreement.

**Canada Shipping Act 2001, Crewing Requirements (not yet in force)<sup>64</sup>**

82. (1) The master of a Canadian vessel shall ensure that every person who is employed in a position on board presents to the master all Canadian maritime documents that they are required under this Part to have for that position.
88. (1) Only a Canadian citizen or a permanent resident within the meaning of subsection 2(1) of the *Immigration and Refugee Protection Act* may hold a certificate of competency that is issued under this Part.

**Canada Shipping Act 2001, Acceptance of Foreign Certificates (not yet in force)<sup>65</sup>**

88. (2) The Minister may, on application by a person described in subsection (1), issue a certificate of competency in respect of certain requirements under this Act to the holder of a certificate of competency that was issued under the laws of a foreign state if the Minister is satisfied that the requirements under those laws for the foreign certificate meet or exceed the requirements under this Act. Before issuing the certificate, the Minister may require that the holder take an examination set by the Minister.

**Canada Shipping Act, Recognition of Certificates (in force)<sup>66</sup>**

128. (1) The Governor in Council may direct, subject to such conditions as he may impose, that any certificate of a master or seaman granted by any

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<sup>63</sup> R.S., 1985, c. S-9, s. 17; R.S., 1985, c. 6 (3rd Supp.), s. 87(F); 1998, c. 16, s. 3.

<sup>64</sup> 2001, c. 26, ss. 88, 323.

<sup>65</sup> 2001, c. 26, ss. 88, 323.

<sup>66</sup> R.S., 1985, c. S-9, s. 128; R.S., 1985, c. 6 (3rd Supp.), ss. 14, 87(F).

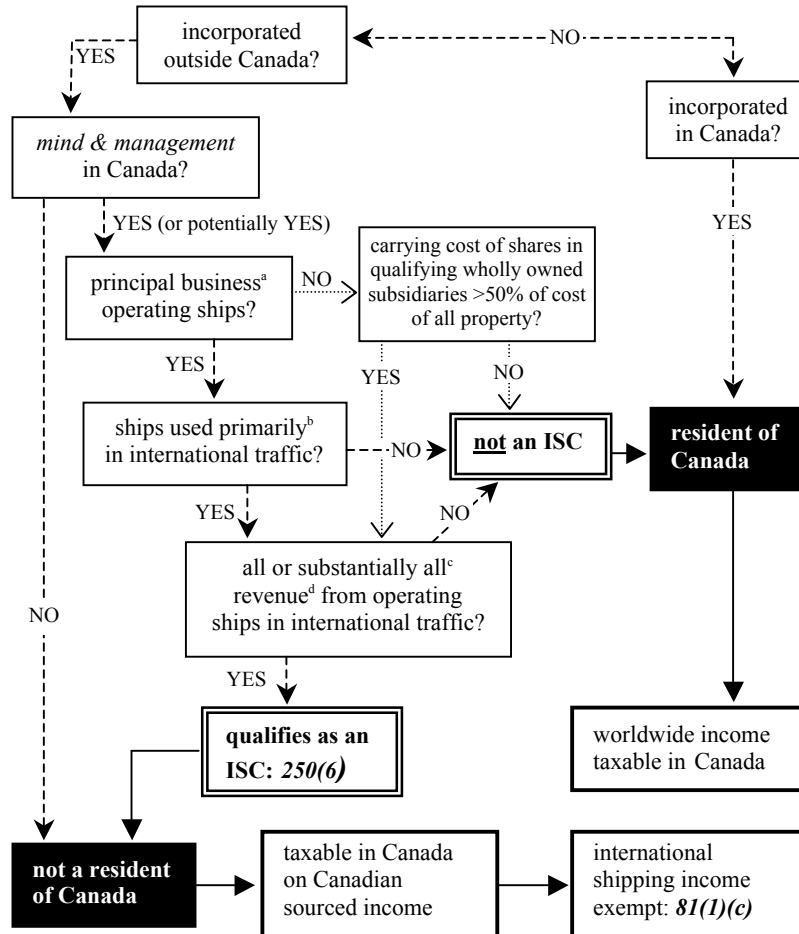


authority competent to issue those certificates under the laws of another country may be accepted in lieu of a certificate granted under this Part, if he is satisfied that examinations for the issue of those certificates are conducted as efficiently as the examinations for the same purpose provided for in this Part, and that the certificates are granted on such principles as to show the like qualifications and competency as those granted under this Part.

### Appendix 3.2: The Application of the Income Tax Act to ISCs

The following chart is based on Appendix 2 from Seymour, Jonathan (1998), A Time for Change: An Internationally Competitive Canadian Flag? Pragmatic Reform of the Canada Shipping Act is the Answer, *Proceedings*, Canadian Transportation Research Forum, 170-84, at page 184. It is used with permission.

#### THE INTERNATIONAL SHIPPING CORPORATION APPLICATION OF SECTIONS 250(6) AND 81(1)(c)



*a principal business could be construed as >50%*

*b used primarily could be construed as >50%*

*c all or substantially all could be construed as >90%*

*d revenue includes dividends from qualifying wholly-owned subsidiary ISCs*

1. A foreign incorporated company engaged in the operation of ships in international traffic, having its mind-and-management in Canada and meeting the prescribed tests, will qualify as an International Shipping Corporation (ISC) under section 250(6) of Canada's Income Tax Act and will be treated as a non-resident of Canada.
2. A non-resident company with international shipping income from traffic to or from Canada is exempt from tax on this Canadian sourced income under section 81(1)(c).

### **Appendix 3.3: Activities at Other IMCs as of October 1993**

This extract from MacNeil, Brenda (1993), *Halifax International Maritime Centre Market Research Report: Final Report*, unpublished report, December (pages 7-11) is used with the permission of Brenda Grob (née MacNeil). The original table numbers have been retained but original footnotes deleted.

#### **Montreal**

In 1991, a special committee headed by the St. Lawrence Economic Development Council (SODES) chairman, was mandated to establish an international maritime centre in Montreal. SODES is similar *to* a Chamber of Commerce in that its members are from the private sector. Although not providing equity assistance, members provide guidance for the centre. The committee used recommendations from the Asia/Pacific Initiative and actions taken by the Vancouver committee as a model. The initiative was delayed because of problems securing funds federally, provincially, and municipally. The funding issue is expected to be settled by the time the report is delivered.

The Montreal committee established three major objectives:

1. To keep shipping companies already operating out of Montreal and involved in international transport from leaving the city;
2. To attract Canadian shipping companies based outside of Canada to the city; and
3. To encourage foreign shipping companies to set up operations in Montreal.

The objectives are closely tied to port activities and development along the St. Lawrence and are to be achieved in three stages:

1. Researching the global market to determine target areas;
2. Organization of an event to draw potential clients to Montreal; and
3. Establishment of a Montreal International Maritime Centre once there is sufficient interest in the initiative.

The committee has lobbied the federal, provincial and municipal governments to support the initiative financially. Federally, the committee has benefited from the tax amendments, and will be receiving funding and support. The committee is attempting to secure extra fiscal advantages for head office employees through Montreal's status as an international financial centre. No decision has yet been reached on that approach.

The Government of Quebec has amended its taxation act to allow improved provincial conditions for all Canadian shipping companies. They have also provided a full time employee from the transportation ministry to initiate the market study; work is expected to begin in October 1993. The City of Montreal is providing financial aid and general

support for the project. They realize the potential benefits and want the process to proceed on schedule.

Once the project has shown that it is viable, the committee will create a separate body, the Montreal International Maritime Centre. Until it is deemed a potential success, no substantial amount of money or manpower will be injected into the project.

Quebec is unique in that it has control of its immigration policy and is not bound by federal convention. To this end, the IMC committee is negotiating with the Quebec government to ensure efficient immigration procedures.

The change to the *Income Tax Act* is the primary marketing factor used by Montreal in the establishment of an International Maritime Centre. Other factors included are: the time zone, the infrastructure, the city's interest in international affairs, lower-than-average wage scales, and quality of life. Several factors mentioned as being unique to Montreal include: high productivity of workers (exceeding Londoners by 301/G to 401/G), the bilingual and multi-cultural environment, the development of a secretariat to deal with international affairs, and the cooperation the city provides to the Société du Centre de Conférences Internationales de Montréal.

**Table 3: Market Factors used by Canadian IMC Locations**

	<i>Vancouver</i>	<i>Montreal</i>	<i>Toronto</i>	<i>Saint John</i>
Tax Changes:				
Federal	X	X	X	X
Provincial		X		
Port Activities	X	X		X
Favourable Time Zone	X	X	X	X
Transportation Infrastructure	X	X	X	X
Telecommunication Network	X	X	X	X
Marine Service Sector	X	X	X	X
Int. Financial Sector	X	X	X	X
Favourable Marketplace	X	X	X	X
Multicultural Environment	X	X	X	X
Quality of Life	X	X	X	X
Cost of Living	X		X	X
Labour Costs	X	X	X	X
Social Programs	X			X
Int. Affairs Secretariat		X		
Immigration & Work Permits	X			
Political Stability	X			

Table 3 lists the marketing factors promoted by the Canadian IMC locations. While not an exhaustive list, it does show the similarities in marketing factors. These factors must be recognized when the committee begins formation of its marketing material. An important success factor may be in differentiating Halifax from other Canadian centres. For example, Montreal has differentiated itself by changing its provincial tax laws, and Vancouver has improved the immigration process.

A recent magazine article in *The Baltic* discussed the Canadian ports of Vancouver, Montreal and Toronto mentioning what each had to offer the international maritime industry. Montreal had a full-page advertisement promoting the IMC, but the text of the article focused solely on recent happenings by the Port of Montreal with no mention of the IMC.

### ***Saint John***

An international marine centre is considered a local addition to Saint John as the city's economy and lifestyle has historically been tied to port activities. The Saint John IMC is being promoted by the city of Saint John and the harbour commission. No grant money has been awarded to the committee and they are striving for promotion of the initiative by the city and the private sector, not the government.

In September 1993, Saint John distributed its first marketing material in the form of a 32-page brochure which promoted the city as a safe haven for the international shipping industry and as the most cost effective business location in North America. Specific advantages of Saint John that are being promoted in the brochure include: Canada's favourable tax environment, a world class maritime infrastructure, modern telecommunications services, affordable rental space and low labour costs. New Brunswick is profiled, economic comparisons to other provinces are made, operational costs are correlated with several North American cities, and corporate taxes are matched to specific international countries.

Saint John is featured in the fall edition of *The Baltic* along with Halifax. The port capability and the IMC initiative are profiled in the article. Specific mention is made to New Brunswick being the only bi-lingual province in Canada.

### ***Toronto***

Toronto hopes to establish an International Maritime Centre despite the fact that it does not have an ocean port. Following the change to the *Income Tax Act*, Toronto commissioned a feasibility study from the international consulting firm of Peat Marwick Thorne. The firm's mandate was to determine whether international shipping companies

could be attracted to central Canada. The report concluded that Toronto had a good chance of attracting shipowners and ship managers due to the federal taxation changes, infrastructure, and location in the Eastern Time Zone. *The Baltic* article depicts Toronto as a leading financial centre with a world-class transportation network and a leading marine insurance centre in Canada. The fact that the International Union of Marine Insurance is holding its annual conference in Toronto in 1994 is thought to reflect that importance.

At the present time, requests for information are being directed to the Municipality of Metropolitan Toronto. Marketing material is still believed to be in the preparation stage, and no potential targets have been publicly identified.

### **Appendix 3.4: Assessment of the Vancouver IMC as of October 1993**

This extract from MacNeil, Brenda (1993), *Halifax International Maritime Centre Market Research Report: Final Report*, unpublished report, December (pages 12-14) is used with the permission of Brenda Grob (née MacNeil). The original table numbers have been retained but original footnotes deleted.

Vancouver has had an advantage over other Canadian IMC initiatives. Brochures and newsletters have been in circulation since the legislative decision came into force in March 1992. A well designed and laid out 18-page information package was issued in November 1992. The package was broken up into sections entitled taxation, customs and incentives, about Vancouver, economic overview, markets and trade, social programs, marine services, business contacts, property costs, labour, transportation and communication.

Vancouver also participated in an article in the summer issue of *The Baltic*. Vancouver received the majority of the attention in the article and proclaimed the virtues of both its port facilities and its IMC potential.

Vancouver has used both trade missions and trade shows as market tools. Missions have been in the form of information groups and individual meetings. A Mission to Greece spoke to shipowners and operators to spread awareness of the tax changes. Individual meetings were held with selected companies from Hong Kong. Communication with these firms had previously been initiated. Vancouver also sent the Executive Director of the IMC to the Nor-Shipping trade show held in Oslo in June 1993.

[next paragraphs deleted]

**Table 4. Profile of Companies Relocating To Vancouver**

	Valles Steamship Co.	South Pacific Interline	Teekay Shipping Co.	Canadian Transport Co.
Nationality of Owner	Hong Kong	Canadian	Norway	Barbados Subsidiary
Previous Location	Hong Kong	Canada	Long Beach, California	Canada
Size	10-12 vessels	2-4 vessels	60 vessels	6 vessels
Type of Vessels	Bulk Carriers Tankers	Bulk Carriers	Tankers	Bulk Carriers
Canadian Employment	N/A	6 people	85 people	27 people
Other	Benefited through new Immigration Agreement	Trades along West Coast of NA	\$2.5 million set-up cost	Owned by MacMillan Bloedel

Teekay Shipping was the first to move “mind and management” offices to Vancouver. Management officials with Teekay Shipping were involved with the lobbying efforts to change the Canadian tax laws. Norwegian owned, it manages 52 tankers for its exclusive principals, and 16 others are directly or indirectly under its control. Teekay Shipping was reported in the *Financial Times* to be worth \$2 billion in 1991.

The present Teekay Shipping (Canada) Ltd. relocated to Vancouver from Long Beach, California. Captain John Hood, President of Teekay Shipping, cited quality of life, reasonable costs, and the supply of motivated and highly educated people as the prime factors in relocation. Captain Hood stated that it cost \$2.5 million to set up in Vancouver, and that it is foreseeable that between 54 million and \$5 million would be spent annually, including salaries.

The relocation of Teekay Shipping was reasonably problem-free, as they had the Department of Employment and Immigration Canada and the BC Ministry of International Business and Immigration on their side. The trade-off for swift entry was job creation, with certain requirements laid down by the government. Teekay expected that by the end of 1992, 85 people would be employed, all but 13 of them hired in Vancouver.

Vancouver has been successful in keeping a local shipping company, Canadian Transport Co. in Canada. To become eligible for the tax benefits, Canadian Transport Co. was sold by MacMillan Bloedel to a subsidiary company in Barbados in 1992. The “mind and management” of the six vessels, and the 27 people employed, will remain in Vancouver.

South Pacific Interline (SPI) is the third company to take advantage of Vancouver’s IMC location. SPI is a small company which trades from Vancouver and US Pacific northwest ports to Tahiti, the Samoas and Tonga. SPI ships carry power poles, lumber and agricultural products from BC, Alberta and Quebec. The firm presently employs six people.

The Premier of British Columbia announced on April 28, 1993, that Valles Steamship Ltd. would be locating its shipping headquarters in Vancouver. Valles controls 10-12 vessels and is owned by the Koo family of Hong Kong. Management control is by David Koo, former chairman of the Hong Kong Shipowners Association. Valles Steamships is the first major Asian company to apply for relocation in Vancouver and a government agreement to establish guidelines for immigration acceptance of key company personnel is considered an important factor in attracting the firm. Mr. Koo is a very influential businessman, and it is felt that if Valles receives smooth and swift acceptance, then other Hong Kong firms will soon follow.



Wilford Vacheresse, an immigration consultant who turned his attention to helping shipping companies emigrate to Vancouver, says his company, Secretariat Overseas Shipping (SOS), lobbied on behalf of Hong Kong owners in 1991, facilitating negotiations directly with the government. Five Hong Kong-based shipping companies were rumoured to be in the process of moving to Canada: Fairmont Shipping, Oak Steamships, Grand Seatrade, Teh-Hu and Valles Steamship Ltd.

Valles is the only one of the five publicly announced to apply for relocation since the *Seatrade Review* article. Information contained in the 1993 *Lloyd's Maritime Directory* on the remaining four firms indicates that Teh-Hu Cargocean Management Ltd. operates at least four bulk carriers. Oak Steamships operates 11 bulk carriers and a general cargo carrier. Fairmont Shipping was listed as a Creek company and Grand Seatrade was not listed.

[end of Appendix 3.4]

### **Appendix 3.5: Teekay Shipping Corporation**

Teekay Shipping Corporation is a provider of international crude oil and petroleum product transportation services through a fleet of medium-sized oil tankers. The Company's modern fleet of tankers provides transportation services to major oil companies, oil traders and government agencies worldwide. As of March 1, 2002, Teekay's fleet consisted of 95 vessels, including 63 Aframax oil tankers (including five time-chartered vessels, two Aframax-size oil/bulk/ore (O/B/O) carriers trading exclusively as crude oil carriers, two Aframax tankers converted to floating storage and off-take vessels (FSOs) and two newbuildings); 18 shuttle tankers (including three newbuildings and one vessel converted to an FSO); eight oil/bulk/ore carriers that are operated through an O/B/O pool managed by the Company; two smaller oil tankers; one Very Large Crude Carrier, and three Suezmax-size newbuildings.

*From: <http://www.nyse.com/>*

Founded	1973
Fiscal Year End	December 31*
Corporate Head Office	Nassau, The Bahamas
Operational Headquarters	Vancouver, Canada
Number of Offices	16 offices worldwide
Fleet	105 vessels (including five vessels time-chartered-in and 15 newbuildings to be delivered by 2003 and 2004)
Average Age of Aframax Fleet	9.07 years (including newbuilds) / 11.02 years (excluding newbuilds)
First Quarter Fiscal Year 2003 Voyage Revenues	US\$282,232,000
Fiscal Year 2002 Voyage Revenues	US\$783,327,000
IPO	July 20, 1995
Listed	NYSE
Symbol	TK
Shares Issued and Outstanding	39,757,954 (as of March 31, 2003)
Dividend	\$0.215 per share, per quarter (paid every quarter since IPO)

*From: [http://www.teekay.com/TK\\_311.asp](http://www.teekay.com/TK_311.asp)*

### **Appendix 3.6: The Original ISCs and Their Status Today**

The list of companies was provided by Bernie Jones of Seaspan Shipbroking in June 2003.

<b>Company</b>	<b>Comments</b>
Alcan	
Canadian Transport	Bought by Gearbulk
Expedo	
Fairmont	
Fednav	
Golden Ocean	No longer in business
Desgagnes	
Kent Line	
Manhattan Shipping	
Normar	Closed down
Northern Star	Closed down
Oak Maritime	
Orient Steamship	
Pacific Concord	Closed down
Seaboard Shipping	
Seaspan	Strong growth (see Section 3.7)
Sinotrans	
Supership	Can't trace them
Teekay	Strong growth (see Appendix 3.5)
Teh-Hu	Relocated to Hong Kong
Transpacific	
Unique	Closing their office down due to internal reasons
Valles	
Waterfront (Methanex)	

### **Appendix 3.7: The ISCs in 2003**

This information was provided by Bernie Jones of Seaspan Shipbroking on behalf of ISC companies prepared to provide this information.

<b>Owner</b>	<b>Vessels</b>	<b>New Buildings</b>	<b>Staff</b>
Alcan	3		
Expedo	4		
Fairmont	38	2	50
Fednav	70 (53 on t/c)	15 (all t/c)	125
Desgagnes	13		
Kent Line	4		
Manhattan	Does not want to reveal any information		
North American Steamships	11 (on t/c)		14
Oak Maritime	15	5	19
Orient Steamship	3	1	9
Seaboard	No information provided		
Seaspan Container	6	7	9
Sinotrans	6		10
Teekay	61 (in Canada)	6	246
Transpacific	Believed to be 2-3 ships		
Valles	9		18
Waterfront (Methanex)	No information provided		
<b>Total</b>	<b>247</b>	<b>36</b>	<b>500</b>

Note: t/c means time-charter.

### **Appendix 3.8: Summary Information on Selected Known ISCs**

**Teekay Shipping Canada Ltd.  
Suite 1400, 1 Bentall Centre  
505 Burrard Street  
Vancouver, BC V7X 1M5**

<b>Type of Ship</b>	<b>Ship Name</b>	<b>Year</b>	<b>Gross Tonnage</b>
Bulk/ore/oil carrier	Vancouver Spirit	1992	63709
Bulk/ore/oil carrier	Victoria Spirit	1993	63709
Bulk/ore/oil carrier	Tekay Fair	1981	44887
Oil Tanker	Alliance Spirit	1989	52515
Oil Tanker	Bahamas Spirit	1998	57947
Oil Tanker	Clare Spirtir	1986	52518
Oil Tanker	Clyde Spirit	1985	52629
Oil Tanker	Coumbia Spirit	1988	49279
Oil Tanker	Falster Spirit	1995	52875
Oil Tanker	Gotland Spirit	1995	52875
Oil Tanker	Hudson Spirit	1988	49279
Oil Tanker	Kiowa Spirit	1999	62619
Oil Tanker	LOA Spirit	1999	62619
Oil Tanker	Kyeema Spirit	1999	62619
Oil Tanker	Mersey Spirit	1986	52862
Oil Tanker	Orkney Spirit	1993	55864
Oil Tanker	Sabine Spirit	1989	49279
Oil Tanker	Shannon Spirit	1987	52524
Oil Tanker	Shetland Spirit	1994	55864
Oil Tanker	Cook Spirit	1987	53156
Oil Tanker	Oinoussian Spirit	2002	62247
Oil Tanker	Hamane Spirit	1997	57463
Oil Tanker	Kanata Spirit	1999	62685
Oil Tanker	Koyagi Spirit	1989	52787
Oil Tanker	Musashi Spirit	1993	153642
Oil Tanker	Namsan Spirit	1988	59289
Oil Tanker	Nassau Spirit	1998	57925
Oil Tanker	Pacific Spirit	1988	59289
Oil Tanker	Sebarok Spirit	1993	52508

Oil Tanker	Seletar Spirit	1988	52764
Oil Tanker	Semakau Spirit	1988	52484
Oil Tanker	Senany Spirit	1994	52508
Oil Tanker	Sentosa Spirit	1989	52500
Oil Tanker	Seraya Spirit	1992	52507
Oil Tanker	Shilla Spirit	1990	59289
Oil Tanker	Singapore Spirit	1987	52997
Oil Tanker	Sudong Spirit	1987	52764
Oil Tanker	Torban Spirit	1994	57486
Oil Tanker	Torres Spirit	1990	54963
Oil Tanker	Ulsan Spirit	1990	59289
Products Tanker	Sotra Spirit	1995	52875
Products Tanker	Kyushu Spirit	1991	53988
Products Tanker	Leyte Spirit	1992	57448
Products Tanker	Luzon Spirit	1992	57448
Products Tanker	Mayon Spifit	1992	57448
Products Tanker	Onozo Spirit	1990	57450
Products Tanker	Palmstar Cherry	1990	57450
Products Tanker	Palmstar Lotus	1991	57450
Products Tanker	Palmstar Orchid	1989	57450
Products Tanker	Palmstar Poppy	1990	57450
Products Tanker	Palmstar Rose	1990	57450
Products Tanker	Palmstar Thistle	1991	57450
Products Tanker	Poul Spirit	1995	57463
Products Tanker	Teekay Spirit	1991	57450
Tanker	Magellan Spirit	1985	55903
<b>Total</b>		55	3169187

**Kent Line**  
**2nd Floor, 300 Union St.**  
**Saint John, NB E2L 4B4**

<b>Type of Ship</b>	<b>Ship Name</b>	<b>Year</b>	<b>Gross Tonnage</b>
Container Ship	Tropic Atlantic	1999	13020
Container Ship	Tropic Canada	2000	12827
General Cargo	Kent Voyageur	1982	12472
Other Pontoons	Kent Carrier	1971	8365
Products Tanker	Irving Canada	1981	22233
Products Tanker	Irving Eskimo	1980	21673
Products Tanker	Wellington Kent	1980	7745
<b>Total</b>		<b>7</b>	<b>98335</b>

**Expedo Management Canada**  
**Expedo Ship Management (Canada) Ltd.**  
**Suite 1510, One City Center Drive**  
**Mississauga, ON L5B 1M2**

Chemical Tanker	New Concord	1980	22519
Chemical Tanker	New Endeavor	1981	22519
Oil Tanker	New Horizon	1988	80274
Oil Tanker	New Vision	1994	164251
Oil Tanker	New Wisdom	1993	164251
Oil Tanker	New World	1991	80000
<b>Total</b>		<b>6</b>	<b>533814</b>

**Fairmont Shipping Canada**  
**300-1112, West Pender St.**  
**Vancouver, BC V6E 2S1**

<b>Type of Ship</b>	<b>Ship Name</b>	<b>Year</b>	<b>Gross Tonnage</b>
Bulk carrier with vehicle decks	Crystal Bulker	1995	18302
Bulk carrier with vehicle decks	Emerald Bulker	1995	18302
Bulk carrier with vehicle decks	Tier Durban	1995	18302
Bulk carrier with vehicle decks	China Merchant	1986	22145
Bulk carrier with vehicle decks	China Trader	1990	28320
Bulk carrier with vehicle decks	Star Savannah	1983	11896
Bulk carrier with vehicle decks	Star Masaya	1998	24953
Bulk carrier with vehicle decks	Victory	2001	30053
General Cargo	Tiger Falcon	1997	17879
General Cargo	Torm America	1990	13651
Wood chip carrier	Southern Belle	1988	34739
<b>Total</b>		11	238542

**Valles Steamship Canada**  
**Suite 1160, Guinness Tower**  
**1055 West Hastings St.**  
**Vancouver, BC V6E 2E9**

Bulk carrier with vehicle deck	Silver Clipper	1993	77201
Bulk carrier with vehicle deck	Navios Bulker	1981	37271
Bulk carrier with vehicle deck	Gateway Bulker	1994	77201
Oil Tanker	Seabridge	1996	56951
Oil Tanker	Seamaster	1990	54961
Products Tanker	Seafalcon	1991	52603
<b>Total</b>		6	356188

**Oak Maritime (Canada)**  
**Suite 1500, 1111 West Georgia Street**  
**Vancouver, BC V6E 4M3**

Wood chip carrier	Crimson Jupiter	1996	39901
Bulk carrier with vehicle decks	Yue Shan	2000	86192
Bulk carrier with vehicle decks	Mineral Oak	1996	85721
<b>Total</b>		3	211814



**Seaspan International  
10 Pemberton Avenue  
North Vancouver, BC V7P 2R1**

<b>Type of Ship</b>	<b>Ship Name</b>	<b>Year</b>	<b>Gross Tonnage</b>
Tug	Seaspan Canadian	1975	149
Tug	Seaspan Challenger	1970	476
Tug	Seaspan Champion	1970	150
Tug	Seaspan Chief	1966	149
Tug	Seaspan Commodore	1974	648
Tug	Seaspan Corsair	1975	149
Tug	Seaspan Crusader	1974	148
Tug	Seaspan Cutlass	1975	149
Tug	Seaspan Discovery	1984	435
Roro cargo/ferry	Seaspan Doris	1968	2612
Tug	Seaspan Falcon	1993	188
Deck cargo pontoon	Seaspan Forester	1970	8648
Roro cargo/ferry	Seaspan Greg	1964	2493
Tug	Seaspan Guardian	1974	149
Tug	Seaspan Hawk	1993	188
Tug	Seaspan King	1968	498
Tug	Seaspan Lorne	1961	149
Tug	Seaspan Master	1966	149
Tug	Seaspan Monarch	1977	376
Tug	Seaspan Navigator	1970	148
Tug	Seaspan Pacer	1967	203
Tug	Seaspan Queen	1964	207
Tug	Seaspan Regent	1976	621
Deck cargo pontoon	Seaspan Rigger	1981	6277
Tug	Seaspan Sovereign	1944	432
Tug	Seaspan Valiant	1970	110
Tug	Seaspan Victor	1970	110
Other pontoons	Seaspan 240	1962	4826
Deck cargo pontoon	Seaspan 250	1976	5102
Deck cargo pontoon	Seaspan 251	1977	5102
<b>Total</b>		<b>30</b>	<b>41041</b>

**FedNav**  
**Suite 3500, 1000 de la Gauchetière Ouest**  
**Montreal, QC H3B 4W5**

<b>Type of Ship</b>	<b>Ship Name</b>	<b>Year</b>	<b>Gross Tonnage</b>
Ore/bulk/oil carrier	Arctic	1978	20236

*Source: Lloyd's List of Shipowners 2002-2003*

# CHAPTER 4 – RECENT INTERNATIONAL SHIPPING POLICY DEVELOPMENTS AMONG DEVELOPED COUNTRIES

## 4.1 Introduction

While the number of deep-sea shipping studies undertaken by Canada from 1970-1985, as summarized in Chapter 2, demonstrated an intense interest by government in this matter, Canada did not then choose, and has not since chosen, to set out in any formal and comprehensive way a national shipping policy. Nevertheless, initiatives announced and taken, particularly following the submission of the 1985 *Task Force on Deep-Sea Shipping*,<sup>67</sup> provide a broad indication as to the government's policy objectives, at least in relation to this sector of the Canadian shipping industry. These objectives stem mainly from apparent broad acceptance of the principal recommendations of the Task Force Report, which advocated that Canada maintain and strengthen a core of international shipping expertise, but also made clear that this goal did not necessarily have to be achieved through ownership and operation of Canadian registered vessels.

As it has now been 18 years since the *Task Force on Deep-Sea Shipping*, the time for Canada to take stock of its deep-sea policy is long overdue. Furthermore, it is useful to examine what other options exist as possibilities for implementing its *de facto*, if undeclared, policy. As part of this stock-taking, it makes sense to examine and review the strategies adopted by other developed countries to see whether courses of action that they have pursued might shed light on possible future courses of action for Canada. This chapter is therefore devoted to a review of other national, principally European, deep-sea shipping policy initiatives that have been taken over the course of the last decade.

## 4.2 European Marine Transportation Policy Directions

As the oversight role of the European Commission in maritime transport has evolved, it has become increasingly concerned with the decline in the traditional shipping registers of its Member States. This has manifested itself in various ways. The first step to establish a substantive European economic policy for shipping was taken in 1986 with a

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<sup>67</sup> Transport Canada (1985), *Task Force on Deep-Sea Shipping. Report to the Minister of Transport*.

package of measures covering market liberalization and competition policy, set out in a major paper entitled *Towards a New Maritime Policy*.<sup>68</sup> The revised policy objective was stated as: “to ensure freedom of access to shipping markets across the world for safe and environmentally friendly ships, preferably registered in EC Member States with Community nationals employed on board.”

The document proposed a two-fold strategy: to ensure safety and fair competition in international open markets, and to establish a Community framework for enhancing shipping competitiveness. This framework encompassed policy support for training and employment (to develop and safeguard maritime expertise), enhancement of research and development, and the provision of state aids. Guidance on state aids was first provided in guidelines promulgated in 1989, and was subsequently refined and adjusted in revised guidelines put out in 1997.

### **4.3 The European Commission State Aid Guidelines**

#### **4.3.1 Objective**

The European Commission, in its 1997 Guidelines, endorsed the long-term aim as being to ensure freedom of access to shipping markets across the world for safe and environmentally friendly ships. While accepting this free market principle, the EC also reaffirmed its preference that, as far as possible, such ships should be registered in EC Member States with Community nationals employed on board.<sup>69</sup> The guidelines recognized, however, that it was relatively expensive to operate EC registered ships with EC seafarers on board, and that this situation inhibited the pursuit of high quality operations and undermined the goal of safe, efficient, environmentally friendly transport. It was these circumstances that led to the fundamental decision taken by the European Commission to support the provision of state aid to maritime transport, and that the reason for doing so was to create conditions that allowed fair competition with flags of convenience. Particularly targeted was fiscal competition, and competition in relation to crewing costs.

The stated reason for the 1989 guidelines was recognition that “Member States’ fleets faced a difficult competitive position because of advantages available to operators flying flags of third countries, including flags of convenience.”<sup>70</sup> The declared aim of these guidelines was, therefore, to reduce this difference in operating costs while ensuring that State aid did not exceed a ceiling constituting the difference between the lowest cost

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<sup>68</sup> European Commission (1996), *Towards a New Maritime Policy*.

<sup>69</sup> European Commission (1997), *Community Guidelines on State Aid to Maritime Transport (97/C 205/05)* 5.07.1997, Para 1.1

<sup>70</sup> European Commission (1997), Para 1.3.

Member States (the guidelines cited Portugal and Cyprus) and those operating under flags of convenience.

In view of the continuing decline in Community fleets in the early 1990s, and a concern regarding increasing divergence of policy responses by Member States, the Commission concluded that the aid strategy required further review. In a document *Community Guidelines on State Aid to Maritime Transport 97/C 205/05* published in the EC Official Journal on July 5, 1997, the European Commission updated its guidelines within which state aid to maritime transport would be approved. The principal objectives of this aid were declared to be to safeguard EC employment (both on board and ashore), to preserve maritime know-how and skills in the Community, and to improve safety.<sup>71</sup>

In these new guidelines, the European Commission recognized that the competitive difference between ships registered in the Community and those registered outside, especially those operating under flags of convenience, depended primarily on fiscal costs. This was due, principally, to the fact that the cost of capital was essentially the same worldwide, and that there was little or no difference in the technology available. The fiscal costs, mainly corporate taxation and wage-related liabilities, were concluded to be the critical and distortive factors.<sup>72</sup>

The EC also recognized that, whereas normally operating aid should be ‘exceptional, temporary, and degressive,’ in the case of maritime transport the competitiveness problem was seen as structural, deriving in large part from external factors. Hence no immediate prospects existed for closing the cost gap, and the need for aid measures was not expected to be short-term.<sup>73</sup>

#### **4.3.2 Fiscal Directions**

With regard to fiscal treatment, the Guidelines endorsed a number of measures on the basis that they were shown to safeguard high quality employment. These included accelerated depreciation and the right to reserve profits made on the sale of ships for a number of years on a tax-free basis provided that they were eventually re-invested in the acquisition of ships. The guidelines also endorsed the replacement of the normal corporate tax system by a tonnage tax. (This latter tax is described in more detail later in this Chapter and in Appendix 4.1.)

The document also made clear that, since the objective was to promote the competitiveness of the EC fleets, fiscal alleviation schemes should require a link with a Community

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<sup>71</sup> European Commission (1997), Para 2.2

<sup>72</sup> European Commission (1997), Para 1.4

<sup>73</sup> European Commission (1997), Para 1.4

flag as a rule. However, the guidelines accepted that such schemes might also exceptionally be approved where they applied to the entire fleet operated by a shipowner company established within a Member State's territory. Approval depended upon it being demonstrated that the strategic and commercial management of all ships concerned was effectively carried out within the territory, and that this activity contributed substantially to economic activity and employment within the Community. Furthermore, in such instances, the aid had to be necessary to promote the repatriation of the strategic and commercial management of all ships concerned to the EU and the beneficiaries of such schemes had to be liable to payment of corporate tax in the Community. In such cases, the Commission would also require the provision of regular reports, and would closely monitor the situation to ensure it did not distort competition between Member States.<sup>74</sup>

Such schemes were intended to benefit only the shipping sector, and so the fiscal advantages offered had to be restricted to shipping activities by suitable 'ring-fencing' provisions. To quote the guidelines: "This approach would help EC shipping to be competitive, with tax liabilities comparable to levels applying elsewhere in the world, but would preserve a Member State's normal tax levels for other activities and the personal remuneration of shareholders and directors."<sup>75</sup>

### **4.3.3 Labour Cost Directions**

With regard to labour-related costs, again the Commission accepted that maritime transport required special consideration. While in most industrial sectors differentials between low wage countries and Member States were very significant, it was generally accepted by the Commission that competitiveness and employment could be improved in many of them by integrating new production technology, innovation, quality and training. However, the Commission took the position that this was not the case with maritime transport. As a result, the Commission authorized state aid, permitting up to a maximum reduction of liabilities to zero, in the form of:

- Reduced rates of contribution for the social protection of EC seafarers,
- Reduced rates of income tax for EC seafarers.

In addition, the Guidelines included as acceptable any aid provided to reduce the cost of crew relief, and thus authorized any payment or reimbursement of the costs of repatriation of seafarers working on board ships that were entered in Member States' registers.

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<sup>74</sup> European Commission (1997), Para 3.1

<sup>75</sup> European Commission (1997), Para 3.1.

## 4.4 Initiatives by Major European Maritime States

The promulgation of these 1997 guidelines acted as a stimulus for action by many of the Member States, some of whom had already adopted measures under the 1989 guidelines. This section broadly summarizes the nature and extent of the steps taken by a number of the major European maritime States.

State aid that has been declared to be acceptable under the EC Guidelines has taken a variety of forms, including:

- Accelerated depreciation
- Deferred taxation on capital gains
- Tonnage tax
- Social-security cost relief
- Seafarers income tax relief
- Relief in relation to crew repatriation
- Aid to support safety and environmental standards
- Aid to support training.

It is noteworthy that, while the forms of aid selected by individual states have varied, there are at least two common themes. First, the application of a tonnage tax has almost invariably, sooner or later, been regarded as an essential ingredient. Second, it has been generally accepted by many tonnage tax proponents that such a tax needs to be supported by a number of other measures, usually including those associated with crewing cost reduction.

While Greece has had a tonnage tax regime in place since 1938, the comparatively high level of that tax meant that it did not attract much attention for nearly five decades. In this respect, the first European State to adopt, as an option, a tonnage tax pitched at a level to compete with flag of convenience tax rates was the Netherlands in 1996. The Dutch government was thus the first to conclude that the decline in national shipping, maritime skills and maritime-related economic activity could not be halted by its current measures. These included a policy of subsidizing shipowners, a practice that tended to distort the market rather than enhance market competitiveness. The new approach relied instead on creating an attractive climate in which shipping was seen as the nucleus of the country's maritime business cluster. The central element of the Netherlands policy package (reflecting the new emphasis on Dutch ownership rather than the Dutch flagged fleet) was an optional tonnage-based tax regime. Labour cost distortions were addressed by flag-related wage subsidies coupled with increased flexibility in manning rules.<sup>76</sup>

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<sup>76</sup> UK Department of Environment, Transport and the Regions (1998), *British Shipping Charting a New Course*, December.

The dominant view in that country now is that the new initiatives have been an outstanding success. Despite the fact that qualifying ships did not need to fly the Dutch flag in order to qualify, the Dutch flag fleet grew by around 20% during the first year of application. Indeed, the demand for Dutch seafarers became so great that it created a significant shortage, to a point where the rules requiring Dutch ships to have a Dutch master had to be changed to authorize masters from other EU States.<sup>77</sup> The results have been viewed as so successful that the Netherlands is now exploring ways of extending the provisions to other sectors of the maritime industry.

Very shortly thereafter, Norway introduced a tonnage tax regime modeled on the system introduced by the Netherlands. This move followed adoption of, and added support to, its two register concept, the Norwegian Ordinary Ship Register (NOR) and the Norwegian International Ship Register (NIS), which had been in place since 1987. The introduction of the tonnage tax resulted in a significant growth in the Norwegian owned and operated fleet, aided by the fact that seafarers were entitled to allowances on their pre-tax income, and by the introduction of a “net-wage” system. Since that time, however, there has been significant turbulence in Norwegian policy-making regarding fiscal and labour-related costs for the shipping industry, possibly simply because the success of the measures raised questions as to whether they were overly generous. This has resulted in adjustment to aid levels, either up or down, by successive governments. At present there exists an uneasy compromise, and the expectation of possible transfers of Norwegian-flagged vessels to more attractive Swedish or Danish registers.<sup>78</sup>

Germany introduced an optional tonnage tax system in early 1999, again modeled on the Netherlands’ approach. Provisions, approved by the EC as meeting its Guidelines, were also introduced that permitted retention of a percentage of income tax, provided support in reducing non-wage labour costs, and stimulated expanded maritime training. Germany was followed in early 2000 by the United Kingdom, which is discussed more fully as a case study in Section 4.6.

Following on the heels of the UK, a number of other European States have now opted for a tonnage tax regime coupled with various labour-related aid measures. Ireland, Finland, Denmark and Spain have all now introduced such measures, while France and Belgium have announced plans to do so, and are currently seeking EC approval for their proposals. France has also agreed to set up a new French International Register to replace the uncompetitive Kerguelen flag.<sup>79</sup> Sweden, which already has in place an attractive “net wage” system, is also considering the introduction of a tonnage tax regime.

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<sup>77</sup> The Transportation Institute, Washington, DC. *Maritime Aid Policies of Select Countries* <http://www.trans-inst.org> accessed May 2003.

<sup>78</sup> Ibid.

<sup>79</sup> France to replace Kerguelen Flag. *Fairplay International Shipping Weekly*, 8 May 2003.



It is noteworthy that in Italy, despite significant debate, no decision has been taken to introduce a tonnage tax regime. There is, as a result, an expectation of a mass exodus of Italian shipping to other European Member States where more favourable fiscal terms exist.<sup>80</sup>

#### **4.5 Marine Transportation Aid Policies—Other Non-European States**

While it is fair to say that the dominant activity with regard to the provision of state aid to improve fiscal and labour cost competitiveness has been focused in Europe, by no means has it been restricted to EC States. Significant attention has been directed by a number of leading maritime countries outside Europe to exploring the merits of following the European policies, and indeed action has been taken to move in a similar direction.

In the United States, there has been considerable attention paid to the trends in national shipping policies of many European States, and the associated tax and labour laws applying to marine transportation. This increased focus of attention took on new, more substantive meaning with the introduction of a draft Bill, entitled *HR 3262—The Merchant Marine Cost Parity Act*, which was introduced by Congressman Oberstar in December 2001 for consideration by the Transportation and Infrastructure Committee, and the Ways and Means Committee of the US Congress. This draft legislation included proposals to:

- Replace the current corporate tax on the operations of qualifying shipping in US international trade with a tonnage tax constructed along the lines of European models,
- Exempt the first \$80,000 of a mariner's overseas income from federal taxes.

The MARAD Administrator, Mr. William Schubert, in a speech delivered on September 17, 2002 stated:

*We need to explore the tonnage tax regime as an alternative to income tax for U.S. vessels in the foreign trade. The tonnage-based system has been successfully implemented in the United Kingdom and could provide a model or framework for this country to follow.*<sup>81</sup>

It would appear that the Bill has been overtaken by the heavy focus on security and did not survive the last session of Congress. While no reintroduction is currently scheduled, there appears to be some expectation that it will be in due course.

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<sup>80</sup> The Transportation Institute, Washington, DC. *Maritime Aid Policies of Select Countries* <http://www.trans-inst.org> accessed May 2003.

<sup>81</sup> Speech to the Maersk Master and Chief Engineer Conference, Portsmouth, Virginia, September 17, 2002.

Other countries have also followed European developments with interest. It was reported that, early in January 2003, the Japanese government sent a team to Europe to study the tonnage tax concept after strong representation by the Japanese Shipowners Association.<sup>82</sup> The Korean Government is also understood to be ready to announce the introduction of a tonnage tax-based system. While India has not yet chosen to commit to a tonnage tax regime, the government is being lobbied strongly to do so and has the concept under active consideration. Pakistan is also advocating a tonnage tax regime,<sup>83</sup> and both New Zealand and Australia are examining the concept.

## **4.6 The United Kingdom—A Case Study**

### **4.6.1 Origins of the recent initiatives**

Virtually all countries that have chosen to adopt measures to reduce fiscal and labour costs for their respective marine transportation industries have engaged in extensive deliberations as to the rationale and justification for its adoption. In this section, one example has been selected to explore more deeply the evolution of current thinking on these measures. The United Kingdom has had a long history of involvement in shipping and provides the home for many of the key shipping institutions. The fact that it has experienced a major and sustained decline in its seagoing fleet since the late sixties and has now taken steps to arrest that decline makes it a suitable candidate for detailed study.

For the UK, current shipping policy had its genesis in the increasing concern expressed throughout the early 1990s about the decline of the UK shipping industry. Pronouncements of particular note include the Labour Party's 1993 paper *Full Steam Ahead: A Maritime Strategy* and reports by the Commons Select Committee on Employment in 1994 and the Committee on Defence in 1997. These reports stressed the importance of the merchant navy's strategic and economic contribution to the UK, and made a number of recommendations directed at greater support for training, measures to reduce employment costs and incentives to stimulate investment.<sup>84</sup>

Other important input flowed from two studies undertaken by the University of Wales<sup>85</sup> and the London Guildhall University.<sup>86</sup> The first study, undertaken in 1996, examined the demand in the shore-based maritime-related sector for people with seagoing experience,

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<sup>82</sup> The Transportation Institute, Washington, DC. *Maritime Aid Policies of Select Countries* <http://www.trans-inst.org> accessed May 2003.

<sup>83</sup> Country Report, Pakistan. Regional Seminar on Liberalization of Maritime Transport Services under WTOGATS, 11-13 February 2002.

<sup>84</sup> UK Department of Environment, Transport and the Regions (1998), *British Shipping Charting a New Course*, December.

<sup>85</sup> University of Wales (1996), *The UK's Requirements for People with Experience of Working at Sea*.

<sup>86</sup> London Guildhall University (1997), *UK Seafarers – An Analysis*.

and forecast that problems would face this sector as a result of a dwindling supply of this source of expertise. The second study, undertaken in 1997, examined the demographics of the present UK seafaring community, and estimated the contraction that would result from an imbalance between those retiring and those entering the workforce. These two studies and their documentation of labour force issues were of interest to industry experts around the globe, and reinforced the growing interest in a new shipping policy in a number of countries.

#### ***4.6.2 The Shipping Working Group Report***

In 1997, largely as a consequence of these various inputs, the government established the Shipping Working Group. This group was chaired by the Department of Environment, Transport and the Regions, and its membership comprised other government departments, representatives from the British Chamber of Shipping, and all the major unions with an interest in shipping. Various experts from government and other related sectors were also drawn upon to provide specialist advice. The Group was tasked to identify actions to:

- enable the maximum economic and environmental benefit to be obtained from shipping,
- reverse the decline in the UK merchant fleet
- increase the employment and training of British seafarers
- encourage shipowners and the wider maritime industry to commit more resources to seafarer training.

The Shipping Working Group submitted its report in March 1998 and made some 37 proposals falling into seven broad categories:

- Funding training
- Facilitating training
- Adding value to British seamen
- Improving the employment environment
- Improving the fiscal environment
- Opening up new opportunities for UK shipping
- More user-friendly operation of the UK Register

The central thrusts of these 37 proposals focused on finding ways to stimulate the provision of more and better qualified seafarers, and the right fiscal and regulatory environment to make the UK an attractive location to do business for both UK and foreign shipowners.

### **4.6.3 The UK White Paper on the Future of Transport**

In July 1998, shortly after the submission of the Working Group Report, the UK government published its *White Paper on the Future of Transport*. While this paper had a multi-modal dimension, it chose to set out four broad aims for an integrated shipping policy:

- To facilitate shipping as an efficient and environmentally friendly means of carrying the country's trade,
- To foster the growth of an efficient UK-owned merchant fleet,
- To promote the employment and training of British seafarers, in order to keep open a wide range of job opportunities for young people and to maintain the supply of skills and experience vital to the economy,
- To encourage UK ship registration, to increase ship owners' identification with the UK, to improve the regulatory control of shipping, and to maintain the availability of assets and personnel that may be needed in time of war.

### **4.6.4 The new UK shipping policy**

The next major step in the evolution of UK shipping policy was the publication of the document *British Shipping – Charting a New Course*. The release of this paper, as a product of close and sustained collaboration between the government, the maritime trade unions, the UK shipping industry, 'maritime London,' the UK ports and other marine-related sectors, can probably be regarded as a defining moment in the turnaround of British shipping fortunes.

Drawing on the thinking described above, the paper set out the UK government's strategy for reviving the shipping industry. It stressed the importance of UK interest and involvement in shipping, not only from an economic perspective, but also in relation to safety and security considerations, and protection of the environment. It recognized that the support that had been provided, and the deregulation initiatives that had been taken to date, had not been effective in reversing the decline of the maritime sector. It declared that the previous government's *de facto* policy position to ignore the industry's strategic and economic importance and to accept the decline as an inevitable consequence of market forces was wrong. The paper took the position that continued acquiescence to the steady erosion of the UK's core maritime capability was not a tenable long-term policy. It concluded that a more interventionist policy, in line with the maritime policies of the European Union, and following the successful initiatives taken by certain European countries, should form the foundation for a new integrated maritime policy. The paper set out a comprehensive strategy in the form of 33 inter-related measures focused on four broad categories: increasing skills, encouraging employment, increasing the UK's attractiveness to shipping enterprises, and gaining safety and environmental benefits.

With regard to increasing maritime skills, the policy advocated a broader role and responsibility for the maritime industry in setting up and promoting training schemes, and in sharing the associated costs. In particular, industry was expected to share in the costs of training and to make trainee berths available on ships. With regard to encouraging employment, the policy committed the government to improving employment provisions for seafarers in legislation and regulations, and to providing enhanced funding for crew relief, improvements in the social security scheme for seafarers, and improved opportunities for career advancement.

With regard to fiscal changes, the policy was still quite cautious. While recognizing the benefits that such measures had achieved elsewhere, the UK government promised only to discuss with industry fiscal options for shipping, including the tonnage tax option. It tied any subsequent agreement on fiscal relief to a matching investment by industry in the development of the UK seafarer skills base. The policy did, however, commit the Maritime and Coast Guard Agency to improving services to British shipping such that growth in the number of merchant vessels flying the UK flag would be encouraged.

It is interesting to note that the UK shipping policy was built upon, and was designed to be directly supportive of, the government's wider economic and industrial aims. These included:

- promoting open and competitive markets at home and internationally
- fostering enterprise and innovation, and the use and advancement of new technology
- encouraging investment, greater productivity and the pursuit of quality
- strengthening the country's international competitiveness and export potential
- promoting safety and environmental quality
- encouraging the development of a skilled and flexible workforce.

The policy also recognized, however, that the peculiar nature and circumstances of the shipping industry gave rise to a need for means to achieve these aims that differed from those that were appropriate for other industrial sectors. This was because the shipping industry was seen to have a number of distinctive features, which, while each individually might not be viewed as unique to shipping, in combination gave rise to a exclusive set of circumstances requiring a specialized, tailored approach. Such features included the fact that the productive capital consisted of discrete and very expensive assets that had no fixed land location, that the industry was exposed to an unusually high degree of globalization, and that this global dimension gave rise to unique freedoms in the employment of labour.

It is important to note that while the UK policy might reasonably be viewed as interventionist, it was not in any way protectionist. Instead it emphasized repeatedly the importance of maintaining international shipping markets that were open and competitive, and ensuring that ports remained open to foreign shipping provided that international standards were met. In this way, shippers could be assured of the necessary choice of services at a cost that did not disadvantage them in relation to their competitors.

In summary, the policy document proposed a number of integrated measures that represented a comprehensive industrial management strategy, designed to build a dynamic maritime industry providing long-term benefits to the United Kingdom. It saw the success of the measures as depending upon a concerted and sustained partnership between British shipowners, the maritime-related industries, the trade unions and the government.

#### **4.6.5 Advancing fiscal reform—Report by Lord Alexander of Weedon QC**

The discussions with industry regarding the merits and issues of fiscal reform, to which the shipping policy document committed, advanced at a rapid pace. In the Budget statement delivered on March 9, 1999, the Chancellor of the Exchequer made the following announcement to launch the comprehensive examination of the tonnage tax concept by Lord Alexander of Weedon:<sup>87</sup>

*The shipping industry has put to me the case for enhanced training incentives and for a lower rate, ring-fenced, tonnage tax. While I am attracted to these options I have to be satisfied that lower tax rates will not become a vehicle for tax avoidance and I am grateful to Lord Alexander of Weedon for agreeing to conduct an independent study of the national and international issues involved.*

The terms of reference for the study were as follows:

*To conduct an independent study of the case for, and the design of, a lower rate ring-fenced tonnage tax and additional enhanced training incentives, for the shipping industry, taking account of the Government's objectives for shipping, and the national and international competitiveness issues involved, concluding as soon as it is practical.*

In his report, Lord Alexander:

- reiterated the challenges facing the UK shipping industry,
- reviewed the existing corporation tax system as it applied to the shipping industry,

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<sup>87</sup> HM Treasury Release (1999), *Independent Inquiry into a Tonnage Tax. A Report by the Lord Alexander of Weedon QC*, July.

- described what a tonnage tax would be and how it would benefit the industry,
- examined the interaction between the UK tonnage tax concept and the European Commission aid guidelines,
- assessed the spillover benefits for related industries,
- proposed and costed an illustrative design for a tonnage tax, including a full detailed design specification and reflecting ring-fencing provisions designed to clearly and effectively limit the scope for avoidance,
- considered the potential implications for competition with other sectors, and
- provided recommendations as to timing of a government decision to adopt a tonnage tax,

With regard to Lord Alexander's views as to the desirability and importance of this initiative, it is perhaps worth quoting his conclusions in full:

*I have obviously not addressed the priority this measure should receive relative to other demands on public finances, whether from other aspects of transport policy or from unrelated Government responsibilities and commitments. This question was quite properly outside my remit since it is, after all, the role of Government to take such decisions. But I believe that the Government's policy for shipping cannot be achieved without creating a tonnage tax regime to ensure a fiscal environment which is, and is perceived to be, user-friendly both in the sense that it is tax-exempt or virtually so and that it offers certainty and clarity. The existing structure is unsatisfactory. It acknowledges the principle of subsidy, provides substantial backing to the industry, yields comparatively little tax, but is not commercially attractive to companies or investors. The DETR, the industry and the trades unions are willing in partnership to attempt to revive the industry and promote skilled employment to benefit seafarers and those who switch from active seafaring to join the valuable shore-based industries. Whilst the economic case alone is not wholly convincing, and the success of the policy in a highly competitive market is far from assured, the future of our shipping industry is now at a critical point. Without attempting the tonnage tax, further decline seems inevitable and may soon reach a point where it will become irreversible. A tide of enthusiasm and commitment is flowing, and if it is allowed to ebb the opportunity may not come again. So I advise acceptance of the proposal with the design which I have indicated.*

The report was completed and submitted to the Transport Select Committee for its consideration, and on May 26, 1999, that committee recommended to the government that a tonnage tax regime be introduced without further delay. This recommendation was accepted by the Chancellor on August 12, and following development of the necessary

clauses for inclusion in the Finance Bill, and the supporting regulations, the tonnage tax legislation was enacted in July 2000. Details of the UK tonnage tax regime can be found in Appendix 4.1.

#### **4.7 Evaluating the Concept, Some Academic and Other Perspectives**

It is, of course, still early in the evolution of this new policy environment to conduct an extensive evaluation as to the degree of its success or failure, but there have been some early opinions expressed as to the merits or otherwise of these new policy directions. Brownrigg<sup>88</sup> stated in 1999, “In my judgment (it) is the right decision—and not a moment too soon.” In a subsequent paper in 2001,<sup>89</sup> he offers comment on the potential downsides, observing that potentially “it could involve some cost to the Exchequer, encourage tax avoidance, or distort competition between shipping and other modes or UK industries” (p. 219). He offers reassurance however, observing that the cost of the tonnage tax was not expected to be large, and that the risk of tax avoidance could be minimized by carefully designed, ring-fenced, legislation. With regard to modal diversion he offers the view that:

*The potential for a modal switch towards shipping following the introduction of a tonnage tax appears to be limited. Moreover, to the extent that freight is switched from road to water, there is likely to be some environmental benefits and a reduction in road congestion. (p. 219)*

There appears to be general agreement that it is not just the fiscal element, but the entire policy package that decides the success or failure of the policy objectives. Brownrigg, in his 1999 speech, also emphasized this point, observing that “the success of a shipping policy—whatever that may encompass—does not stem from its fiscal dimension alone, but from the full package of proposals within the policy.”

Commenting on the fact that today most of the world’s shipping that competes internationally operates in a fiscal climate with little or no tax on profits, Knudsen<sup>90</sup> observed:

*In the maritime countries that stick to conventional taxation of their shipping industry there is serious unrest in the industry. It seems impossible to compete for equity capital against players who need not include tax on*

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<sup>88</sup> Brownrigg, Mark, Director of Policy UK Chamber of Shipping (1999), *Tonnage Tax, The UK’s Choice*, Barbican Centre, September.

<sup>89</sup> Brownrigg, Mark, Geoff Dawe, Mike Mann & Phillip Weston (2001), Developments in UK Shipping: the tonnage tax, *Maritime Policy and Management*, 28, 3, 213-223.

<sup>90</sup> Knudsen, Kristen (1997), The Economics of Zero Taxation of the World Shipping Industry. *Maritime Policy and Management*, 24, 1, 45-54.



*profits as a cost element. The costs of joining or not joining the zero tax club must be considered by governments. (p. 45)*

Knudsen also offered comfort to those who might be concerned that a zero tax environment may cause serious investment distortions. He pointed out (p. 45) that while taxation of profits is the norm in other industries, zero tax is the rule in global shipping. In such circumstances, he observed that zero tax does not systematically lead to super profits, and therefore is no more attractive to investors than other options.

While mainstream support for a tonnage tax regime is clearly strong in Europe, there are limited signals of skepticism in some quarters. It would appear that Italy has yet to be persuaded as to the merits of a tonnage tax regime, and policy turbulence in Norway and Finland suggest differences of view as to what the optimum balance should be. Even in the UK attention has been focused on the tax benefits available to shipowners domiciled abroad but resident in the UK who are not liable for tax on earnings made by companies registered and resident overseas. This provision has been crucial in attracting Greek owners among others to London.<sup>91</sup>

Academic criticism appears generally muted at this moment of time, although Selkou,<sup>92</sup> in an analysis of the UK initiative, concluded the initiative was no more than a subsidy. They presented the argument that, for such a taxation regime to be justified, the case needs to be made that shipping constitutes a special case and that without this support the UK economy would be unduly harmed. They then argued that shipping is not a special case, and that “the UK government should be clear in that it is supporting a taxation regime that is clearly discriminatory and based upon a political rather than a fiscal agenda” (p. 402). While the special case debate is certainly valid and appropriate, it would appear that the views expressed by Selkou are weakened by the absence of any analysis of the European maritime aid guidelines in which the rationale for treating shipping as a special case is set out.

## **4.8 General Conclusions**

What conclusions can be drawn from this chapter? First, it is clear that the shift to a tonnage tax concept is not just a fiscal policy being pursued by one or two developed maritime States to improve their competitive position relative to their developed country neighbours. It is, rather, a significant, wide-ranging initiative that is directed at

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<sup>91</sup> Lloyd's Shipping Economist (2002), London's Taxing Question, *Lloyd's Shipping Economist*, November.

<sup>92</sup> Selkou, Evangelia & Michael Roe (2002), UK Tonnage Tax: Subsidy or Special Case?, *Maritime Policy and Management*, 29, 4, 393-404.

fundamentally reshaping the industrial environment of maritime transport, and reversing the trend towards using open registry shipping

As made clear by Lord Alexander of Weedon, the justification for adopting a tonnage tax regime was not based on economic reasons.<sup>93</sup> In his study he examined the various economic arguments, but remained unconvinced that they were significant. In his conclusions he stated, “the economic case alone is not wholly convincing”. Nevertheless, he finished by strongly recommending acceptance of the proposed tonnage tax concept.

Thus the justification of this fiscal regime is related more to maintenance of expertise and influence than to industry competitiveness. The public interest of the country is deemed to be best served when sufficient maritime knowledge and experience is available to protect and nurture a State’s trading interests, and to ensure that its trading activities are conducted in an efficient, safe and environmentally sensitive manner.

If this public policy is accepted, there is a need to adopt a policy package that includes fiscal relief in the form of a tonnage tax, **as well as other initiatives**. In Chapter 5 we will examine the implications for Canada of such a shipping policy stance.

## **Acknowledgement**

The assistance of Philip (A.J.) Nichols, Dalhousie MBA ’03 candidate, in undertaking the background research for this chapter is much appreciated.

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<sup>93</sup> HM Treasury Release (1999), *Independent Inquiry into a Tonnage Tax. A Report by the Lord Alexander of Weedon QC*, July, para 66.

## **Appendix 4.1 – The Details of the UK Tonnage Tax Regime<sup>94</sup>**

Tonnage Tax is an alternative method of calculating corporation tax profits by reference to the net tonnage of the ship operated. The tonnage tax profit replaces both the tax-adjusted commercial profit/loss on a shipping trade and the chargeable gains/losses made on tonnage tax assets. Other profits of a tonnage tax company are taxable in the normal way. Companies paying corporation tax, which operate qualifying ships that are “strategically and commercially managed in the UK”, can take advantage of the Tonnage Tax regime.

A company is regarded as operating a ship owned by it or chartered to it, if it is:

- Used by the company, or
- Time or voyage chartered-out, or
- Bareboat chartered-out to another UK group member or, in some circumstances, bareboat chartered-out to a third party where there is short-term over-capacity and the charter does not exceed three years. However a single company or group cannot enter the Tonnage Tax regime if more than 75% of its net tonnage is time or voyage chartered-in from outside the group.

A qualifying ship must be seagoing (i.e., certificated for navigation at sea by a competent authority of any country), be of at least 100 gross tons, and be used for:

- Carriage of passengers, or
- Carriage of cargo, or
- Towage, salvage or other marine assistance, or
- Transport in connection with other services of a kind necessarily provided at sea.

The following types of ship are excluded from the Tonnage Tax regime:

- Fishing vessels or factory ships
- Pleasure craft (this does not mean cruise liners, which do qualify)
- Harbour or river ferries
- Offshore installations
- Tankers dedicated to a particular oil field
- Dredgers
- A vessel the main purpose of which is to provide goods or services normally provided on land (e.g., floating hotel or supermarket).

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<sup>94</sup> Material drawn from an explanatory leaflet *TTM0101 Introduction to Tonnage Tax* issued by the Tonnage Tax Unit of the Inland Revenue Department. The formal guidance is contained in *Schedule 22 Tonnage Tax*.

Tonnage tax is computed by calculating the daily profit and multiplying it by the number of days operated. A profit for each day a ship is operated by a company is calculated by reference to the following:

For each complete 100 net tons up to 1,000	£0.60
For each complete 100 net tons from 1,001 to 10,000	£0.45
For each complete 100 net tons from 10,001 to 25,000	£0.30
For each complete 100 net tons above 25,000	£0.15

The daily profit is multiplied by the number of days operated (for a normal year 365). A similar calculation is done for each ship operated. The total for all ships is the company's tonnage tax profit for the accounting period.

The actual profits covered by a tonnage tax profit include those from:

- Core qualifying activities in operating its own ships.
- Other necessary ship-related activities integral to the above.
- Qualifying secondary activities (see below).
- Qualifying incidental activities, not exceeding 0.25% turnover from qualifying core and secondary activities.
- Distributions from overseas shipping companies (which only operate qualifying ships).
- Loan relationship profits and foreign exchange gains, which would otherwise be trading income.
- Gains on disposal of tonnage tax assets.

Qualifying secondary activities are ship-related activities, which are not the direct operation of the company's own ships but have a substantial connection with the company's or a fellow group member's core qualifying activities. These include:

- Support services to fellow group member's ships that would be qualifying core or secondary activities if carried out for own ships.
- Carriage of passengers or cargo beyond the sea-leg of an inclusively priced journey where the transport is bought in from a third party.
- Administration and insurance services.
- Embarkation and disembarkation of passengers.
- Loading and unloading cargo.
- Excursions for passenger where cabin remains available to passenger.
- Normal sales and services to, and entertainment of, passengers.
- Similar services to third parties where use of surplus capacity

- Reciprocal arrangements with third parties.

The UK Inland Revenue also pronounced on how it would interpret ‘strategic and commercial management.’ It announced that it was adopting a common-sense interpretation, taking into account the various strands of activity carried out in the UK, including:

***Strategic***

- Location of headquarters, including senior management staff
- Decision-making of the company board of directors
- Decision-making of operational board
- UK stock exchange listing.

***Commercial***

- Route planning
- Taking bookings for cargo or passengers
- Managing the bunkers, provisioning and victualling requirements
- Personnel management
- Training organization
- Technical management of vessels
- Extent to which foreign offices/branches work under the direction of UK-based personnel
- Support facilities in the UK (e.g., training centre, terminal, etc.).

***Other factors***

- Extent to which work is carried out in UK compared to elsewhere
- Nature and extent of accommodation in UK
- Number of employees in UK
- Residence of key staff, including directors, in the UK
- For an international group, a reasonable balance between UK activities and tonnage in the UK
- Flagging, classing, insuring or financing of vessels in UK.

The Inland Revenue applies special rules to:

- Vessels providing services at sea, where only the transport element is subject to Tonnage Tax.

- Vessels operating in the UK Sector of the North Sea on “offshore activities” (but not supply vessels, tugs, anchor-handlers or tankers, which are subject to normal tonnage tax rules).
- Transitional provisions on capital cost allowances.
- Transitional provisions on chargeable gains.
- Ring-fencing of tonnage profits from non-tonnage tax profits or losses, particularly finance costs.
- Leasing companies owning vessels, which cannot make an election, and to which a special regime of capital allowances applies.
- Corporate partnerships.
- Legal avoidance.

A company enters the tonnage tax regime by electing for an initial period of 10 years. For existing UK operators the election must be made within one year of ‘Royal Assent’ to the *Finance Act*, i.e., by July 27, 2001 (“window of opportunity”). Businesses newly liable to UK tax have one year from commencing the operation of ships in the UK. The regime applies to the accounting period in which election is made, commencing no earlier than January 1, 2000; but entry may be backdated, or postponed for up to two years, in certain circumstances. A tonnage tax election may be renewed for a further 10 years at any time prior to its expiry.

An important element of the tonnage tax regime in the UK is the training commitment requirement. A condition of entering into the tonnage tax regime is that a company or group must enter into a “Training Commitment” with the Department for Transport.

Broadly, this requires:

- The training of one trainee per year for each 15 officers, or
- Payment in lieu to the Maritime Training Trust.
- The trainees must be British or EEA nationals and ordinarily resident in the UK.

## **Appendix 4.2**

### **Selected Websites on Tonnage Tax Regimes Elsewhere**

Anonymous, (2000) “Regulatory Impact Assessment – Tonnage Tax” Inland Revenue Department. [http://www.inlandrevenue.gov.uk/ria/ria\\_tonnage.pdf](http://www.inlandrevenue.gov.uk/ria/ria_tonnage.pdf)

Danish Shipping, “The Danish Tonnage Tax System”  
<http://www.danishshipping.com/com/pdf/TonnageTaxationNotel.pdf>

European Commission, (2002), State Aid No. N572/2002 Spain, Subject: *Introduction of a Tonnage Tax*, Brussels, 5.2.2003, C(2003) 389fin;  
[http://europa.eu.int/comm/secretariat\\_general/sgb/state\\_aids/transport/n572\\_2002.pdf](http://europa.eu.int/comm/secretariat_general/sgb/state_aids/transport/n572_2002.pdf)

European Commission, (2002), State Aid No. N504/2002 Ireland, Subject: *Ireland Introduction of a Tonnage Tax*, Brussels, 11.12.2002, C(2002) 4371fin;  
[http://europa.eu.int/comm/secretariat\\_general/sgb/state\\_aids/transport/n504-02.pdf](http://europa.eu.int/comm/secretariat_general/sgb/state_aids/transport/n504-02.pdf)

European Commission, (2000), State Aid No. N790/1999 United Kingdom, Subject: *UK Tonnage Tax*, Brussels, 02.08.2000, SG (2000) D/105768;  
[http://europa.eu.int/comm/secretariat/sgb/state\\_aids/transport/N790-99.pdf](http://europa.eu.int/comm/secretariat/sgb/state_aids/transport/N790-99.pdf)

Government of Norway, (2003) General information,  
<http://odin.dep.no/nhd/engelsk/publ/brochures/024001-120051/index-dok000-b-n-a.html#nisoppe>

People’s Republic of China, “Provisional Regulations of the People’s Republic of China on Vehicle and Vessel Usage Tax” Issued: 15 September 1986.  
[http://www.novescn.com/vehicle\\_vess\\_usage\\_tax.html](http://www.novescn.com/vehicle_vess_usage_tax.html).

# CHAPTER 5 – THE IMPLICATIONS FOR CANADA

## 5.1 Canada's Current Shipping Policy Position

It is perhaps not totally unreasonable to suggest, indeed it has been suggested by Sletmo (p. 486),<sup>95</sup> that Canada's *de facto* shipping policy is to have no policy at all. It is noteworthy that the National Marine Policy, as set out in Section 4 of the *Canada Marine Act*, only addresses Canadian marine infrastructure and services (ports, the Seaway, ferries and pilotage). Again legislation such as the *Coasting Trade Act* and the *Shipping Conferences Exemption Act* reflect certain specific policy positions taken by Canada, regarding cabotage and competition in liner shipping services respectively, but do not include any explicit policy statement. In addition, significant work has been undertaken on the *Canada Shipping Act*, principally in relation to safety and environmental protection but with no accompanying policy pronouncements in relation to Canada's shipping objectives. From a multi-modal perspective certain policy insights may be drawn from the *Canada Transportation Act*, in which is set out Canada's national transportation policy, but there is no mention of the marine mode in the CTA, and the principal focus is on railways and air services. Contrast this with the 1998 UK *White Paper on the Future of Transport*, which despite also being focused on multimodal considerations, nonetheless includes specific aims for an integrated shipping policy.

While these various elements provide 'snapshots' into Canada's policy thinking on shipping, there is no cohesion or connectivity, and at no time has Canada chosen to articulate a comprehensive policy that sets out its aims and expectations with respect to shipping services. Indeed it may be appropriate to quote Howard Darling's perspective, which, while written nearly 30 years ago, still has relevance today:

*In Canada shipping policy is fragmented between different departments and agencies, each having its own priorities and terms of reference. There exists neither a definition of objectives, a unified administration, an authorization of powers for dealing with the subject matter, nor any continuity of purpose or effort.*<sup>96</sup> (p. vi)

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<sup>95</sup> Sletmo, Gunnar K. (2002), The Rise and Fall of National Shipping Policies, *Handbook of Maritime Economics and Business*.

<sup>96</sup> Darling, Howard (1974), *The Elements of an International Shipping Policy for Canada*.



In the absence of any formal pronouncements as to Canada's shipping policy in the recent past, the summary to Chapter 2 sets out the themes that have emerged in the evolution of Canada's policy deliberations. Included in these themes is recognition that the competitiveness of its international trade hinges on free and fair competition, and that Canada needs to ensure that it has in place, at least as a contingency measure, the necessary minimum diplomatic and legislative tools to act in the event that such competition was threatened. This was the main thrust of the 1980 Transport Canada policy document *A Shipping Policy for Canada*, but was not acted on specifically and was not picked up substantively in the 1985 Task Force report. Post 1985 policy may therefore be considered to have distilled into two essential policy thrusts:

- No steps should be taken by the Canadian government to support the expansion of a Canadian flag fleet if such steps have the potential to adversely affect Canada's trade competitiveness;
- In order for Canada to be able to respond effectively and forcefully to the changing international shipping environment, Canada needs to ensure that it has an appropriate capacity of international shipping expertise to enable it to understand, analyze, and effectively participate in, the business of ocean transportation, and to respond to its trends and issues.

As we have seen from Chapter 4, this policy position has certain parallels with the policy positions adopted by other major maritime nations, particularly in Europe, where an important emphasis was also placed on developing and safeguarding maritime expertise, to be achieved by stimulating ship ownership and management with only incidental encouragement to national registration.

The problem for Canada was that, to its credit, it arrived at its current policy position in the mid-1980s significantly in advance of similar policy positions being adopted by other OECD countries. This presented serious difficulties for Canada since it was then faced with considering quite radical and largely unprecedented fiscal reform for shipping, an industry sector in which it was only playing a modest role. As we have seen in Chapter 3 and will discuss further below, Canada was clearly influenced by the absence of similar initiatives among its OECD partners, and thus felt obliged to choose a less overt fiscal approach than was later adopted by Europe, relying instead on establishment of non-resident international shipping corporations as the means by which taxation could be avoided.

It should also be noted, in reviewing the history of Canada's policy deliberations, that there were certain policy considerations that received little focus at the time but which later attracted more attention in Europe. These included the following:

**(a) Safety and environmental protection**

While national security (with a focus more on military mobility than terrorism at that time) was frequently addressed in the various analyses undertaken, little policy consideration was given to the potential safety and environmental risks, inherent in the expanding use of open registry vessels.

This may perhaps be attributed to the fact that North America did not become fully focused upon the risks of environmental disasters until the *Exxon Valdez* incident off Alaska in 1989. On the other hand, Europe had become much more concerned with this hazard as a result of the *Torrey Canyon* (1967), *Amoco Cadiz* (1979) and subsequently the *Braer* (1993). More recently Europe has become increasingly preoccupied with reducing its exposure to the risks inherent in the operation of poor quality ships around its shores. The sinking of the *Erica* and the *Prestige*, and the extensive damage that their cargoes caused to the coastlines of France and Spain, have served to provide impetus to policy initiatives that serve to lessen the presence of such ships. Again with the heightened concern over terrorism, illegal immigration, piracy and drugs, Europe has viewed increased involvement in ship management by Member States as serving to reduce potential risks in relation to maritime security.

This concern provided the impetus for Europe to pursue enhanced Port State Control (including the Paris Memorandum and the French-led 'Equasis' initiative) as well as for other initiatives such as the International Safety Management (ISM) Code and the new STCW Convention with its associated 'white list'. Canada has, of course, also strongly supported these initiatives, but Europe chose to go further and made safety and environmental protection important goals in its initiatives designed to make EC registered ships competitive with flag of convenience ships. While Canada has strongly supported the former regulatory and information exchange initiatives, it has shown little interest in seeking cost parity with flag of convenience ships as a means of enhancing safety or protecting the environment.

Recognizing the significant safety and environmental issues that still prevail in the shipping industry, Canada's policy position in this matter may well merit review. With issues such as terrorism that involve malign intent, or environmental issues such as ballast water control, antifouling paint, greenhouse gases, pollution risk, single hulled tankers, and so on, there continues to be substantial cause for concern and vigilance. While undoubtedly the enforcement of standards through such mechanisms as Port State Control has gone some way to enhancing safety and environmental standards, there are limitations to the extent to which those standards can be assured through the regulatory process (for example the convention obligation requirement is for only 25% of ships to be PSC inspected). The greater the degree to which Canada's trade is moved in ships owned

and controlled by Canadians, and hence subject to public scrutiny, whether or not the ships are flagged in Canada, the less the risk that trade may be carried in more suspect quality ships. In this respect, this consideration perhaps merits increased attention.

***(b) The importance of seagoing experience***

Another aspect that perhaps received less attention than it should through this period of policy review related to the importance that should be attached to seafaring experience and competencies in implementing the objective of promoting shipping expertise in both the public and private sectors. We have seen that the Canadian policy studies recognized the value of establishing and maintaining shore-based institutions in such fields as ship acquisition and financing, ship management, ship chartering and brokerage, shipping agencies, ship chandlery, freight forwarding, marine insurance, etc. Also important, but not highlighted to quite the same degree was the need for public sector expertise in marine safety, ship inspection, Coast Guard fleet operations, accident investigation, and so on. However, in addressing these needs Canada appears to have paid little attention to the requirement for persons in those institutions to have had substantive sea-going experience. In this respect the importance of sea-going experience, and the challenges that provision of that experience presented, were not highlighted to any great extent in Canada's policy analyses. This again constituted an important difference from the policy perspectives of European countries, where sea training received considerable attention.

***(c) Synergies between international and domestic shipping operations***

Whereas European countries have sought in their policy frameworks, to achieve synergies between international and domestic shipping policies, particularly in providing the possibility for ships predominantly engaged in international trade, to engage in certain coasting trade activities as and when opportunities arise, Canada has chosen, or possibly been compelled as a result of the Canada United States Trade Agreement (CUSTA), to maintain a strong division between these two regimes. At issue, therefore, is whether Canada's policy position to keep a separation between domestic and international shipping activities continues to be appropriate. This issue is both highly complex and vitally important, but beyond the scope of this present study.

Finally, an important message emerging from the intensive policy development work that has been undertaken in Europe is the critical need for close collaboration among all interested parties, both in the development of the policy and its subsequent implementation. The UK Shipping Working Group, with membership drawn from governments, shipowners and unions, is an excellent example, as is the role of the Merchant Navy Training Board in supporting the training and qualification of seafarers. Unfortunately, the low importance that Canada has attached to shipping, coupled with the

recent imposition of cost-recovery charges, has created a strong climate of mistrust in Canada, characterized in particular by the formation of the National Marine and Industrial Coalition, whose principal role is to challenge the government on this cost recovery issue. This negative climate between government and industry is not conducive to progressive collaboration on future shipping policy, and challenges government to establish a neutral forum for more positive collaboration between government and industry.

## 5.2 Implementing the Fiscal Initiative in Canada

Not only were the objectives of Canada's *de facto* policy position quite similar to subsequent positions adopted by European States, the implementation proposals contained in the 1985 Task Force Report (Recommendations 2 and 3) and subsequently pursued by government, had quite similar features, at least in terms of encouraging ship ownership and management, to those later adopted by numerous European countries in the 1990s, and the early years of the new century.

However, as recognized earlier, because Canada was ahead of its OECD colleague states in its thinking at that time, there was a strong reluctance to adopt radical changes in its fiscal approach to shipping. More particularly, a principal concern expressed by the Department of Finance at the time was that Canada was contemplating fiscal adjustments that had no counterparts elsewhere in the OECD, and it was therefore unable to support, **in the form proposed** (a tax-exempt one), the 1985 Task Force proposal regarding the establishment of "International Shipping Corporations."

Instead the Department of Finance proceeded to construct a fiscal solution built around a condition that any such corporations that wished to locate their 'mind and management' in Canada could only avoid taxation in Canada by qualifying as non-residents. As we have seen in Chapter 3, these provisions were first implemented in 1991, and were progressively adjusted through to 1998 as minor points arose that required clarification.

In addition, various marketing efforts, including the establishment of International Maritime Centres were mounted across the country to promote the new regime.

However, as we have seen in Chapter 3, the marketing effort was challenged by the fact that most well established operators had already sought out what they regarded as optimum conditions, and therefore any option needed to be sufficiently attractive to justify the one-time costs as well as the uncertainty associated with a shift to a new legal regime. The factors influencing the success of the various International Maritime Centres in attracting shipping companies may be summarized as follows:

- Vancouver had some notable success in attracting companies, particularly from the US and Asia, the latter attributed in some degree to the approaching change in political regime in Hong Kong. Vancouver had a more established maritime services sector, and was the second largest ship-broking centre in North America after New York.
- In the East, only Montreal at the time had substantial shore-based capacity. However, Montreal faced an uncertain political relationship with the rest of Canada and this hurt its ability to attract inward investment, irrespective of industry. Other locales may not have had the necessary ‘critical mass’ to take advantage of the opportunity.
- The cost of relocating business physical assets and personnel is an expensive one. The quality of life, the cost of living, and many other features of the new location play a strong role in business relocation decisions. Today, Canada compares favourably on many of these dimensions, but did not in the early to mid-1990s.
- For some Canadian companies already structured to operate deep-sea services from offshore (e.g., CP Ships, Canada Steamships Lines), the implementation of the ISC model may have been too late (the latter), or never stood a chance when compared with the structure already in place (the former). It must be remembered that relocation required that key management personnel be prepared to immigrate. For these, it is doubtful any alteration to the existing fiscal climate would prove to be attractive.

### **5.3 Evaluating the Fiscal Options**

The introduction of the ISC concept in Canada and the subsequent, more widespread adoption of a tonnage tax option by a number of other developed countries raises two important questions. Was the ISC initiative a success? And would the tonnage tax option serve Canada better?

#### ***(a) How successful was the ISC initiative?***

There is very little in the way of substantive data available that can shed light on the degree of success of the ISC initiative, and opinions as to its success depend in large part on who one talks to. Some of the original companies have now gone, while some new ones have arrived. In all there are understood to be about 25 shipping groups operating as ISCs in Canada today.<sup>97</sup> As we have seen from Chapter 3, various statistics are offered as to the contribution that these ISCs have made, but these statistics are difficult to verify.

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<sup>97</sup> Sletmo, Gunnar K. (2002), The Rise and Fall of National Shipping Policies, *Handbook of Maritime Economics and Business*, Section 3.1

***(b) Would the tonnage tax option serve Canada better?***

In considering the specific fiscal mechanism, there are arguments for and against whether a tonnage tax regime would serve Canadian shipping interests better. On the one hand it can be argued that a tonnage tax approach is simple to estimate and is less complex in its qualification requirements. There are also no reciprocity requirements with other countries and no need to set up two separate offices. On the other, the ISC ensures full tax avoidance while tonnage tax involves a tax payment, albeit a very modest one.

Perhaps of more pertinence is the fact that we have the ISC tax regime in place, and any move to a tonnage tax regime would require wrenching changes to the Income Tax Act and other related legislation. This is, of course, difficult at any time, but particularly now when taxation adjustments designed to assist the operation of ships in international trade under Canadian management would need to be considered politically at the highest levels. In short, if the only issue was whether there should be adjustments in the nature of the tax regime, then almost certainly the answer would be ‘no.’

This is not however the case. The message emerging from the European policy experience is that the implementation of shipping policy will only be successful if a range of initiatives are adopted **as a package**. As we have seen earlier in Chapter 4, most European States consider that this package needs to include not only fiscal relief on corporation tax, but also income tax relief for seafarers (to offset crewing cost differentials with third flag shipping), the assumption of certain marine training responsibilities, and more user-friendly registration requirements.

Another point that needs to be emphasized is that, under the European regime, it is not only international shipping that is eligible. Both international **and domestic** ship movements are eligible for the tonnage tax regime, as well as activities that extend significantly beyond the transportation of passenger and goods which are the only activities that qualify under the ISC concept. Normally also eligible under a tonnage tax regime are, for example, such activities as towage, salvage, offshore resupply and cruise shipping.

## **5.4 A Look at Canada under a European Style Shipping Policy**

Recognizing the quite fundamental differences that exist in Europe’s approach to shipping policy, it is instructive to examine how Canadian shipping policy and practice might look, were the European model to be adopted in full.

### ***(a) Policy considerations***

A first important, indeed one might say unprecedented, new step for Canada would be the pronouncement of a national shipping policy! Accepting the premise that Canada is adopting a European policy approach, this new Canadian policy would recognize, as many, if not most, of its OECD partners have done, that in order to preserve maritime know-how and skills, and strengthen safety and environmental protection, it must reduce the difference in operating costs between ships that are owned and managed in Canada, whether national or foreign flag, and its third flag competition including flags of convenience. The policy would recognize that this would require fiscal and other mechanisms designed to remove differentials in corporate tax and crew costs.

It is perhaps worth elaborating on this point. As emphasized by Knudsen:<sup>98</sup>

*There is keen competition between the majority of shipping companies that are already zero tax based, and among those many highly competent and efficient operators are to be found. Taxation of profits is the norm in other industries, while zero tax is the rule in global shipping.*

As already pointed out in Section 4.3.1, the Community guidelines on State aid to Maritime Transport make clear that a competitive position in international shipping is only achievable if differences in fiscal costs (both corporation tax and wage related liabilities) are removed. In this respect, the guidelines emphasize that maritime transport presents a special case. If achieving competitiveness requires relief from both corporate and labour related fiscal costs, then both are critical. Thus, providing one without the other will not achieve international competitiveness or the policy objectives that flow from it.

Additionally, in response to the recognized need to encourage the development and maintenance of maritime know-how and expertise, Canada's shipping policy would also recognize that it must provide expanded opportunities for a career in the shipping field, including ensuring the availability of the necessary training and advancement opportunities, both at sea and ashore.

In doing so Canada would also adopt the policy position that circumstances exist justifying shipping being treated as a special case. While this might be seen by some as a radical step for Canada, they should draw comfort from the fact that this policy stance is the norm for the majority of its OECD partners. The justification for this policy position is based on the argument that, unlike virtually all other commercial activities the principal capital assets in shipping are highly mobile, the cost of capital varies little worldwide,

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<sup>98</sup> Knudsen, Kristen (1997), *The Economics of Zero Taxation of the World Shipping Industry*, p. 53

there is little or no difference in technology available, and that therefore corporate taxation and wage related liabilities are the critical factors deciding competitiveness. It should be noted that, in relation to international shipping, Canada has effectively partially assumed this policy position with its adoption of the ISC tax regime.

There would also be the need to recognize the policy benefits of increased synergy between domestic and international movements. More particularly, if Canada were to aspire to achieve this increased synergy, a feature to which much importance is attached in Europe, Canada would need to examine the policy implications of removal the duty requirement for the operation of foreign built, Canadian flag non-duty paid ships in domestic movements.

This is not as radical as it may seem. Indeed Canada, with the US, trails much of the world in reducing cabotage protectionist measures. As Goss<sup>99</sup> points out, the European Union and Mercosur have significantly reduced cabotage restrictions in Europe and South America respectively. He goes on to suggest that “it would be good to see a thorough study of the effects of opening the domestic trades of Canada and the USA to international competition. There can be no doubt that this would lead to lower costs and freight rates, to the great benefit of consumers in both countries.”

If the full policy package was to be implemented, this really should not be problematic, albeit recognizing that some transitional provisions may be required. Canada should perhaps draw comfort from the fact that its tariff requirement for the importation of shipping services is now virtually unique and unprecedented. Whether or not the Canadian coasting trade could be opened to other than Canadian flag vessels would need more careful consideration, but clearly should not be opened to any nation not offering reciprocal arrangements.

It also needs to be recognized in the policy formulation process that, with the advent of the tonnage tax era, the window of opportunity to attract more foreign shipowners under the ISC regime is now closed. The focus of Canada’s efforts must therefore be on stimulating ‘home-grown’ capacity. These efforts will yield only a slow return, but in the long run may offer higher potential in meeting Canada’s policy objectives.

Another policy consideration to which importance is attached in the Canadian policy context is the commitment to modal neutrality, broadly endorsed in a number of recent studies, including the 2001 review of the *Canada Transportation Act* and in the principles set out in the recently released ‘vision’ for Canadian transportation, contained in the document “Straight Ahead”. At issue is whether a deep-sea shipping policy stance, along

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<sup>99</sup> Goss, R.O. (2002), *The Future of Maritime Economics*.



the lines of that being pursued by many of Canada's OECD partners, would somehow be in conflict with the 'modal neutrality' goal.

In addressing this issue, it should be noted that the marine mode received little attention in the "Straight Ahead" exercise, due in no small part to the fact that the *Canada Marine Act* review was ongoing at the time. The report of the CMA review has now been released, and while the focus of this review was principally directed at infrastructure, it may be noted that the Review Panel made a number of observations, including that there was a requirement for the Government of Canada to promote and more fully recognize and integrate the marine transportation industry into the *Canada Transportation Act*."

What form this recognition and integration should take is vitally important but beyond the scope of this study. Suffice it to say that 'modal neutrality', as a fundamental policy objective, appears to be unique to Canada. Rather, as we have seen in numerous references and particularly in the EU guidelines, marine transportation is viewed by many other nations as having a number of special features that argue for it being treated as a special case. In addition, as noted in Section 4.7, at least one analyst has expressed little concern regarding the risk of modal diversion resulting from the fiscal adjustments for the shipping industry, even though such adjustments might be viewed as a departure from the concept of neutrality. Suffice it to say here that the policy choice of many of Canada's OECD partners clearly eschews 'modal neutrality'. It is also probably fair to say that many in the Canadian shipping industry who have been pressing for the articulation of a national shipping policy would share the views of Canada's OECD colleagues. Certainly this significant policy anomaly merits careful analysis.

A final point should perhaps be made with regard to modal neutrality. Concerns have been expressed regarding the impact of any change in fiscal regime on cross-border US traffic, in particular the potential for significant modal shifts. However it should be noted that, being international voyages, any such marine movements are presently legally wide open to foreign flag (including flag of convenience) ships that are effectively benefiting from a zero tax environment. Again, economic feasibility of a large-scale modal shift to short-sea shipping for Canada-US trade has yet to be studied. The fact that foreign flag ships are not presently engaging in such operations would tend to suggest that, even when benefiting from significant fiscal advantages, the circumstances do not offer a business bonanza!

### ***(b) Implementation considerations***

In terms of implementation of this policy, the choice of fiscal mechanism to provide relief from corporate taxation would need review, depending on the nature and scope of the entire policy package. If Canada were to adopt the European policy package in full,

then the extension of qualifying activities to domestic movements could possibly render the ISC mechanism inappropriate. While it would be clearly preferable for there to be one regime for the industry as a whole, the debate about what could be workable needs to take place.

Either way, and as discussed earlier, if Canada aspires to achieve its policy goals above, some form of tax relief similar to that offered in Europe would be required for Canadian seafarer salaries, when working in international trades. Only in this way would it be possible to remove disparities in crew costs and achieve competitive neutrality.

Recognizing the renewed emphasis on sea-going experience as an important element in a number of shore-based activities and industries, Canada would likely need to include matching obligations to provide training billets for Canadian seafarers along the lines of the concept adopted by the UK. Some stimulus may also be required to revamp the fortunes of Canada's marine training colleges, many of which have encountered difficulties due to reduced demand. Finally, a marketing program designed to attract Canadians to a career at sea in a newly invigorated Canadian shipping industry would also be necessary.

As part of the package, Canadian policy would need to promote ways of improving the 'user-friendliness' of its registration process. While Canadian waters present some of the harshest operating conditions in the world, and standards must ensure that those conditions are recognized, Canada can undoubtedly learn from the UK Marine and Coastguard Agency which, with the encouragement of government, has taken significant steps to ease the cost and complexity of UK registration without compromising ship safety.

Finally, none of this can be achieved by government without the strong and sustained support of industry. While this climate of collaboration does not exist at present, the potential offered by adoption of a package of measures along the line of that outlined above should provide the interest and stimulus required to achieve it.

## **5.5 Conclusions and Recommendations**

In conclusion, it is first worth reiterating the point made in Section 1.3 of this study, namely that the aim of the study has not been to make any recommendations with regard to the deep-sea shipping policy regime that Canada should adopt, nor, more specifically, to argue for Canadian registry in any form as a principal goal. Its primary objective has been to offer insights into the new and far-reaching policy directions being pursued by many, if not most, of Canada's OECD partners, and to provide a broad illustration of what Canada's deep-sea shipping policy regime might look like, were it to adopt similar measures.

There have been observations made recently by government representatives, for example at the Transport Canada Conference ‘From Vision to Reality’ held in Toronto in May 2002, that the marine sector has not been receiving its fair share of policy attention. The authors of this report share that view, and hope that some of the observations offered here may serve as a stimulus to new policy activity. Such stimulus we hope comes from pointing out the significant degree to which Canadian shipping policy has departed, and is continuing to depart, from mainstream international policy thinking.

Ultimately the debate as to the merits of adoption of a tonnage tax regime versus maintenance of the ISC concept is inconclusive and depends much more on **policy considerations external to the fiscal issue**. What the discussion presented in this report hopefully highlights is the need for a much broader examination of Canadian shipping policy that looks at shipping activity in Canada as a cohesive package and addresses why, and if so to what degree, Canada should choose to pursue a unique course that, from a number of perspectives, has no parallel in the policies and practices adopted by its OECD partners.

It should be noted that while the study highlights important issues to be addressed in relation to deep-sea shipping policy, it also raises other policy issues that extend significantly beyond the parameters of deep-sea shipping. For example, the study highlights the present lack of cohesion that exists between deep-sea and domestic shipping policies, and the need to evaluate whether maintenance of the current clear division between the two best serves the needs of the Canadian marine transportation system. Moreover, as illustrated in the previous section, were Canada to adopt a deep-sea shipping policy along the lines of many of its OECD counterparts, such a policy would likely conflict with Canada’s current principle of modal neutrality. Again this policy anomaly merits further study and evaluation. In particular, it begs the question as to whether, and if so why, Canada’s over-arching transportation policy framework should dictate a marine transportation policy fundamentally at odds with those of its OECD partners.

As outlined in the introduction, the modest scope of this study has precluded extensive consultation with the wide range of Canadian stakeholders who have an interest in this debate. In this respect, the observations made are more in the form of premises to stimulate further consideration and discussion, rather than a summary of any collective view or consensus. Marine transportation has for too long been the poor relation in Canada’s transportation policy deliberations. Hopefully this report can serve as a call to establish an explicit shipping policy for Canada and so assist in stimulating efforts directed at enabling Canada to find its rightful place in national and international marine transportation.

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