

Flags of Convenience

The Whys and Wherefores of Registering Vessels Under Foreign Flags

By Dave Gerr © 2013 Dave Gerr

Think of flags and ships and you may picture frigates under sail exchanging thundering broadsides until the vanquished strikes her colors. Or, perhaps, the *ruse de guerre* in which a vessel flies the flag of friendly nation until it can get close enough to fire on its foe without warning. Then, there's the skull and cross bones, the Jolly Roger, which no self respecting pirate would sail without . . . of course. There are signal flags, and courtesy flags, and yacht club and owner's burgees, and then there are flags of convenience . . . Flags of what?

It's natural to assume that a ship or boat would fly the flag of the country of its owner or the flag of its real working homeport. In fact—at least for ships and large yachts—this is seldom the case. Indeed, most ships are registered under foreign flag. Such registrations are known as flags of convenience or FOC. This is done for a number of reasons.

Advantages of Foreign Flag (FOC)

One is that the owner of the ship or yacht will usually avoid many or even all taxes on the vessel in his or her real home country. Another is that the regulations the ship or boat has to comply with may be less complex and costly than those of the true home country. For example, included in the U.S. regulations for U.S. registered (U.S. flag) vessels are requirements that three quarters of the crew be U.S. citizens and that all crew be legal U.S. residents.

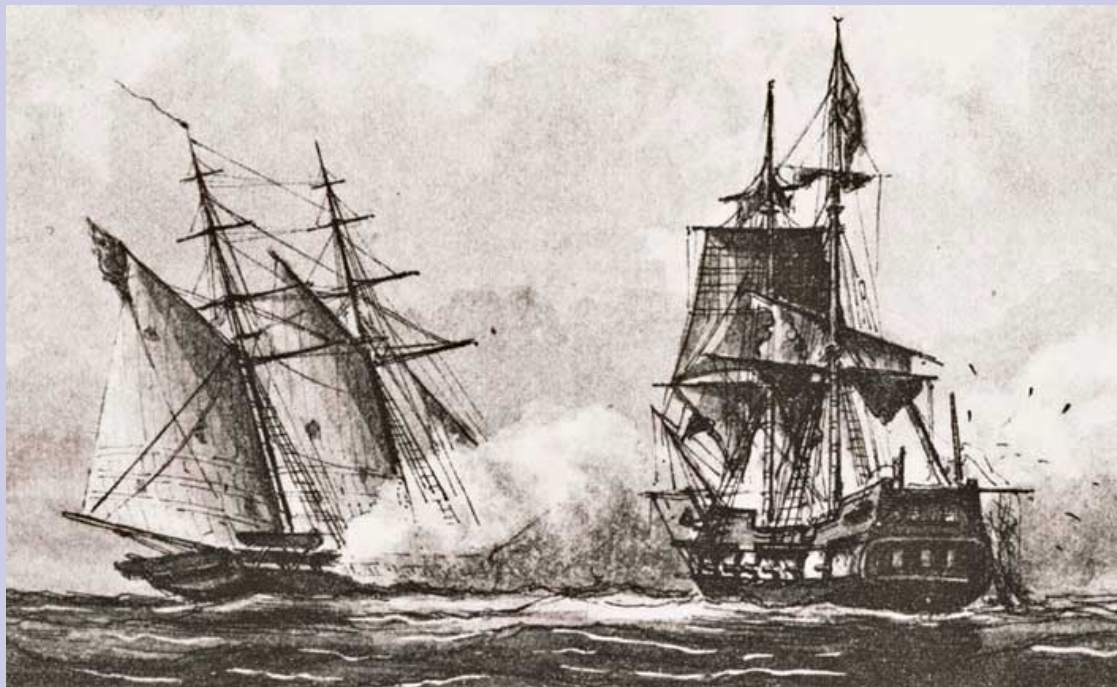
You can think of a boats registration or “flag” as its passport. A vessel

could be built in Australia, owned by a U.S. citizen, with a British captain and mate and largely Mexican and Philippine crew, but sailed under a Cayman Island flag. The boat is still considered a Cayman Island vessel wherever it goes. What's more, the wages paid to crews from various developing-nation countries are usually considerably less than U.S. or European crews command.

Regulations and Restrictions

Nations which can register boats are signers of the International Maritime Organization (IMO) and therefore technically enforce SOLAS (Safety of Life at Sea), MARPOL (International Convention for the Prevention of Pollution From Ships), and International Load Line Conventions. In practice, many (though not all) nations offering flags of convenience (foreign registry) are lax in enforcing rules and regulations, often because they lack the resources for this large and complex task. This too leads to savings for the ship or boat owner, but it can also lead to problems.

Because of the lax restrictions and enforcement on many FOC vessels, the US Coast Guard grades flags of



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convenience relative to their past experience with poor maintenance, quality control, and observation of regulations. Some FOCs are almost automatically singled out for special inspection and thus possible detention and delays on entering port. Further, these lax regulations, and the lower pay its crew may be receiving, do not make maritime or International Transport Federation (ITF) unions very happy, nor do they make for safe vessels. Using a flag of convenience is a cost saving measure and you should be aware that it can be frowned upon. (There are some shipping companies who use flags of convenience, but who do work responsibly with ITFs to ensure safe working conditions, fair wages, and proper maintenance.)



Flying the U.S. Flag

The flip side of this is FOCs whose vessels have a detention rate of less than 1% for three consecutive years. Under the Quality of Shipping for the 21st Century (Qualship 21), created in 2001, FOCs in this category meet Qualship 21, and are not likely to be singled out for

special inspection when arriving in a U.S. port. The U.K. flag is an example of a flag that can technically be used as an FOC, but which meets Qualship 21, a sign of excellent management, strong record keeping, and a commitment to safety.

Development of Flags of Convenience

Contrary to what you might expect, the U.S. has had an important part in the spreading use of flags of convenience. It was in the 1920s, when the United Fruit Company instituted the Honduran registry to reduce the cost of shipping its bananas from South America to the U.S.

U.S. Prohibition resulted in the creation of Panamanian registry in the 1920s as well. This was because U.S. flag vessels wanted to serve liquor to their passengers. The U.S. government allowed them to switch to Panamanian flag to get around the “dry” laws of the time.

As early as 1933 ITF unions began contesting transfers of ship registry to Panama. After World War II, the trend to foreign flag increased, encouraged by a low-cost surplus ships and strict, costly U.S. regulations. Panamanian registry had grown to over three million gross tons by 1948. Liberian registry increased dramatically during the Cold War. Liberia was created as a colony of freed U.S. slaves in 1821, and—chronically poor—it was seeking additional sources of revenue. At the same time, U.S. shippers, and others, needed a neutral flag to enter ports during periods of U.S./Soviet tension. In 1976 Liberian flag tonnage surpassed U.K. flag tonnage as the largest fleet in the world, though the number of tons under Liberian and Panamanian flags (and others) has fluctuated over the decades since.

Corporate Ownership

In almost all instances—to register a ship or boat under a flag of convenience—the owner sets up a corporation in the FOC country. The vessel is then registered under the corporate name. This offers two additional advantages: When an FOC boat is sold the owner can simply transfer ownership in the foreign corporation, which owns the boat, and the sale is done. This also means anonymity if it’s desired. The corporation is the legal owner of the boat, so the actual owner’s name can be hidden. It’s even possible to sell the boat without revealing the true owners personal information.

Foreign-Flag Countries

In commercial shipping two of the largest FOC countries are Panama and Liberia. Others major players are China, Malta, Singapore, and Hong Kong. For large yachts, some of the most popular registries are the Cayman Islands, Marshall Islands, and St. Vincent. These

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three offer relatively protected and inexpensive yacht registry services. As we've seen, the offshore registries require that the owner establish a corporation in their jurisdiction, and that corporation owns the vessel. The owner is the majority or controlling shareholder in the corporation. George Town, in the Cayman Islands, is a common hailing port for flags of convenience for yachts. The Cayman's are ideally located for U.S. boat owners. In Europe, The Channel Islands, Malta, and Cyprus are often used. However, any FOC country anywhere in the world can be used if the vessel's owner can meet that country's requirements.



Cayman Island Ensign

Flags of Convenience Is for Large Yachts

Most boats under 90 feet (27 m) can't justify the paperwork and complications involved in foreign registry (flag of convenience or FOC). As size increases over 90 feet (27 m) so does cost and crew requirements. Accordingly, the larger the yacht the more likely it is to use an FOC. You should be aware of flags of convenience and what advantages they may provide their boat's owners when you are working on large vessels. On superyachts, foreign flag is almost the rule rather than the exception.

Next time you see a yacht with George Town as the hailing port and the Cayman Island flag as its ensign, you'll know what it means.

Flag of Convenience Criteria

In 1970 a British committee of inquiry set down the criteria to define a flag of convenience. This is often referred to as the Rochdale Criteria. It is:

- The nation allows non-citizens to own and control vessels
- Access to and transfer from the register is easy
- Taxes on shipping income are low or zero.
- The nation of registration doesn't require the shipping tonnage for its own purposes, but is aiming to earn the tonnage fees
- Crewing by non-nationals is allowed
- The nation does not have the ability or the willingness to impose regulations on its ship owners