

Analysis of Issues Related to the International Ship Registration System in the Hainan Free Trade Port

ZHANG Liying*, XIAO Yijie**
zlysea@126.com

Abstract: In recent years, the problem of Chinese-funded ships' emigration has not been effectively solved, which has caused some negative impacts, such as hurting China's fiscal revenue, diminishing China's influence as a major shipping country and being detrimental to national security. Although since 2007, China has begun to explore the countermeasures for the return of Chinese-funded ships under Flags of Convenience, and has successively carried out a series of attempts, such as "Tax Exemption Registration System of Special Cases" (encouraging those vessels registered abroad and hanging "flags of convenience" to re-register in China and hang the flag of the PRC), "Yangshan Port of China" Bonded Ship Registry, Tianjin East Port Free Trade Zone and International Ships Registry in China (Shanghai) Pilot Free Trade Zone, but the number of vessels recalled is still very limited. While with the promulgation of the Overall Plan for the Construction of Hainan Free Trade Port in 2020, Hainan provincial authorities decided to leverage the opportunity to deepen opening up. Against this backdrop, the international ship registration system was introduced, which was devised by referring to both the experience and lessons of China Mainland, and those of China Hong Kong and Singapore. A series of institutional reforms and innovations have been carried out in relaxing registration conditions, deducting and exempting taxes and fees, optimizing financing requirements and streamlining registration procedures. Additionally, a batch of initiatives exclusive to Hainan Free Trade Port have been launched, such as the Regulations on the International Ship Registration Procedures for the Hainan Free Trade Port¹, the Circular on Preferential Corporate Income Tax Policy for the Hainan Free Trade Port², the Circular on Preferential Individual Income Tax Policy for High-level and Urgently-needed Talent³ and "Zero Tariff" on Imported Vehicles and Yachts Management Measures (Trial).⁴ At present, the International Ship Registration System in the Hainan Free Trade Port has successfully attracted many Chinese-funded ships under Flags of Convenience to return back for registration. However, due to the immature development of the system, many problems have gradually been exposed in practice, such as the practical implementation of favorable policies, tax base erosion and the supervision of ships. All these need to be further solved and optimized by continuously improving the relevant supporting facilities and legal system in the future.

Keywords: Chinese-funded ships under Flags of Convenience; the Hainan Free Trade Port; international ship registration

* ZHANG Liying, Professor and Doctoral Supervisor from the School of International Law, Director of the Research Center for Maritime and Commercial Law from China University of Political Science and Law; Managing Director of WTO Law Research Society of China Law Society and Chinese Society of International Economic Law; Arbitrator of China Maritime Arbitration Commission. This article is a phased research result of a special project of the National Social Science Foundation: the International Cooperation Framework Mechanism Design of "The Belt and Road Initiative" (Project Approval Number: 18VSI050).

** XIAO Yijie, Master of International Law, China University of Political Science and Law.

1 *The Regulations on the International Ship Registration Procedures for Hainan FTP*, issued by Hainan Maritime Safety Administration of PRC on Nov. 3, 2020.

2 *The Circular on Preferential Corporate Income Tax Policy for Hainan FTP* (No.31, [2020]) jointly released by Department of Finance of Hainan Province and the State Taxation Administration on June 30, 2020.

3 *The Circular on Preferential Individual Income Tax Policy for High-level and Urgently-needed Talent* (No.32, 2020) jointly released by the Department of Finance of Hainan Province and the State Taxation Administration on June 23, 2020.

4 *"Zero Tariff" on Imported Vehicles and Yachts Management Measures (Trial)*, jointly issued by Department of Finance of Hainan Province, the General Administration of Customs and the State Taxation Administration on Dec. 30, 2020.

I. The Imperative of Attracting Chinese-funded Ships under Flags of Convenience to Register in the Hainan Free Trade Port

i. Lacking Supervision of Ships under Flags of Convenience May Easily Lead to Safety Hazards

Currently, 35 countries are recognized as Flag of Convenience (hereinafter referred to as FOC) countries by the International Transport Workers Federation (hereinafter referred to as ITF),¹ and most of them are developing countries². Countries that have adopted open registries mostly use loose ship supervision, preferential tax policies, fewer registration restrictions, and low labor costs to attract foreign ships to register there. The data in 2020 from the UNCTAD³ shows that if the registered tonnage and fleet value are used as the standard, Panama, Liberia, and the Marshall Islands are the top three countries in the world for ship registration. As of January 1, 2020, the ship tonnage of the above three countries is nearly half of the global ship tonnage, which is as high as 42%, and they are all FOC countries identified by the ITF (see Table 1).⁴

- 1 International Transport Workers Federation, which was established in 1896 and is headquartered in London, England. It has resisted flag ships of convenience for many years since its establishment. The main measures are as follows: 1. Forcing the owner of the flag of convenience ship to sign an agreement with the organization to improve the wages and benefits of the crew of the ship; 2. Boycotting the owners of flag of convenience ships that have not signed an alliance to prevent them from loading and unloading goods in ports with branches of the organization.
- 2 International Transport Workers' Federation, *Flags of Convenience* (Nov. 06, 2018), <https://www.itfglobal.org/en/sector/seafarers/flags-of-convenience>.
- 3 UNCTAD, its full name is United Nations Conference on Trade and Development, it is the only intergovernmental body in the United Nations system that deals comprehensively with issues related to development and trade, capital, technology, investment and sustainable development. Every year, it publishes the Review of Maritime Transport according to the global maritime transport situation in that year.
- 4 United Nations Conference on Trade and Development, *Review of Maritime Transport(2020)*, United Nations Publications(Dec, 20, 2020), <https://unctad.org/publications>.

• Antigua and Barbuda 安提瓜和巴布达 (北美洲国家)	• Jamaica 牙买加 (北美洲岛国)
• Bahamas 巴哈马群岛 (拉丁美洲国家)	• Lebanon 黎巴嫩 (亚洲国家)
• Barbados 巴巴多斯 (拉丁美洲国家)	• Liberia 利比里亚 (非洲国家)
• Belize 伯利兹城 (拉丁美洲国家)	• Malta 马耳他 (南欧岛国)
• Bermuda (UK) 百慕大群岛 (北大西洋西部群岛)	• Madeira 马德拉群岛 (大西洋的群岛)
• Bolivia 玻利维亚 (南美洲西部国家)	• Marshall Islands (USA) 马绍尔群岛 (美国)
• Cambodia 柬埔寨 (亚洲国家)	• Mauritius 毛里求斯 (非洲国家)
• Cayman Islands 开曼群岛 (位于拉丁美洲)	• Moldova 摩尔多瓦 (东欧内陆国家)
• Comoros 科摩罗群岛 (非洲国家)	• Mongolia 蒙古
• Cyprus 塞浦路斯 (亚洲国家)	• Myanmar 缅甸
• Equatorial Guinea 赤道几内亚 (非洲国家)	• Netherlands Antilles 荷属安的列斯群岛 (拉丁美洲群岛)
• Faroe Islands (FAS) 法罗群岛 (欧洲国家)	• North Korea 朝鲜
• French International Ship Register (FIS) 法国国际船舶登记处	• Panama 巴拿马 (中美洲国家)
• German International Ship Register (GIS) 德国国际船舶登记处	• Sao Tome and Principe 圣多美和普林西比岛 (非洲国家)
• Georgia 乔治亚州 (美国)	• St Vincent 圣文森特岛 (北美洲国家)
• Gibraltar (UK) 直布罗陀	• Sri Lanka 斯里兰卡 (亚洲国家)
• Honduras 洪都拉斯 (北美洲国家)	• Tonga 汤加 (南太平洋岛国)
	• Vanuatu 瓦努阿图 (西南太平洋岛国)

Table 1 The 35 FOC countries and regions recognized by the ITF in 2018¹

Moreover, according to the statistics of the IMO, nearly 70% of the fleet in the world fly FOC²,

¹ See International Transport Workers' Federation (ITF) official website, <https://www.itfglobal.org/en/sector/seafarers/flags-of-convention>.

² International Maritime Organization: *The Structure and Operations of the Liberian Registry*, Liberian Registry (March 5, 2020), https://wwwcdn.imo.org/localresources/en/OurWork/Legal/Documents/IMLIWMUSYMPOSIUM/9%20Panc%203_Ladas.pdf.

which is a staggering number. However, as the number of FOC continues to increase, the problems caused by the lack of supervision of the registration country have also been exposed. In terms of navigation safety, the FOC states have set low ship registration thresholds and low safety technical requirements, attracting many ships with poor ship conditions to register for naturalization. Such practice pose a potential safety hazard for international navigation¹. With regard to the safety of transactions, FOC ships conceal the identity of the real owner of the ship, which is not conducive to the effective supervision of the FOC states, and then in practice there are often cases of maritime fraud and unsuccessful claims for personal injury in traffic accidents. In the aspect of maritime security, ²FOC ships often become tools for illegal activities such as arms smuggling, concealing money, trafficking in goods and people, and becomes a hotbed of terrorism. In respect of environmental protection³, FOC countries generally lack environmental and ecological protection legislation, and marine pollution and illegal fishing incidents related to FOC ships occur from time to time.⁴

ii. Overseas Registration of Chinese-funded Ships and its Negative Impact

According to the data of the UNCTAD in 2020, the Chinese fleet ranks third in the world with approximately 22.84 million deadweight tons (228,371,455DWT), with a total of 6,125 ships. Among them, the number of Chinese ships (4,569) far exceeds the number of foreign ships (2,300), but in terms of deadweight tonnage, Chinese ships account for only 43.56%, and more than half are foreign ships. This makes the average tonnage of a Chinese ship about 21,000 tons, while the average tonnage of foreign ships owned by China is as high as 56,000 tons, more than twice the tonnage of Chinese vessels⁵. These figures show that ships under Chinese flag, despite their large number, are small in tonnage; although the number of ships flying foreign FOC is small, their tonnage is rather large relatively. Moreover, according to the registration and dead-weight of Chinese ships from 2008 to 2020 (see Table 2), it can be clearly seen that although the proportion of foreign ships has declined, it still remains at more than half, and even has an upward trend since 2015.

Year	Number of vessels	Number of ships flying foreign flag	Dead-weight tonnage of ships flying foreign flag	Dead-weight tonnage of ships flying foreign flag as a percentage of total
2008	3,303	1,403	50,530,684	59.53
2009	3,499	1,555	55,594,490	59.91
2010	3,633	1,609	63,426,314	61.00
2011	3,629	1,569	72,285,422	58.29
2012	3,651	1,607	61,762,042	57.20
2013	5,313	2,648	123,142,883	64.79
2014	5,406	--	126,928,000	63.00
2015	4,966	1,996	83,746,441	53.15
2016	4,960	1,915	84,778,140	53.36
2017	5,206	--	89,282,495	53.97
2018	5,512	1,956	99,455,000	54.30
2019	6,125	2,138	115,307,656	55.92
2020	6,869	2,300	128,892,849	56.44

- 1 YUAN Xue & WANG Qiannan, *Breakthroughs and Countermeasures for the Return of Chinese-funded Flag-of-convenience Ships, Cognition and Practice*, Issue 3, 2015, p. 56.
- 2 Hamad, *Flag of Convenience Practice, A Threat to Maritime Safety and Security*, IJRDO-Journal of Social Science and Humanities Research, Vol.1:1, p. 207-230 (2016).
- 3 Yale University, *Crimes Under Flag of Convenience*, Yale Global Online (Dec. 22, 2020), <https://yaleglobal.yale.edu/content/crimes-under-flags-convenience>.
- 4 Dempsey, P. S. & Helling L. L., Oil pollution by ocean vessels - an environmental tragedy, *the legal regime of flags of convenience, multilateral conventions, and coastal states*, Denver J. Int. Law Policy, Vol: 10:1, p. 3-4 (2016).
- 5 United Nations Conference on Trade and Development, *Review of Maritime Transport(2020)*, United Nations Publications(Dec. 20, 2020), <https://unctad.org/publications>.

Table 2 Ship Registration and Dead-weight in China from 2008 to 2020¹

The problem of numerous Chinese-funded ships switching to open registries, if not addressed effectively, would ultimately exert adverse effects on China's finance, shipping, national defense and national image.

1. Leading to a Partial Loss of Our Fiscal Revenue

A large number of Chinese-funded ships registered in foreign countries are not under the direct control of our government as they are not registered in China, resulting in the loss of taxes and fees that should be paid to our country. Subsequently, in April 2017, ²China ceased to levy ship registration fees, so that the registration fee lost due to the transfer of ship registration before 2017 will no longer be regarded as part of the loss of our country's fiscal revenue. However, although the ship registration fees have been canceled, ship tonnage tax, vehicle and vessel tax, stamp duty, etc. are still taxes and fees that must be paid after ship registration. In 2020, the average tonnage of Chinese vessels registered as foreign nationality was about 56,000 tons³. According to China's vehicle and vessel tax levy standards⁴, for every additional Chinese ship registered in a foreign country, China's fiscal revenue will lose nearly 168,000-336,000 yuan.

2. Weakening the Status and Image of China as a Major Shipping Country

The tonnage of a country's merchant fleet flying its national flag is a key factor in measuring a country's shipping status⁵. However, many high-quality national vessels with large tonnage and small age are registered overseas, which has accelerated the aging of our fleet. Moreover, the decline of the gross tonnage of the Chinese shipping fleet will hinder the continuous expansion of the scale of naturalization of the China Classification Society, which is not conducive to the promotion of the status of the China Classification Society. All the above problems will become obstacles to the transformation of China into a shipping power and weaken the status.

3. Not Conducive to China's National Security

According to Table 2, it can be seen that nearly 1/3 of Chinese ships engaged in international navigation in 2020 have been registered as foreign nationality. The tonnage of the remaining 2/3 ships flying the the flag of the PRC is less than 1/2 of the gross deadweight tonnage of Chinese ships. The current international situation is in a state of tension. In the event of war or local disputes, a large number of Chinese ships moving overseas will not be used by the Chinese government. As far as the current situation is concerned, China's demand for ships sailing internationally is on the rise. Whether our army participates in international peacekeeping activities, or the construction of overseas logistics support bases or ocean support transportation, a large number of international ships are needed. However, it is difficult for national defense mobilization departments at all levels to grasp the actual situation of flag of convenience ships, which makes it difficult to quickly dispatch Chinese-funded FOC ships in wartime or emergency situations. ⁶

iii. China's Previous Attempts to Attract Chinese-funded FOC Ships to Return to China for

1 Data source: 13 copies of Review of Maritime Transport published by UNCTAD from 2008 to 2020.

2 Notice on the Policy on Cleaning and Regulating a Batch of Administrative Fees and Charges (No. 20 [2017]): Starting from zero o'clock on April 1, 2017, 41 administrative fees set up at the central level will be canceled or suspended, including:... ship registration fees, inspection fees for ships and marine products and facilities...

3 United Nations Conference on Trade and Development, Review of Maritime Transport (2020), United Nations Publications(Dec, 20, 2020), <https://unctad.org/publications>.

4 Travel Tax Law of the People's Republic of China (No.191 [2019]): The specific applicable tax amount for ships shall be determined by the State Council within the tax amount range specified in Travel Tax Items and TaxAmount Table attached to this Law. The net tonnage of motor ships is taxed per ton from 3 yuan to 6 yuan.

5 YE Yanglian, Research on the Legal System of Ship Registration, Ph.D. Thesis of East China University of Political Science and Law in 2013, p. 35-37.

6 LIU Baoxin& LIU Jiasheng, A Study on National Defense Mobilization of Chinese-funded Flags of Convenience Ships, Journal of Military Communications College, Vol. 20, No. 1, p. 15-18,41 (2018).

Registration Have not Achieved Good Results

In June 2007, the Ministry of Transport issued an Announcement:¹ from July 1, 2007 to June 30, 2009, the Tax Exemption Registration System of Special Cases will be implemented. According to the Regulations on the Tax Exemption Registration System of Special Cases, if a Chinese-funded ship acquires nationality abroad and meets the conditions such as ship age before the end of 2005, it will be able to enjoy the policy.² During this period, four batches of 55 Chinese-funded FOC ships registered in China. In order to attract more Chinese-funded FOC ships,³ the Ministry of Transport extended the implementation period of this policy in 2009 and 2011 respectively, and finally the Tax Exemption Registration System of Special Cases was extended to December 31, 2015. ⁴However, only 16 Chinese-funded FOC ships returned during the extended period, the policy has far less effect than expected.⁵

In 2016⁶, the Ministry of Transport issued an announcement that would extend the policy of exempting Chinese-funded FOC ships from customs duties and import value-added tax until September 1, 2019. Compared with the previous policies, the adjusted and improved preferential tax policies no longer require all kinds of imported ships to comply with the relevant and previous regulations on the import of ships. From 2016 to 2019, a total of 80 Chinese-funded FOC ships returned to China for registration. ⁷

In order to further attract the return of Chinese-funded FOC ships, China began to explore international ship registration systems. The Registration Policy of Bonded Ships in the Pilot Project of “Yangshan Port of China” was carried out in 2011; Tianjin East Port Free Trade Zone took the lead in implementing the International Ship Registration System nationwide in 2013; The Ministry of Transport approved Shanghai’s Pilot Program for the International Ship Registration System in 2014⁸, relaxing restrictions on ship registration, foreign crew allocation, etc., allowing registered entities to have a foreign investment ratio of more than 50%, but the effect was still poor. Tianjin East Port Free Trade Zone has attracted only 12 Chinese-funded FOC ships to return to China for registration since 2013. ⁹ The failure is principally attributable to China’s strict registration conditions and high tax rates; at the same time, the relatively weak financing environment and cumbersome registration procedures are also important reasons.

Therefore, in order to reduce the potential safety hazards brought by FOC ships and alleviate the adverse effects of overseas migration of Chinese-funded ships on China, the Hainan Free Trade Port

- 1 Announcement on the Implementation of Tax Exemption Registration Policy for Special Cases of Chinese-funded International Shipping Vessels, (No. 18, [2007]) issued by the Ministry of Communications Water Transport Bureau on June 13, 2007.
- 2 The Announcement on the Implementation of Tax Exemption Registration Policy for Special Cases of Chinese-funded International Shipping Vessels, No.18, [2007], clearly requires that Chinese-funded ships declared for import and registered during the period from July 1, 2007 to June 30, 2009 shall be exempted from customs duties and import value-added tax if they meet the following conditions: (1) They have been registered overseas before December 31, 2005;(2)Range of ship age: 1. Oil tankers (including asphalt tankers) and bulk chemical tankers with a ship age of 4-12 years; 2. Bulk carriers and ore carriers with a ship age of 6-18 years; (3) Container ships, general cargo ships, multi-purpose ships, bulk cement ships, etc. with a ship age of 9-20 years.
- 3 See the website of the Ministry of Transport of the People’s Republic of China, <http://www.mot.gov.cn/fenixigongbao/>, visited on Dec. 23, 2020.
- 4 YUAN Xue& WANG Qiannan, The Dilemma Breakthrough and Countermeasures for the Return of Chinese-funded FOC Ships. *Cognition and Practice*, No. 3, 2015, p. 58.
- 5 See the website of the Ministry of Transport of the People’s Republic of China, <http://www.mot.gov.cn/fenixigongbao/>, visited on Dec. 23, 2020.
- 6 Announcement on Implementing the Import Tax Policy for Registration of Chinese-funded Flag of Convenience Ships Returning to China, No. 42, [2016] jointly issued by the Ministry of Finance of the PRC, the General Administration of Customs of the PRC and the State Taxation Administration of the PRC on 31 August 2016.
- 7 See the website of the Ministry of Transport of the Peoples Republic of China, <http://www.mot.gov.cn/fenixigongbao/>, visited on December 23, 2020.
- 8 Pilot Program for International Ship Registration System in China (Shanghai) Pilot Free Trade Zone, which was released by Shanghai Maritime Safety Administration on January 21, 2014.
- 9 See the website of the Ministry of Transport of the People’s Republic of China, <http://www.mot.gov.cn/fenixigongbao/>, visited on December 23, 2020.

(hereinafter referred to as Hainan FTP) decided to establish the registry port of “Yangpu Port of China” and carry out international ship registration business¹. By drawing lessons from the past and learning from the experience of well-known ports at home and abroad, Hainan FTP has carried out a series of institutional improvements and innovations in its international ship registration system (hereinafter referred to as the Registration System), hoping to have better results in attracting the return of Chinese-funded FOC ships.

II. Relevant Policies and Legal Provisions on the Registration System in Hainan FTP

i. Definition of Registration System international ship registration system

At present, the ship registration systems of all countries in the world can be divided into three types: strict ship registration system, open ship registration system and international ship registration system. Among them, neither will the international ship registration system imposes strict restrictions on the nationality of ship owners, crew allocation, capital contribution ratio, technical safety, etc. like² the strict ship registration system, nor will it be like the open ship registration system, relax the registration and supervision of ships too easily, in other words, the international ship registration system is a kind of new registration system between the two.³

In the past, China implemented a strict ship registration system. It was not until the establishment of Tianjin East Port Free Trade Zone in 2013 and Shanghai Pilot Free Trade Zone in 2014 that it began to try the international ship registration system regionally, so that ships coming to register could enjoy a series of preferential treatment on taxation and registration.

While this time, Hainan FTP took over the baton of the construction of international ship system in Tianjin East Port Free Trade Zone and Shanghai Pilot Free Trade Zone, and carried out a new round of exploration and pilot on the implementation of this system.

ii. Analysis of the Registration System in Hainan FTP

As of January 1, 2020, the five economies with the largest number of ships are Greece, Japan, China, Singapore and Hong Kong China, accounting for more than 50% of the world's gross tonnage.⁴ Among them, more than 70% of the fleets (by tonnage) are registered as foreign nationality, and only Singapore and Hong Kong China keep the proportion of foreign nationality of ships less than 50%, which are 41.32% and 26.31% respectively.⁵ A comparison of those figures reveals that Singapore and Hong Kong China are quite effective in controlling the emigration of ship nationality. The key reason lies in the international ship system of combining leniency with strictness, which can not only ensure the number of registered ships through a series of preferential policies, but also guarantee the quality of registered ships by the strict supervision imposed. Therefore, both the Hong Kong China flag and the Singapore flag enjoy a very good reputation in the world. In the design process of the international ship registration system, Hainan FTP also mainly benchmarked the relevant regulations of Singapore and Hong Kong China and made important adjustments and innovations in many aspects.

1. Relaxation of Registration Conditions

(1) Abolishing the Restriction on Foreign Shareholding Ratio of Ship Registration Entities

In 2018, the Ministry of Transport proposed to cancel the restriction that the ratio of foreign shares

1 The Overall Plan for the Construction of China (Hainan) Free Trade Port, issued by the Central Committee of the Communist Party of China and the State Council on June 4, 2020.

2 WANG Shumin & YANG Xin & LI Ruikang, Research on Legal Issues of “Implementing International Ship Registry” in Shanghai Pilot Free Trade Zone, Research on China's Maritime Law, Volume 26, No. 2, 2015, p. 103.

3 YUAN Xue & WANG Qiannan, The dilemma breakthrough and countermeasures for the return of Chinese-funded FOC ships, Cognition and Practice, No. 3, 2015, p. 58.

4 United Nations Conference on Trade and Development, Review of Maritime Transport (2020), United Nations Publications (Dec, 20, 2020), <https://unctad.org/publications>.

5 United Nations Conference on Trade and Development, Review of Maritime Transport (2020), United Nations Publications (Dec, 20, 2020), <https://unctad.org/publications>.

should not exceed 50% for international shipping agencies registered in Hainan. ¹Two overall plans in October of the same year and June 2020 respectively also reiterated the policy requirement of “canceling the restriction on the ratio of foreign shares of ship registration entities”. ²

For a long time, China has strictly required Chinese investors to contribute at least 50% ³of their capital among ship registration entities. Whether it is the bonded ship registration policy of “Yangshan Port of China” piloted in 2011, or the international ship registration system of Tianjin East Port Free Trade Zone in 2013⁴, all strictly implement this regulation. Although Shanghai Pilot Free Trade Zone allowed the proportion of foreign investment to be higher than 50%,⁵ it has never given up the restriction on the share ratio of foreign capital. However, Hainan FTP directly canceled the restriction on the ratio of foreign shares of ship registration subjects, which is undoubtedly an important breakthrough against the previous strict regulations. This measure is not only conducive to the return of Chinese-funded FOC ships, but also conducive to attracting ships mainly invested by foreign investors to register in Yangpu Port, Hainan.

(2) Relaxation of Restrictions on Classification Societies

According to China’s Regulations on Inspection of Ships and Offshore Facilities in 2019 (hereinafter referred to as the Inspection Regulations), ships registered in China can only be inspected by China Classification Society if they want to engage in international navigation⁶, which is substantially different from Singapore and Hong Kong China. In addition to Singapore’s own classification society, Singapore also recognizes 7 foreign classification societies to carry out ship classification inspection⁷, Hong Kong China has 9 foreign ones⁸. In contrast, Panama and Liberia have recognized more classification societies, with 29 and 10 respectively⁹. In fact, the strict restrictions on the qualification of inspection agencies in China will reduce the efficiency of ship registration to a certain extent, and further undermine the shipowners’ intention to register their ships in China.

Therefore, in order to absorb useful international experience, in 2018, the Ministry of Transport

- 1 Implementation Plan of the Ministry of Transport for Implementing the Guiding Opinions of the CPC Central Committee and the State Council on Supporting Hainan to Comprehensively Deepen Reform and Opening up, issued by the Ministry of Transport on July 25, 2018.
- 2 The two overall plans specifically refer to: China (Hainan) Pilot Free Trade Zone Overall Plan (2018) and the Overall Plan of Construction for China (Hainan) Free Trade Port (2020).
- 3 Article 2, paragraph 2, of the State Council’s the Ship Registration Regulations of the People’s Republic of China (2014) stipulates: Ships of enterprise legal persons established in accordance with the laws of the People’s Republic of China whose main business offices are within the territory of the People’s Republic of China. However, if foreign investors contribute to the registered capital of the legal person, the amount of Chinese investors’ contribution shall not be less than 50%.
- 4 The Pilot Scheme for Innovation of International Ship Registration System in Tianjin East Port Free Trade Zone (Water Transport Bureau of the Ministry of Transport [2011]) clearly requires: ships of enterprise legal persons established in Tianjin East Port Free Trade Zone according to the laws of the People’s Republic of China. If foreign investors contribute to the registered capital of the legal person, the amount of Chinese investors’ contribution shall not be less than 50% (if overseas Chinese-funded enterprises recognized by the state-owned assets supervision and administration department return to invest, their contribution may be taken as the amount of Chinese contribution).
- 5 The Pilot Scheme for International Ship Registration System in China (Shanghai) Pilot Free Trade Zone (Ministry of Transport [2014]) explicitly requires: ships of enterprise legal persons established in Shanghai Pilot Free Trade Zone according to the laws of the People’s Republic of China. If there is foreign investment in the registered capital of the legal person, the proportion of foreign investment may be higher than 50%.
- 6 Article 13, paragraph 1, of the State Council’s Regulations on the Inspection of Ships and Offshore Installations of the People’s Republic of China (2019) stipulates that the following Chinese ships must apply to China Classification Society for classification inspection: (1) Ships engaged in international navigation; ...
- 7 FENG Junxin, Comparative Study on Ship Registration System, Master’s Thesis, Ocean University of China, 2009, p. 32.
- 8 Hong Kong, China only recognizes 9 of the 10 members of the International Federation of Classification Societies: American Bureau of Shipping (ABS); Bureau Veritas (BV); China Classification Society (CCS); Det Norske Veritas (DNV); Germanischer Lloyd (GL); Korea Classification Society (KR); Lloyd’s Register of Shipping (LR); Japan Classification Society (NK); Registro Italiano Navale (RINA), and the Russian Classification Society has not yet been recognized.
- 9 Tobin & Harry, The Flag of Convenience, Publish America press, 2007, p. 34.

explicitly encouraged the relaxation of classification society restrictions¹. On June 28, 2020, the State Council formally recognized the status of a foreign ship inspection agency, allowing ships with Chinese nationality registered in the China (Hainan) Pilot Free Trade Zone to conduct ship classification inspections by foreign ship inspection agencies instead of complying with the regulations in the Inspection Regulations that Chinese ships must apply to the China Classification Society for classification inspection.²

2. Tax Reduction and Exemption

For a long time, too many taxes and too high tax rates have been the key reasons for the overseas migration of Chinese ships (see Table 3). Moreover, compared with the fiscal and taxation systems of free trade ports at home and abroad, it basically presents the following three characteristics: First, there are few taxes; Second, preferential tax rates; Third, there are various ways of tax incentives³. Hainan FTP has also introduced various favorable policies in terms of fiscal and taxation system, and implemented “zero tariff, low tax rate and simple tax system” to the end.

Hong Kong, China	Singapore	China Mainland
Annual tonnage tax on ships	Annual tonnage tax on ships	Tonnage tax on ships
Corporate income tax (16.5%)	Corporate income tax (17%)	Corporate income tax (25%)
		Import and export tariff
		Added-value tax on import
		Vehicle and vessel tax
		Added-value tax
		Stamp tax

Table 3 Comparison of Fiscal and Tax Systems in Hong Kong China, Singapore and China Mainland⁴

(1) Zero Tariff on Raw and Auxiliary Materials

According to the general regulations of our country, the total taxes and charges paid by shipbuilding enterprises on ship imports are 27.53%⁵ of the ship price (including 9% import tariff and 17% value-added tax). In contrast, Singapore and Hong Kong China are directly exempt from this tax. In order to reduce the tax burden on Chinese ships and attract the return of Chinese-funded FOC ships, China implemented the Tax Exemption Registration System of Special Cases in 2007, exempting

- 1 The Implementation Plan of the Ministry of Transport for Implementing the Guiding Opinions of the CPC Central Committee and the State Council on Supporting Hainan to Deepen Reform and Opening up in an All-Round Way ([2018]): Based on the principle of reciprocity, the inspection business of Chinese international sailing ships registered in Hainan Pilot Free Trade Zone will be gradually liberalized.
- 2 Notice of the State Council on Temporary Adjustment and Implementation of Relevant Administrative Regulations in China (Hainan) Pilot Free Trade Zone, No.88, [2020] issued on June 18, 2020.
- 3 LI Heng, Research Trends on Building a New Fiscal and Tax Policy System in Hainan FTP, in *China Business Theory*, No. 22, 2020, p. 18-21 and 35.
- 4 Data Source: See Yuhui Zhou, Comparison of Ship Registration and Operating Taxes of Shipping Enterprises in China and Singapore, *Water Transport Management*, Volume 39, No. 3, 2017: p. 17-20 and 28.
- 5 Making Chinese-funded Flag of Convenience Ships More Pleasant to Go Home, *China Communications News*, March 22, 2017, p. 7.

Chinese ships from customs duties and import value-added tax if they meet the conditions.¹ Hainan FTP not only continued this tax preference, but also issued a Notice on the “Zero Tariff Policy for Yachts” on December 25, 2020,² and the Administrative Measures (Trial)³ on December 30 in the same year. Before the whole island of Hainan becomes a bonded area, enterprises registered in Hainan FTP and engaged in transportation and tourism, when importing ships used for transportation and tourism, can enjoy the preferential treatment of exemption from import duties, import value-added tax and consumption tax⁴. After the customs is sealed, goods subject to “zero tariff” can also be exempted from routine customs supervision. However, because the ship is built overseas, the materials and equipment needed for shipbuilding have to be imported, and these materials and spare parts are still subject to pay 27.53% tax at the time of import⁵. Therefore even though the Ministry of Transport extended the implementation period of the Tax Exemption Registration System of Special Cases in 2009 and 2011 respectively, the number of Chinese FOC finally re-registered in China is still very limited.

Aware of the reality that the tax burden remained heavy in the past, the Department of Finance of Hainan Province and two other departments jointly issued “the Notice on “Zero Tariff” on Raw and Auxiliary Materials in 2020, announced that it will implement the “zero tariff” policy in Hainan FTP, and implement positive list management. The contents of the list will be dynamically adjusted by the Ministry of Finance in conjunction with relevant departments according to the actual situation in Hainan. This means that after international ships are registered in China, not only can the ships themselves be exempted from tax, but also can shipbuilding parts enjoy corresponding tax incentives. At the same time, the zero tariff policy for raw and auxiliary materials also stipulates that ships (including related parts) operated by shipping companies registered in Hainan with independent legal personality and with ports in Hainan Province as their ports of registry can also enjoy the zero tariff policy.

(2) Reduction and Exemption of Corporate Income Tax

Hainan FTP issued preferential policies for corporate income tax on June 30, 2020⁷: for

- 1 Ships enjoying the Tax Exemption Registration Policy for Special Cases of Chinese-funded International Shipping should meet three conditions: First, they must be Chinese-funded international shipping ships. The Ship Registration Regulations of the People’s Republic of China stipulates that the proportion of Chinese capital contribution in registered ships shall not be less than 50%. Second, the age of the ship must meet certain requirements. Specifically: (1) It has been registered overseas before December 31, 2005; (2) Range of ship age (taking July 1, 2007 as the deadline for calculating ship age): oil tankers (including asphalt tankers) and bulk chemical tankers with a ship age of 4-12 years; Bulk carriers and ore carriers with a ship age of 6-18 years; Container ships, general cargo ships, multi-purpose ships, bulk cement ships, etc. with a ship age of 9-20 years. Three, special tax-free ships must comply with the relevant provisions of the Regulations of the People’s Republic of China on the Inspection of Ships and Offshore Facilities, obtain a statutory inspection certificate, go through the classification procedures with China Classification Society, and meet the conditions for safe navigation.
- 2 Notice on the “Zero Tariff Policy” for Transportation and Yachts in Hainan FTP, No. 54, [2020] issued on December 25, 2020.
- 3 Administrative Measures for “Zero Tariff” on Imported Vehicles and Yachts in Hainan FTP (Trial), issued by the Ministry of Finance, the General Administration of Customs and the State Taxation Administration on December 30, 2020.
- 4 Notice on the “Zero Tariff” Policy for Transportation and Yachts in Hainan FTP (No. 54 [2020]) clearly requires: First, before the whole island is closed, enterprises registered in Hainan FTP with independent legal person status and engaged in transportation and tourism (aviation enterprises must take Hainan FTP as the main operating base) are exempted from import duties, import value-added tax and consumption tax for ships, aircraft, vehicles and other operational vehicles and yachts used for transportation and tourism. The list of enterprises that meet the conditions for enjoying the policy shall be jointly determined and dynamically adjusted by The competent departments of transportation, cultural tourism, market supervision, maritime and civil aviation administration of Hainan Province, together with Hainan Provincial Department of Finance, Haikou Customs and Hainan Provincial Taxation Bureau of the State Administration of Taxation with reference to the items of transportation and tourism-related industries in the Catalogue of Encouraged Industries of Hainan FTP.
- 5 ZHANG Yuanbo& ZHANG Cheng, Some Thoughts on Reforming and Perfecting China’s Ship Tonnage Tax System, Journal of Harbin Institute of Technology (Social Science Edition), Vol. 17, No. 2, 2015, p. 130-134.
- 6 Notice on the Policy of “Zero Tariff” on Raw and Auxiliary Materials in Hainan FTP, No. 42, [2020] issued on November 12, 2020.
- 7 The Circular on Preferential Corporate Income Tax Policy for Hainan FTP clarifies: The term “practical operation” means the management body of an enterprise set up in Hainan FTP that actually performs management functions and carries out substantial and comprehensive management and control over production and operation, personnel, accounting and property

encouraged industries, enterprises that are registered in Hainan FTP and have a practical operational record are entitled to a reduced corporate tax rate of 15%¹. Are shipping companies engaged in international transportation able to enjoy this concession? The answer, the authors believe, is positive. The Catalogue of Encouraged Industries in Hainan FTP includes the Catalogue for the Guidance of Industrial Structure Adjustment (2019 Edition), the Catalogue of Industries Encouraging Foreign Investment (2019 Edition) and the Catalogue of Newly Encouraged Industries in Hainan FTP². Among them, the Catalogue for the Guidance of Industrial Structure Adjustment has the independent category of ships included in the category of encouraged industries³. Although the Catalogue of Newly Encouraged Industries in Hainan FTP has not been officially released, the draft for soliciting opinions issued by the National Development and Reform Commission on September 1 this year has added more than 100 new industries, including ship supporting facilities and services among the innovative industries, such as enterprises engaged in ship registration, management, repair, maintenance and bonded oil refilling services, all of which can enjoy a 15% corporate income tax rate.⁴

According to relevant statistics, the current corporate income tax in China Mainland is calculated at 25%, while that in Hong Kong China and Singapore is calculated at 16.5% and 17% respectively. Although some enterprises in the Mainland also pay income tax at 15%, Hainan's corporate income tax policy has a wider scope of application and can enjoy direct tax exemption⁵. Therefore, if this policy can be finally implemented, not only can shipping enterprises registered in China enjoy tax reduction and exemption, but also can surrounding supporting facilities and services obtain maximum tax concessions, which is conducive to further reducing the operating costs of Chinese-funded FOC ships after returning home and improving the attractiveness and competitiveness of ship registration in Yangpu Port, Hainan.

(3) Individual Income Tax Deductions and Exemptions

Vessels' crew has always been a high-risk profession, for which the salaries are relatively high. To protect the right of vessels' crew, many countries will deduct or exempt their individual income tax. For example, in Singapore and Sweden, the income tax of vessels' crew gets totally exempted; in Japan, the income tax will be only levied on their income from activities on land. As for the subsidies provided during the sail, the tax will be exempted⁶; in the UK, the individual income tax will be exempted for those vessels' crew who sail abroad for over 183 days in a year; in Netherlands, 38% of the individual income tax will be deducted for vessels' crew from the shipping companies with permanent organizations in Netherlands.⁷ However, in China, there is no such preferential policies for vessels' crew, which leads that many Chinese-funded vessels will choose to register in the FOC countries to relieve their tax burden. In 2020, Hainan government released official documents of central government, which said that high-end talents and highly-demanded talents employed in Hainan FTP are entitled to the individual income tax rate of 15%.⁸ And qualified crew members (including vessels' crew and fishing vessels' crew), vessel management talents, vessel service talents are all qualified as

affairs.

- 1 The Circular on Preferential Corporate Income Tax Policy for Hainan FTP clarifies: The term "enterprises in encouraged industries" refers to enterprises whose main business are described and included in the catalogue of encouraged industry for Hainan FTP, and major business income accounts for more than 60% of the total income.
- 2 ZHOU Meifeng, Analysis of Enterprise Income Tax Policy in Hainan FTP, *China Taxation*, No. 8, 2020, p. 34-35.
- 3 The Catalogue for the Guidance of Industrial Structure Adjustment (2019 Edition), No.29 [2019] of the National Development and Reform Commission, issued on October 30, 2019.
- 4 The Catalogue of Encouraged Industries in Hainan FTP (2020 Edition, Draft for Soliciting Opinions), released by the National Development and Reform Commission of the People's Republic of China on September 1, 2020.
- 5 JIANG Yuesheng, Thoughts on International Tax Policy of Hainan FTP, published in Economic Observation Network, August 15, 2020, <http://www.eeo.com.cn/2020/0815/399830.shtml>.
- 6 ZHAO Shubo, Completing the Taxation System of Ocean Transportation Industry in China with the Reference of International Practice, *Taxation Research*, Vol. 4, 2012, p. 81. (in Chinese)
- 7 GAO Yanming, the Advice on exempting the Individual Income Tax of International Vessels' Crew, http://www.eeworldship.com/html/2016/person_character_0304/112599.htm, March 4, 2016. (in Chinese)
- 8 The Central Committee of the Communist Party of China, the State Council, Overall Plan for the Construction of Hainan Free Trade Port, June 4, 2020.

highly-demanded talents in Hainan¹. So as long as the vessel is registered in Hainan, the vessels' crew will get individual income tax deduction and exemption accordingly.

(4) Tax Rebate of Vessels

In the Overall Plan for the Construction of Hainan Free Trade Port (hereinafter referred to as the Overall Plan) issued in 2020, there are special tax rebate policies for the domestically built vessels², which should meet all the following three requirements:

- ① vessels should be built domestically;
- ② vessels should be registered at Yangpu Port of China;
- ③ vessels should be engaged in international shipping.³ Such policy will reduce the cost and trigger the vigor of domestic shipbuilding industry.

(5) Bonded Oil

Bonded oil is a kind of duty-free oil specifically for the international sailing vessels offered by one country. Those authorized bonded oil companies can import international fuel oil directly and independently, and avoid the import tax like tariff and consumption tax, while the import quota of domestic fuel oil of those companies can still be retained.⁴ Compared with the oil price in Singapore, the oil price at ports in China is \$10-\$15 higher per ton⁵. For further developing the shipping industry of Yangpu Port, Hainan FTP determines to provide bonded oil for the international shipping vessels and carry out export tax rebate policy⁶. Furthermore, technological innovation has been made to the mode of bonded oil refueling, from "one fuel ship for one shipping vessel"⁷ to "one fuel ship for more shipping vessels"⁸.

Yangpu bonded fuel business started from a 97-ton fueling in February 2020. Since then, the business has seen a continuous growth. Up to now, there have been 174 international vessels fueled more than 93 thousand tons bonded oil at Yangpu Port, which strongly stimulates the construction of Yangpu Free Trade Port Zone.⁹

3. Optimizing Financing Conditions

Shipping industry has a big demand for capital, which cannot be satisfied by the limited financing products directly offered by domestic banks. In that case, the industry practitioners have to mainly resort to loans to cover the payment for the purchase or building of ships.¹⁰ In fact, China once had

- 1 The People's Government of Hainan Province: The List of Highly-demanded Talents in Hainan Free Trade Port, August 28, 2020.
- 2 Overall Plan for the Construction of Hainan Free Trade Port: Under the premise of effective supervision and risk control, domestically built ships registered at Yangpu Port of China and engaged in international shipping are entitled to export tax rebate as in the situation of export.
- 3 The Central Committee of the Communist Party of China, the State Council, Overall Plan for the Construction of Hainan Free Trade Port, June 4, 2020.
- 4 ZHU Shiqiang, LI Jun & ZHANG He, Exploring the Construction of International Vessels service Base in Archipelago New Area: Thoughts on Building International Vessels Service Base in Zhoushan Archipelago New Area, Zhejiang Economy, Vol. 16, 2013, p. 48-49. (in Chinese)
- 5 ZHUANG Shaohui & CHEN Sheng, Strategies of Industry Development under New Systematically Supply: Take the International Vessels Bonded Oil Supply Industry in Zhoushan as Example, Chinese Market, Vol. 29, 2020, p. 58-59. (in Chinese)
- 6 Overall Plan for the Construction of Hainan Free Trade Port: Domestic ships with both domestic and foreign trade goods on board which transit at Yangpu Port of China are allowed to refuel with bonded fuel required for the voyage, or tax rebate could be claimed if the ships refuel with locally produced fuel oil for the voyage.
- 7 During one voyage, one fuel ship can fuel up just one international shipping vessel.
- 8 During one voyage, one fuel ship can fuel up more than one international shipping vessel.
- 9 FU Zhi, CHEN Kairen & LI Zheng, New Engine: Yangpu Bonded Oil Fueling Center Has a Steady Start, <http://hi.people.com.cn/n2/2020/1204/c231190-34455709.html>, December 4, 2020.
- 10 HAN Jingwei, REN Jinghui & JIANG Qihua, The Barriers that Prevent Chinese-funded Vessels with Foreign Nationality from Returning to China, China Transportation News, Vol. 7, 2015, p. 1. (in Chinese)

preferential policies for shipbuilding loan of shipping companies. However, such policies were abolished after 1995. Since then, the loan interest rate was raised to 8%-15% from 3.6%, which was about 4% higher than that in other countries. The repayment period was also narrowed to 5-10 years and the loan should be repaid after tax. Once delayed repayment happened, the ship companies should pay another 20% penalty interest.¹ While in abroad, there are more financing products, better service and more flexible modes. In most occasions, their loan term is generally 10 years with a lower interest rate of 3.23%-3.75%. In 2018, the volume of constructed vessels in China accounted for 43% of that in the whole world, while the vessel financing was lower than 10%. Newly-built international vessels generally choose overseas financing.²

To ameliorate the financing environment of vessels with Chinese nationality, the Overall Plan proposes to cancel the restriction on overseas financing of vessels and replace deposit with insurance. It also encourages financing institutions to put forward various financing business. The implementation of specific policies still needs to be further issued by Hainan.

4. Streamlining Registration Procedure

In the past, China was notorious for its cumbersome registration procedures. During the implementation of the Policy of "Tax Exemption Registration System of Special Cases", to complete the whole procedure, vessels should get 11 related documents and materials, which needed many departments to approve like Ministry of Transport, the registration authority of applying vessels, China Classification Society.³ What's more, because the time limit for approval were not specified, it still needed 6-9 months to complete re-registration, even if the applying procedure was smooth, which may cause huge loss to the vessel owners due to a long port time.

So in order to mitigate negative effects caused by complex registration procedure, on November 10, 2020, Hainan FTP issued the Stipulation of International Ship Registration Procedure in the Hainan Free Trade Port (hereinafter referred to as the Stipulation), in which approval process, time limit of approval, nationality changing of vessels and other aspects all get improved.

(1) Optimizing Approval Process

The Stipulation clarifies that the international ship registration can be completed online and by all registration institutions in Hainan⁴. Vessels' certificates and other documents issued or endorsed by maritime administrations will be all approved by ship registration institutions. Registration can be approved with electronic version of related certificates and documents⁵, which streamlining the vessel registration procedure. What's more, the information of vessels' certificates will be shared among ZC, Maritime Safety Administration and Ministry of Transport, which will make approval more efficient.

(2) Shortening Time Limit

When the applicants submit materials during ship registration, the officials in Chinese mainland will make applicants submit all originals of needed materials that may be rejected once there appears any problems, which may extend the time limit of approval. However, in order to offer convenience to applicants, the officials in Hong Kong China will ask them to submit scanned copies of materials at the beginning. Only when the scanned copies all meet the requirement, they will collect and verify originals

1 CHEN Jihong, ZHEN Hong & ZONG Beihua, *The Main Reasons Why Chinese Vessels Change Their Nationalities and Warnings*, *Sailing Technology*, Vol. 5, 2008, p. 72. (in Chinese)

2 JIN Xiaoyu, HE Zhicheng & PAN Tongtong, *The Future Will Be Bright if the Shipping Industry of Hainan Get Precisely Self-position*, *China Transportation News*, June 9, 2020, p. 3. (in Chinese)

3 XU Minxia, *The Advice on Optimizing the Policy of "Tax Exemption Registration System of Special Cases"*, *Water Transportation Management*, 32(9), 2010, p. 13-16, 26. (in Chinese)

4 Article 10 in the Stipulation: The applicants can apply the vessel registration through Maritime Safety Administration information system online, or apply at the registration institution.

5 Article 11 in the Stipulation: For the applicants registering through the information system, the registration institution can register the vessel according to the electronic materials. When applicants get the registration certificates, they should submit applying materials stipulated in the article 8.

of materials¹. The Stipulation issued by Hainan FTP also takes this practice. Applicants are not mandated to present the original certificates which can be verified on the e-government platform, nor the documents issued by maritime authorities, which reduces the applying materials and shortens the approving time. Also, the Stipulation clarifies the time limit for vessel registration. Once the vessel registration institution sends Notification of Acceptance, single item should be completed within one workday; if there are more than two items, one more day is permitted². Compared with the previous 7-day time limit, the approval time get shortened by nearly 86%.³

(3) Making Nationality Changing of Vessels More Easily

Considering that Chinese-funded FOC ships will suffer losses due to long port time when changing nationality, according to the article 16 in the Stipulation, for all the domestic vessels re-registering at “Yangpu Port of China”, when the applicants make cancelation registration at the previous port, they can make registration of international vessels ownership and nationality with relevant materials and certificates at Yangpu Port at the same time, thus solving the problem of non-suspension of ship transfer and greatly reducing the cost of time and money⁴.

5. Relaxing the Limitation on Business

For the shipping business, foreign-funded cruises cannot enjoy the same treatment as Chinese-funded cruises. To attract those Chinese-funded FOC ships, Hainan FTP will permit those Chinese-funded FOC ships to take part in coastal container transportation among ports in China and coastal cruise transportation. What’s more, the policy of international sea cruising for Chinese-funded FOC ships has already been in discussion.⁵

In a bid to attract Chinese-funded FOC ships to reregister in China, Hainan FTP also makes some innovation for the nationality changing of Chinese-funded FOC ships. When the Chinese-funded cruises re-register in China, they can choose to hang the flag of the PRC, or the flag of Hong Kong China, and they are permitted to take part in the coastal cruise transportation with Sanya as their departure port. This policy can not only provide vessels’ owners with more choices when registering, but benefit the expansion of Chinese fleet scale.

III. Prospect Analysis of Hainan FTP Attracting Chinese-funded FOC Ships to Register in China

i. The Achievements of Hainan FTP in Attracting Chinese-funded FOC Ships to Register in China

Since Notice by the State Council of Issuing the Framework Plan for China (Hainan) Pilot Free Trade Zone was issued in 2018, the vessel registration business at Yangpu Port has seen a huge progress (table 4). Although the number of vessels registered at Yangpu Maritime Safety Administration is far less than that of Sanya Maritime Safety Administration, the total load capacity of registered vessels, 78435 tons, ranks the first place among other registration administration in Hainan. From this point, it shows that the vessels registered at Yangpu Maritime Safety Administration are all high quality vessels with big load capacity, which just meets the demand of Chinese fleet.

- 1 ZHANG Liying, the Law-related Problems When Chinese-funded Vessels Register in Hong Kong China and Apply for the Flag of Hong Kong China, *International Economic Cooperation*. Vol. 5, 2011. p. 91-94. (in Chinese)
- 2 Article 12 in the Stipulation: The vessel registration institutions should complete the registration within one workday once they send notification of acceptance. If more than 2 items are applied to be handled together, one more workday is permitted.
- 3 XIAO Xiao, Benchmarking with international practice, Hainan gets some changes. Subscription in Wechat “Hainan Free Trade Port”. November 30, 2020.
- 4 Article 16 in the Stipulation: For the domestic vessels registering at “Yangpu Port of China” for the transiting ownership and other reasons, the applicants are permitted to make cancelation registration at the former port, and make registration of international vessels ownership and nationality with relevant materials and certificates at Yangpu Port at the same time
- 5 The Implementation Plan for Conducting Guiding Opinions of the CPC Central Committee and the State Council on Supporting Hainan in Comprehensively Deepening Reform and Opening Up, Ministry of Transport of the People’s Republic of China, July 25, 2018.

Institution	Number	%	Total load capacity	%
Administrative center of Hainan Maritime Safety	0	0	0	0
Haikou Maritime Safety Administration	48	16.49%	21989	17.09%
Qinglan Maritime Safety Administration	2	0.69%	14	0.01%
Sanya Maritime Safety Administration	202	69.42%	7278	5.66%
Basuo Maritime Safety Administration	1	0.34%	366	0.28%
Yangpu Maritime Safety Administration	31	10.65%	78435	60.96%
Sansha Maritime Safety Administration	4	1.37%	20585	16.00%

Table 4: the number, total load capacity and proportion of registered vessels at different registration institutions in Hainan Province in 2019¹

As the Overall Plan was issued in 2020 and other supporting measures on customs, taxation and administration were also put forward, the number of international vessels with “Yangpu Port of China” as the port of registry has realized an obvious increase. According to the relevant statistics, as of November 25, 2020, there are 5 newly founded shipping companies in Hainan; and 200 more vessels registered or re-registered at Hainan FTP, which is 57% higher than that of last year during the same period; the international vessels’ load capacity increase by 3.2467 million tons, which is 87% higher than that of last year; there are another 19 international vessels registered at “Yangpu Port of China”, which increases by 3.1726 million tons load capacity. The load capacity per vessel increases from 60 thousand tons to 150 thousand tons, then to 300 thousand tons, which has seen twice huge growths in a half year.²

So for attracting Chinese-funded FOC ships, Hainan FTP international ship system has gained some progress. However, because this policy is newly issued and the supporting measures are still being constructed, there are also some problems appearing.

ii. Problems in Carrying out the Registration System

1. The Preferential Policy for the International Ship Registration are Difficult to be Put into Practice

Although some policies in the Overall Plan release many beneficial signs, those policies are hard to be put into practice. For example, in June, 2020, a vessel called “COSCO Shipping Xing Wang” (Shipping Xing Wang from China Ocean Shipping (Group) Company) got registered at “Yangpu Port of China”. This vessel is domestically-built and engaged in international shipping, which meets all requirements stipulated in the export tax rebate policy in the Overall Plan. But the import tariff the vessel’s owner had paid for the accessories of the vessel during construction were hard to be refund³.

1 The Statistics and analysis of vessels registered in administrative areas of Hainan Maritime Safety Administration in 2019. <https://www.hn.msa.gov.cn/data/37841.jhtml>, visited on December 23, 2020.

2 SHEN Xiaoming, the secretary of provincial party committee, investigated and survey at Yangpu Maritime Safety Administration. https://www.hn.msa.gov.cn/hszc_10_1/38894.jhtml, December 4, 2020.

3 HUANG Hailing & CHEN Jinghua, Policy Research Center of Provincial Party Committee: the Challenges of and Advices to the Integrated Innovation of Hainan Free Trade Port International Vessel Registration System, subscription in Wechat “Hainan Today”. Vol. 7, 2020. p. 33-35.

What's more, those newly-built vessels that are going to register at Yangpu Port recently were all built one or two years ago, whose accessories are mostly imported. If it's hard to make tax rebate for the imported accessories, the positivity of vessels registering in Hainan will be greatly affected.

According to the Stipulation, the time limit for making international vessel registration is one workday¹. But "COSCO shipping Xing Wang", as the first vessel registered at "Yangpu Port of China", spent 3 days completing the registration.² In contrast, in Guangzhou Nansha free trade zone and Hong Kong China, the whole procedure just cost 1 day and 2 hours respectively³. Besides, because Hainan Yangppu international vessel registration center was just constructed, there are not enough talents who have good command of foreign language to handle the global vessels consultation and registration all around clock.

2. Various Tax Incentives are Prone to Cause the Risk of Tax Base Erosion

According to the Overall Plan, under certain conditions, Hainan will realize zero-tariff in the future, which is lower than the tariff rate of 7.5% China has now. Corporate income tax rate will decrease to 15% from 25%; individual income tax rate will be reduced from 45% to 15%; VAT, consumption tax, vehicle purchase tax and other taxes will be all concluded into sales tax⁴. There is no doubt that strong taxation preferential policies can improve the competitiveness of Yangpu Port as the international ship registration port, but such policies may also cause tax base erosion. Especially to those multinational corporates doing international transporting business, we should prevent them from setting shell companies in Hainan that abuse tax preferential policies to harm mainland taxation and disturbing the normal order of Chinese taxation.⁵

Hainan FTP has taken some international standards for reference when planning taxation system, like some stipulations on substantial activities and the actual offices of management. And in the policy of deducting and exempting income tax, it is clearly stipulated that corporates must "practically operate"⁶ and persons must "work in Hainan FTP"⁷. But when it comes to practice, the detailed judging elements are still to be further clarified. "Working in Hainan FTP" is generally easy to be judged, which can rely on elements like days staying in Hainan FTP, household registration and labor contract; but "practical operation" of corporates is more abstract⁸, it still needs to be discussed that how to understand and set the rules of "practical operation".

3. Some System Are Still Conservative

Considering the correlation between the age of a ship and its performance in environment protection and safety technology, the Ministry of Transport of China remains reluctant to lift the 34-year limit for general cargo ships and 33-year limit for bulk carriers, despite the shipping companies' strong call for relaxing the limit.⁹ However, the policies in Hong Kong China are more flexible. There is no

- 1 Article 12 in the Stipulation: The vessel registration institutions should complete the registration within one workday once they send notification of acceptance. If more than 2 items are applied to be handled together, one more workday is permitted.
- 2 The first vessel "Prosperity" gets registered at "Yangpu Port of China", all the maritime certificates are approved in 3 workdays, China Transportation News, http://www.mot.gov.cn/jiaotongyaowen/202006/t20200605_3323121.html, June 5, 2020.
- 3 ZHANG Xiheng, The Hong Kong China Vessel Registration System and the experience, Scientific development, Vol. 1, 2009, p. 62.
- 4 The Central Committee of the Communist Party of China, the State Council, Overall Plan for the Construction of Hainan Free Trade Port, June 4, 2020.
- 5 CHEN Yikan, Hainan Free Trade Port Reconstructs Taxation System, Relieving Tax Burden instead of Being Tax Heaven, <http://www.hi.chinanews.com/hnnew/2020-06-03/528782.html>. June 3, 2020.
- 6 Notice by the Ministry of Finance and the State Taxation Administration of Preferential Income Tax Policies for Enterprises in Hainan Free Trade Port, June 30, 2020.
- 7 Notice by the Ministry of Finance and the State Taxation Administration of Preferential Value-added Tax Policies for International Shipping Vessels in Hainan Free Trade Port, September 21, 2020.
- 8 LIU Lei, Thoughts on the Innovation of Taxation System Reform in Hainan Free Trade Port, International Taxation, Vol. 11, 2020, p. 3-8.
- 9 Notice of the Ministry of Transport, National Development and Reform Commission and the Ministry of Finance on Revising and Issuing Opinions on Implementing Mandatory Scraping System of Shipping Vessels, January 6, 2017.

mandatory stipulation for the vessel age, as long as the vessel condition can meet the testing requirements, the vessel can be used for shipping business¹, which is beneficial to the effective use of resources.

4. Lacking Supporting Measures of Supervision

All policies and stipulations issued by Hainan FTP are releasing preferential information to attract vessels to register in China. However, the reason why some countries and regions like Singapore and Hong Kong China can ensure both the quality and quantity of vessels registered is that they carry out strict supervision on the vessels' original registration place. For example, if the Marine Department of Hong Kong China finds out bad records of vessels that come for registration, they will not only conduct pre-registration flag State quality control audits, but also monitor the vessel's movements immediately after registration. Besides, they will inform the vessel's owner of the problems existing in vessels' equipment and staff management and relevant advices. The inspecting content, result and advice on management can be all found in the inspection report issued by the inspector. And the Marine Department of Hong Kong China will visit regularly to secure the safe operation of vessels.²

So apart from giving preferential policies, Hainan FTP should also conduct strict inspection on the quality, technique, ship crew and other aspects of vessels with Chinese nationality. For Hainan FTP ship registration system, it still needs to think about how to scientifically plan and conduct supervision measures of vessels.

IV. Advice on Optimizing the Registration System

i. Clarifying the Responsibility of Relevant Departments to Promote the Conduction of Preferential Policies

As a comprehensive system, international ship registration system doesn't only need to revise relevant marine regulations, but the cooperation of relevant central departments (table 5). If this reform only relies on the efforts of Maritime Safety Administration, all the preferential policies may be hard to put into practice, which may hinder the return of Chinese-funded FOC ships.

No.	Contents	Related department
1	Suspending the implementation of the superior law (including laws and administrative rules) of Hainan Free Trade Port International Vessel Management Regulation; authorizing the legislation about Hainan Free Trade Port international vessel registration management in Hainan Free Trade Port Law.	Hainan Provincial People's Congress
2	Leading the drafting of Hainan free trade port international vessel management regulation; put all integrated innovation regimes into stipulations of law; innovating the systems of Hainan free trade port international vessel registration, ship crew management and shipping company safety management; innovating to conduct joint onboard ship inspection and other supervisory methods	Maritime Safety Administration of Hainan Province
3	Tax deduction and exemption for the registered shipping companies and relevant service companies (financing, leasing, fixing, insurance, law service); tax deduction and exemption for the Hainan free trade port international vessels; personal income tax deduction and exemption for the senior management personnel in the companies above and ship crew; set standard of application for tax incentives; cancel the tax filing requirement of outbound foreign exchange payment	Department of Finance of Hainan Province; Hainan Provincial Tax Service
4	Classifying Hainan free trade port international vessels; tax deduction and exemption for tariff, import VAT; simplifying the supervising and detecting systems	Haikou Customs

1 Liying, A Comparative Study of 'Hong Kong Flag' Ship Registration, *Asia Pacific Law Review*, Vol.18:2, p. 202(2010).

2 ZHANG Liying, The Law-related Problems When Chinese Vessels Register in Hong Kong (SAR) and Apply for the Flag of Hong Kong (SAR), *International Economic Cooperation*, Vol. 5, 2011, p. 91-94. (in Chinese)

5	The feasibility of ad hoc arbitration and arbitration abroad for commercial dispute of vessels; the feasibility of permitting foreign arbitral institution to conduct arbitration in Hainan free trade port; compulsory notarization project for vessels registration; opening up for notarization institution; priority of compensation of financing and leasing leasers	Provincial High Court; Department of Justice of Hainan Province
6	Relaxing the limit on financing abroad of vessels; simplifying the financing procedure and foreign exchange management procedure.	People's Bank of China Haikou Branch Office (State Administration of Foreign Exchange Hainan Branch)
7	Permission to hire overseas ship's crew; social insurance of overseas ship crew; unified conducting of detecting maritime labor condition; permission for enterprises abroad to establish ship crew training institution in Hainan free trade port.	Department of Human Resources and Social Security of Hainan Province
8	Visa free policy and duration of stay of ships' crew with foreign nationality and their accompanying families.	Department of Public Security of Hainan Province
9	Simplifying the industry management for Hainan free trade port international vessels, shipping companies and waterway transportation ancillary industries	Department of Transport of Hainan Province
10	Canceling the import permission of used mechanical and electrical products for vessels; promoting the high-level construction of single window	Department of Commerce Of Hainan Province
11	Setting mutual insurance organization and captive insurance companies of shipping industry; increasing insurance products for shipping industry.	Hainan Banking and Insurance Regulatory Commission

Table 5: the relevant departments and their working contents in Hainan free trade port international vessel registration system¹

So here comes some advice. The provincial leaders should take the leading role, promote the subordinate departments to draw out the working plan, and arrange reasonable timetable according to the complexity of system construction, clarify the responsibilities of each party, put forward more detailed supporting measures and implementing rules and establish practice-oriented international ship registration system, without making the preferential policies castles in the air.

To make it not hard to refund tax anymore, Hainan taxation authorities should further clarify the procedure of tax rebate and complete relevant supporting services. For example, the authorities can learn from the practice of Hong Kong China, putting applying charts, relevant notices and laws and regulations on the website of Yangpu Port office for download, and improve the efficiency of tax rebate through applying and approving tax rebate online. To solve the problem of low registration efficiency, the institution can also learn from Hong Kong China, strengthening the training of approving personnel. At the same time, to avoid registration being affected by jet lag, the institution can set offices in global major cities, to make it easier for vessels' owners to register.

ii. Putting the Rules of Practical Operation into Practice to Avoid Tax Base Erosion

The conducting of rules of practical operation should pay attention to the following two points:

Firstly, we should balance the general rules at home and abroad and the special rules in Hainan FTP.

In Action 5 - 2015 Final Report², it is mentioned that "substantial activity" is one of two factors judging harmful tax practice, which is to prevent some countries or regions from abusing tax

1 HUANG Hailing & CHEN Jinghua, Policy Research Center of Provincial Party Committee: the Challenges of and Advices to the Integrated Innovation of Hainan Free Trade Port International Vessel Registration System, Subscription in Wechat "Hainan Today". Vol. 7, 2020, p. 33-35.

2 BEPS Actions are developed in the context of the OECD/G20 BEPS Project, the 15 actions set out below equip governments with domestic and international rules and instruments to address tax avoidance, ensuring that profits are taxed where economic activities generating the profits are performed and where value is created. Among the Actions, the fifth action is to counter harmful tax practice with a focus on improving transparency.

preferential policies to attract corporates¹. In Commentaries on the Articles of the Model Tax Convention, the meeting places of the board of directors and alike institution have been listed as a factor of places where actual offices of management locate². The domestic law in China has also stipulated the conception and its notification of actual office of management³. While “practical operation” is a new conception raised by Hainan FTP, which is to avoid Hainan FTP being a new tax haven. The innovation of this conception is to combine “practical operation” with actual offices of management. From the aspect of applied environment and purpose, this measure is basically the same as substantive standard to govern and substantial economic law of tax haven in the OECD Model Tax Convention.

Secondly, we should clarify the core factors and auxiliary factors. Core factors is essential to judge whether the corporates registered in Hainan FTP conduct “substantial operation”. The key to judge whether there-existing “substantial operation” is that whether the institutions set in Hainan FTP can conduct comprehensive management and control to corporates⁴. Because management and control rely on relevant personnel, Hainan relevant taxation system should stipulated certain portion for the senior executives and personnel conducting actual control who work or live in Hainan FTP. And such portion can be regarded as one of the core factors judging “substantial operation”. While other factors like capitals, account books and working places can be regarded as auxiliary factors.

iii. Further Relaxing the Limit on Vessel Age

In most countries and regions like America, Greece and Hong Kong China, there is no limit on vessel age for registered vessels. Instead, they will strengthen the vessel inspecting and shipping company management. Because for shipping companies, the fundamental guarantee of their sustainable development is safe operation. The vessel age is not everything that determines navigation safety. To lower risks, most shipping companies will choose to obey the international convention or the stipulations of national maritime safety administration as much as possible. Many vessels whose age has been over 34 years are still usable for transport.⁵

What's more, premature scrapping of ships is not a best strategy no matter for China or for corporates. At present, the 80% of the capital used to construct new vessels is from loan⁶, whose interest is 5% higher than that of international market. For those shipping companies, because of the high cost of financing and lack of shipbuilding allowance, most of the profit earned will be used to repay the loan. For the capital-intensive shipping industry, this can only make things worse. So Hainan FTP can try to relax the limit on the vessel age, paying more attention to the vessel testing and shipping company management.

iv. Establishing Complete International Ship Supervision System

It is a systematic project to strengthen the supervision duty of registration place. First of all, the companies owning vessels and the personnel on the vessel should be also regarded as the targets of

- 1 OECD: Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5 - 2015 Final Report (translated by International Taxation Office of State Taxation Administration), 2016, Beijing: China Taxation Publishing House, p. 367-409.
- 2 OECD: Commentaries on the Articles of the Model Tax Convention (translated by International Taxation Office of State Taxation Administration), 2017, Beijing: China Taxation Publishing House, p. 182.
- 3 Article 2 in Enterprise Income Tax Law of the People's Republic of China (2018 Amendment): The term “resident enterprise” as mentioned in this Law refers to an enterprise that is established inside China, or which is established under the law of a foreign country (region) but whose actual office of management is inside China.
- 4 Article 4 in Regulation on the Implementation of the Enterprise Income Tax Law of the People's Republic of China (2019 Revision): The term “actual office of management” as described in Article 2 of the EIT Law refers to the institutions conducting comprehensive management and control practically to the operation, personnel, capital, accounts and other elements of enterprises.
- 5 Notice by the Ministry of Finance and the State Taxation Administration of Preferential Income Tax Policies for Enterprises in Hainan Free Trade Port: Substantial operation refers to the actual office of management of enterprises are set in Hainan FTP and conduct comprehensive management and control practically to the operation, personnel, capital, accounts and other elements of enterprises.
- 5 GUO Weina, the Discussion about Limit on Vessel Age in China, Transportation Technology, Vol. 5, 2007, p. 114.
- 6 GUO Weina, the Discussion about Limit on Vessel Age in China, Transportation Technology, Vol. 5, 2007, p. 113.

supervision, as well as the vessels. Then the supervising stages should be divided into on-registration and post-registration, which can make supervision more pertinent.

In the course of registering, authorities may, referring to Hong Kong's experience, adopt FSQC system to make a primary assessment to the quality of vessels. Besides, we should strictly conduct the Rules of the People's Republic of China on the Safety Supervision of Ships, requiring vessels to get vessel inspection certificate issued by authorized institution before applying for registration. For ship crew, they should submit the certificates issued by engaged countries of STCW rules.¹ After registration, the maritime safety administration institution can set assessing index for vessel quality and company management, assessing the vessel quality of registered vessels regularly. To those vessels and companies with low marks or bad records, the institution will conduct the special safety detection specifically. For ship crew, blacklist system can be applied. Those crew who have been in the blacklist and make the same mistake again will be forbidden to work on the international vessels.

V. Conclusion

Now, compared with the former policies China adopted to attract Chinese-funded FOC ships, the international ship system in Hainan FTP has made a huge breakthrough, which relaxes registration conditions and taxation greatly, and creates good financing environment and convenient registration procedure for vessels through various methods. However, this system is still in its primary stage, many problems have appeared in the practice, like frustrated preferential policies, inefficient registration, conservative policies and lack of supervision system. In the future, all the related departments in Hainan province should further clarify their responsibilities, perfect relevant supporting measures and laws, promote the conduction of preferential policies. At the same time, they should further relax the limit on the vessel age, remove the center of supervision to the testing and management of vessels, conduct supervision pertinently through complete quality assessing system of vessels' crew, vessels and ship companies and blacklist system. These measures can guarantee the coming back quantity of Chinese vessels hanging "flags of convenience" and the quality of registered vessels, promote the transition of China from a shipping giant to a shipping power.

Translators: YUE Shan
CAO Jie

Editors (English): YUE Shan
CAO Jie

Executive editor: LUO Yueqi

¹ International Convention on Standards of Training, Certification and Watchkeeping for Seafarers: it was adopted by the International Conference on Training and Certification of Seafarers on 7 July 1978, and entered into force on 28 April 1984. The 1991 amendments, relating to the global maritime distress and safety system (GMDSS) and conduct of trials, were adopted by resolution MSC.21(59) and entered into force on 1 December 1992. The 1995 amendments were adopted by resolution 1 of a Conference of Parties to the International Convention on Standards of Training, Certification and Watchkeeping for Seafarers, which entered into force on 1 February, 2002. China was engaged into this convention on 28 June, 1981. Now the Convention and its amendments are all effective to China.