



## **Sri Lanka Shippers' Council**

**ESTD 1966**

### **REFORMS IN THE SHIPPING INDUSTRY**

**This is a response to the allegations from a new set of service providers who are trying to mislead the Government on shipping and trade, once again to distort the freight market in Sri Lanka**

**It's understood that they are lobbying Senior Minister's to bring back these unethical and anticompetitive practices for their personal Gain, which they had done for over 3 decades**

The proposals for the National Budget in 2014, presented by the President in his capacity as Minister of Finance contained in the paragraph Shipping Economy, section 35.1, a policy that intended to provide far reaching benefits for the export sector in general and specifically for the SME export sector, the manufacturing industry and consumers.

The proposal states inter alia that "In order to promote the shipping economy in a more structured manner, It also propose to set up a fully fledged Merchant Shipping Authority by introducing timely amendments to the Merchant Shipping Act. **In order to prevent monopoly pricing in the shipping trade, no shipping line will be permitted to levy terminal handling and other charges in addition to freight and specified international charges for container cargo. Relevant prohibition will be made effective through amendments to the Finance Act, effective from January 2014**".

The Budget Proposal which was enacted through the Gazette Extraordinary No. 1842/16 dated Friday, December 27, 2013 through regulations made under Section 10 of the Licensing of Shipping Agents, Freight Forwarders, Non-Vessel Operating Common Carriers and Container Operators Act No 10 of 1972, read with Article 44(2) of the Constitution of the Democratic Republic of Sri Lanka (attached).

Subsequent to the Proposal and before the enactment of the new regulations, extensive discussions have taken place in several forums and in the media, both for and against the Budget Proposal.

To fully appreciate the importance of the proposal, the relationship between International Trade and the Carriage of Goods has to be clearly understood.

In international trade, the carriage of goods is the responsibility of the shipping lines/ship operators, which is entrusted to them by users of such services. Users could either be buyers or sellers. The service providers, once given the responsibility, undertake to collect and deliver goods from one point to another.

Depending on the custom of a port in the manner in which it operates, containerized cargo is generally delivered from a container yard (CY) to Container yard (CY or container freight station (CFS) to container freight station.

In the case of shipments which are on a freight collect basis, it is an arrangement between the **buyer and the service provider** and in the case of pre paid freight shipments, it is an arrangement between the seller and the service provider who contracts for the full freight. The pick-up, loading, onto a ship, transporting and unloading a consignment of cargo at the relevant destination port and making it ready to be collected by the importer at the given point of delivery is the responsibility entrusted to the shipping line/service provider. It is for this purpose that a shipping line enters into contract with the party who pays the freight charges.

In container handling operations, when a shipping line accepts a consignment from CY to CY or CFS to CFS, all activities including the loading of a container at the port of loading onto the carrier, transporting it to the destination port, discharging it onto the quay apron, moving it to the marshalling yard, demounting and stacking it at the terminal are included.

When a consignment is taken for delivery from one point to another, it is the sole responsibility of the carrier to ensure the delivery. No other party can perform this activity because delivery to the destination is a condition agreed and not merely as a place of convenience. An all inclusive freight rate is levied to cover all these responsibilities and all costs to the port payable by the ship and operator has to be borne by the party paying the freight. It is a known fact that the container is termed as extended ship's gear.

In accordance with prevailing practices internationally, shipping lines are required to pay in advance, these charges to the relevant ports authorities.

However, in 1997, shipping lines providing their service to Sri Lanka, for reasons best known to them, introduced a charge termed "Freight Surcharge", which was immediately renamed as the **Terminal Handling Charge (THC) by circular No. 35/97 issued by CASA on April 21, 1997.**

The claim made by the service providers that the THC is a land based cost payable in full to the ports authority cannot be justified. In terms of the Sri Lanka Ports Authority's (SLPA) tariff guidelines (published in 2011), Section III – stevedoring and harbour tonnage – items 16-20 are payable by the ship or ship operator. There is no necessity to involve the shipping lines to pay these charges if the costs are to be borne by the local shipper. If this is the case, these charges could also be paid direct by the local party in Sri Lanka to the SLPA, as they are already paying the tariff which is identifies as payable by them without going to the service provider. The fact that shipping lines collect these charges and are paying to the SLPA, proves that these charges are payable by the ship/operator and not by the local exporter/importer.

This further strengthens the argument and indeed, proves that these charges must be included as part of the overall freight rate because the contractual obligation is between the carrier and the party who undertakes to pay the freight cost and not any other party.

Shipping lines/service providers have argued that separating the THC from the freight is international practice, barring a few rare exceptions. In developed countries, when a THC is

imposed, it is paid by the party who contracts to pay the freight. An example of this practice is in the USA, where the delivery duty charge which is the equivalent to the THC, is a payment made to the Ports Authority, which is included in the freight cost. Service providers are also fully aware that even the trucking charges are included as a component of the freight charges.

In addition, even in transshipment ports such as Singapore where more than 90% of container throughput is transshipment, the THC is included as part of the freight when cargo is transshipped.

**Bangladesh prohibited the imposition of a THC by administrative fiat in 2007 and experienced a massive growth in exports with ships continuing to call at the port of Chittagong. This proves that the principle of including the THC as a component of freight is accepted. The same principle therefore, should apply to origin ports as well.**

Sri Lanka's Exchange Control Regulations provide only for the repatriation of freight collected, adjusted for any currency adjustment factor (CAF) and Bunker Adjustment Factor (BAF). No other charges which are collected can be repatriated. Accordingly, no charges can be collected on inward cargo which has been shipped on CIF terms.

Although the Fair Trading Commission of Sri Lanka gave a ruling on March 30, 1998 in favour of shippers, citing that the THC should be a part of the freight cost, it could not be implemented because the Commission lacked the legal backing to do so.

Despite increasing pressure from shippers, lines continued to levy the THC as a separate charge to freight cost, until in 2007, shippers comprising exporters and importers sought redress through the Supreme Court of Sri Lanka by way of a fundamental rights application, praying for:

1. a staying of the proposed increase of the THC from USD 115 to USD 155 per TEU
2. requesting the establishment of a proper legal authority to look into matters which are considered anti-competitive in the shipping industry.

The service providers countered the move by requesting the Supreme Court not to grant leave to proceed, citing that shipping lines would not call at the port of Colombo, if such action was proceeded with.

The Chief Justice at that time was of the view that exporters would not come before the Supreme Court if there was no grievance. He also observed that Sri Lanka did not have a modern legal system to resolve disputes such as this.

The Chief Justice appointed Director of Merchant Shipping to chair a committee comprising one representative each from shippers and shipping lines to resolve the issue. The court action was kept open until a solution was reached.

The mediation committee failed in its attempts to address and resolve the issue because a unilateral and unethical mechanism was secretly used by a party with a vested interest, to manipulate and produce a document without consulting the petitioners, instead, used a person from within the petitioners, the Chairman of the Sri Lanka Shippers' Council at that time, to

secretly endorse the document favouring shipping lines. The document was not witnessed by either the petitioning party or the respondents.

The Secretary Ministry of Shipping, realizing that this was an underhand attempt to legitimize an illegal act, appointed a new mediation committee, but after several meetings, and due to reasons unknown, the respondents who were expected to bring about a solution did not attempt to do so.

The International Chamber of Commerce (ICC), which is based in Paris, recognizing that the use of the term FOB (Free on Board) was inappropriate in the case of containerized cargo, where goods are handed over to a terminal, introduced the latest revision of the International Commercial Terms (INCOTERMS), in 2010. This provision was not contained in the previous version of INCOTERMS. The Joint Apparel Association Forum (JAAF), in association with the Sri Lanka Shippers Council lobbied for the change at meetings of the Global Shippers' Forum which were held in San Francisco, London and Montreal by personally representing the case. With the consent of the Global Shippers' Forum, the matter was submitted to the ICC's Drafting Committee which is based in Paris, for inclusion in the new INCOTERMS 2010. Having achieved this important objective, lobbying continued with the government to enact the required local legislation.

The argument put forth by shipping lines is that if the Budget Proposal is enacted, shipping lines would increase freight rates to include the THC component and other charges. They contended that if lines were successful in incorporating these charges, Sri Lanka's trading partners would have to incur higher costs to trade with Sri Lanka.

This is the central feature of the issue. Shipping lines are not required to be concerned about this. All that is required by them is to quote an all inclusive freight rate for CY to CY or CFS to CFS and recover the cost from the party which is responsible for paying the freight.. Such an action will be market friendly as shipping lines/operators will be compelled to compete on actual costs to be incurred and not by unilaterally passing part of the cost to the weaker party who does not have equal bargaining power or a contractual obligation. The buyer and the seller will adjust their prices on the basis of market and actual costs.

The Budget proposal and the ensuing enactment is meant to provide a regulatory mechanism, bring about transparency and accountability to establish fair trading practices and to avoid uncompetitive practices of stronger parties.

What is required is for shipping lines/service providers to fall in line with international practices to harness the full potential of the new legislation that has been promulgated, including the proposed merchant Shipping Authority Act, the Hub Regulation and new Inland Revenue concessions which have been granted to the shipping economy, which will boost the economic activities of shipping agents/service providers.

**An opportunity exists for Sri Lanka to “Internationalise” the initiative, by developing a case study/studies on the methodology which was employed over seventeen years and the approach which was taken, including the essential reform elements which were necessary for institutional change, technical analysis, political economy analysis and political action (in this case, the direct intervention by the President of Sri Lanka).**

Chairman  
Sri Lanka Shippers council