

1. Is Malaysia a Competitive Flag State? A Condition or an Intermediate Term? Bulk Cargo? | All articles by Andrew Chiew Ean Vooi and Jennifer James Ilango |

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Is Malaysia a Competitive Flag State?

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A shipowner is free to choose to flag his ship in a country where he has some genuine connection by way of national or economic ties, or he can have it registered in an open registry system which will accept the ship, regardless of the nationality of the beneficial owner or the country from which the ship is effectively controlled — a flag of convenience.

In Malaysia, a shipowner may register his ship under one of the available traditional registries¹ or under the Malaysian International Ship Registry (MISR), which was established in 2006.² The MISR offers a shipowner the benefits of a flag of convenience and was set up to encourage foreign individuals or shipping companies to register their ships in Labuan.³

Some of the relevant factors that shipowners may want to consider when choosing to flag their ships in Malaysia are discussed below.

- 1 There are four traditional registries in Malaysia: Port Klang, Penang, Kota Kinabalu and Kuching
- 2 By virtue of Part IIC of the Merchant Shipping Ordinance 1952. Amendment introduced by the Merchant Shipping (Amendment) Act 1998 [Act A1014].
- 3 Merchant Shipping Ordinance 1952, s 66B. The ship must be owned by a non-Malaysian or corporation, with a majority of the shareholders (at least 51%) being non-Malaysian.

Operational cost

Tax incentives

More often than not, this will be the dominant factor, generally related to the fiscal regime of the flag state. Government incentives such as a more favourable tonnage tax or tax rebates earned from the operational profits are often given to entice shipowners to register their ships in the flag state.⁴

In Malaysia, tax exemption is granted for revenues earned from shipping activities so long as the qualifying conditions are met.⁵ The tax benefits, however, do not apply to shipping activities involving tugs, barges, supply vessels and crew boats, among others, as they are expressly excluded under the Income Tax Act 1967.⁶ Salaries of Malaysian crew on board supply vessels are also not tax exempted, whereas their counterparts on ocean-going ships are.⁷

Government support

Reduced initial fee related to the registration of a ship would be another factor. There may also be investment grants for local shipbuilding and purchase of second-hand ships. One such initiative was introduced by the Malaysian government in establishing the Government's Shipping Venture Fund to support the purchase of ships and as venture capital for equity participation in local shipping companies.⁸

Crewing constraints

Some States introduce crewing requirements. When a ship is registered with one of the traditional registries

in Malaysia, at least 75% of the crew on board must be Malaysian citizens.⁹ Under the MISR, there is no restriction on the nationality of the crew so long as the ship manager or ship management company operating the ship is incorporated in Malaysia.¹⁰ All crew, however, must meet the standards of the International Convention on Standards of Training, Certification and Watchkeeping for Seafarers (STCW) 1978.

Financing

A shipowner's decision may be affected by the willingness of a financier to lend on ships flying a foreign flag.¹¹ A financier will be unwilling to finance a ship in a jurisdiction where there is a history of default in the repayment of foreign loans or whose legal system may present as an obstacle to the enforcement of the mortgagee's security.

Financiers would also be interested in the priority conferred by the relevant jurisdiction on a preferred mortgagee in the event of default. Under Malaysian admiralty law, which is modelled after the English law, a mortgagee would rank higher than statutory lien holders but lower than maritime and possessory lien holders.¹²

Cabotage policy

It may serve as an incentive to some shipowners to flag a ship in a certain jurisdiction to have the right to engage in cabotage trade.¹³ In Malaysia, all domestic trade and offshore related services within her waters are reserved for ships registered in the country.¹⁴

Employability

A shipowner must be careful to not opt for a disreputable flag state with poor port state control as it will affect the

4 Ian Goldrein, "Ship Sale and Purchase" (Lloyd's Shipping Law Library, 2nd Ed) at 227

5 Income Tax Act 1967, ss 54 and 54A. All incentives under the income tax and stamp duty exemptions apply to ships registered in the MISR so long as qualifying conditions are met. Shipping companies operating ships registered in the MISR can enjoy the competitive tax rate and benefits offered by the Labuan Business Activity Tax Act 1990 by incorporating a Labuan company to conduct their business. See Nazery Khalid, Margaret Ang and Elvia Cory Abu Hasan, "Incentives for the development of Malaysia's merchant shipping and port sectors" <<http://www.mima.gov.my/mima/wp-content/uploads/Incentives%20for%20the%20development%20of%20Malaysia's%20merchant%20shipping%20and%20port%20sectors.pdf>>

6 Section 54A(6)

7 Schedule 6, Exemption from Tax, Para 34(1) and (2) of Income Tax Act 1967

8 <<http://www.treasury.gov.my/pdf/budget/speech/bs01.pdf>>

9 <<http://edsl.mot.gov.my/public/public.cfm?type=details>>. See Goldrein, *supra* n 4 at 226.

10 Merchant Shipping Ordinance 1952, s 66C

11 *Supra* n 4 at 232

12 Toh Kian Seng, "Admiralty Law and Practice" (LexisNexis, 2nd Ed) at 345

13 *Supra* n 4 at 227

14 Merchant Shipping Ordinance 1952, s 65KA(1)

employability of the ship if she is presumed to be sub-standard. This is particularly relevant within the tanker industry. Major oil companies have high standards when chartering a ship as they are careful not to incur liability for environmental pollution or damage, which can have a negative impact on their reputation and have financial consequences.

Port state reputation

A shipowner should also take into account the reputation of the flag state by referring to the detention rate under the Memorandum of Understanding of Port State Control (MOU).¹⁵ The MOU is primarily intended to induce shipowners to register their ships under flags whose ships have a low detention rate because the flag state has taken proper measures to ensure the attainment of basic international treaty obligations.¹⁶

Malaysia is categorised as one of the “White List” countries under the Tokyo MOU.¹⁷ Consequently, they take detention by any local or foreign port authorities due to serious non-compliance as a reason to cancel the detained ship’s Certificate of Registry. This is done to safeguard the image of Malaysia as a preferred and reputable ship registry.¹⁸

Military support

If a ship will be operating in waters with high risk of piracy, shipowners will have concerns with the availability of naval protection. Malaysian-flagged ships have the protection of the Combined Maritime Forces, which is a multinational naval partnership between 32 member states, which exists to promote security and stability among some of the world’s most important shipping lanes.¹⁹

Trade sanctions

Trade sanctions can affect the operations of a ship. For example, any ship that docks at any of the Cuban ports will not thereafter be allowed to dock at any of the US ports for at least 180 days under the Cuba Sanctions.²⁰ Another example is the recent prohibition on insurers and reinsurers operating in the European Union from providing insurance cover in relation to shipments of crude oil or petroleum products that are transported from Syria.²¹ So far, there is no trade sanction that affects Malaysian-flagged ships.

Other factors

Only self-propelled ships can be registered under the Malaysian registries. As the law stands, there is no provision for the registration of floating installations such as an oil rig.²²

Furthermore, to be registered under the MISR, a ship must at least be 1,600 gross tonnage.²³ There is an age limitation of 15 years for tankers or bulk carriers and 20 years for other types of ships.²⁴ With the traditional registries, there is no age restriction, although ships older than 20 years will be subjected to special surveys to verify their seaworthiness and condition. These conditions are intended to eliminate substandard shipping and to promote maritime safety.

Conclusion

In 2017, a total of 108 ships²⁵ were registered under the Malaysian registries. With reputable port state control, governmental support and tax incentives, Malaysia has the potential to grow and be recognised as a preferred flag state in Southeast Asia. When the Merchant Shipping (Amendment) Act 2017 comes into force, registration of ships will extend to bareboat chartered-ships.²⁶ **LH-AG**

15 Malaysia is part of the Tokyo MOU signed in Tokyo on 1 December 1993

16 <<http://www.tokyo-mou.org/>> (accessed 5 February 2018)

17 The White List identifies countries that have demonstrated a plan that complies with the STCW Convention and Code as revised in 1995

18 Malaysian Shipping Note No MSN36/2010 <<http://www.marine.gov.my/jlmeng/pic/article/service/notice/NPM/2010/MSN362010.pdf>>

19 Malaysia is a member of the Combined Maritime Forces. For details, see <<https://combinedmaritimeforces.com/about/>>

20 The Cuban Sanctions was relaxed in November 2017 to include certain exemptions. See <https://www.treasury.gov/resource-center/sanctions/Programs/Documents/cuba_faqs_new.pdf>

21 <<https://www.ukpandi.com/knowledge-publications/article/eu-insurers-prohibited-from-insuring-any-oil-shipments-from-syria-3635/>>

22 Merchant Shipping Ordinance 1952, s 2. In Singapore, the definition of “ship” includes offshore industry mobile unit, whether self-propelled or towed by a barge: see s 2 of the Merchant Shipping Act 1995.

23 Merchant Shipping Ordinance 1952, s 66E(1)(b)

24 *Ibid*, s 66E (1)(c)

25 Equivalent to 177,527.10 gross tonnage according to statistics prepared by the Marine Department of Malaysia <<https://drive.google.com/file/d/1mjFn6L01uInYwlCcz6P4XBqX2eB77iVW/view>>

26 [Act A1551]