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of the adoption of the Final Act of the Conference of Plenipotentiaries, i.e. on April 6, 1979, it shall be convened, at the request of one-third of the states entitled to become contracting parties to the Convention and subject to the approval of the United Nations General Assembly.

Adopted Resolutions

On April 6, 1974, the Conference of Plenipotentiaries also adopted two resolutions and the Final Act of the Conference².

The Conference, in one of the resolutions, resolved that nothing in the Convention "shall be construed so as to deny shippers an option in the choice between conference shipping lines and non-conference shipping lines, subject to any loyalty arrangements, where they exist" and that, in the interest of the sound development of liner shipping service, non-conference lines should not be prevented from operating so long as they adhere to the principle of fair competition on a commercial basis.

In the other resolution, the Conference, noting that proposals had been made to submit certain types of disputes to local conciliation, requested the first Review Conference to give priority consideration to the matter of local conciliation, taking into account the views expressed by the Contracting Parties to the Convention on whether or not the absence of local conciliation has hampered the effective settlement of disputes and, if so, to consider the appropriate subjects and procedures for local conciliation.

Concluding Remarks

There can be no doubt that the Convention is a revolutionary piece of international shipping legislation, of great significance for liner conference shipping. To the extent that it is the first internationally-negotiated and internationally-agreed legal instrument for regulating the activities of what is after all a form of multinational cartel, its significance may be said to go beyond the liner conference industry. By contributing to the progressive development of in-

ternational law, it will also contribute to the building of a new international economic order, on which the UN General Assembly, recently at its sixth special session devoted to the problems of raw materials and development, has adopted a Declaration and a Programme of Action.

The Programme of Action in fact called for all efforts to be made to ensure the early implementation of the Code of Conduct for Liner Conferences³.

It remains for Governments to become contracting parties to the Convention and to take such legislative or other measures as may be necessary to implement the Code. Article 48 of the Convention provides that all states are entitled to become contracting parties to the Convention by signature subject to and followed by ratification, acceptance or approval; by signature without reservation as to ratification, acceptance or approval; or by accession.

² For the texts of the resolutions and the Final Act, see Final Act and Annexes (TD/CODE/11/Rev. 1 and Corr. 1).

³ See General Assembly resolution 3202 (S-VI), para. 4 (IV).

Flag Discrimination – A Pressing Problem

by Dr K. Reese, Johannesburg *

During the last decade private shipping companies have been under ever increasing pressure from competing state owned lines. The latter gained much ground even though the private companies, as a rule, run their ships more economically. The relative success of the state liners has rather been brought about by non-economic factors, i. e. owes much to political weapons, such as bilateralism and revitalized nationalism. The basic rule of efficient ship-

ping, as advocated by the established maritime nations of Europe, is under attack, viz. the freedom of every shipper to select whichever vessel he wants, irrespective of the flag it flies¹.

Private shipping has been and is beset by a host of "other" problems, e. g. containerization, lack of capital to push the construction of profitable specialized ships such as liquid gas tankers or oil/bulk/ore carriers, etc². All of these "other" problems are, however, relatively

easy to cope with because they are economic in nature. Real serious difficulties for private shipping only arise once the decisive variables are outside their direct sphere of influence, i. e. once the variables are political. Flag discrimination, the topic of this article, undoubtedly

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¹ J. Horn, Nationalism Versus Internationalism. In: Shipping, Journal of Transport Economics And Policy, Vol. III, No. 3, September 1969, pp. 246 and 249.

² Sea Shipping. In: Economic Quarterly Review, Industrial Kaleidoscope, Amsterdam – Rotterdam Bank, No. 27, December 1971, pp. 15 and 20-21.

is *the* most pressing political problem for private shipping; a problem which has highly unpleasant economic consequences for private shipping companies in particular and efficient low-cost sea transport in general.

Threatened Freedom of Choice

The term "flag discrimination" refers to the practice of an ever growing number of countries to reserve a certain share of their foreign trade for transportation by ships that fly their respective national flags. Unfortunately not only less developed nations indulge in this practice — arguing that their fledgling national fleets would soon be overwhelmed by the established shipping companies unless protected from free competition — but developed countries such as the USA as well threaten the freedom of international shippers to select the vessel of their choice, whichever it may be³.

The so-called Cargo Preference Act, which became law in the USA in 1954, is a good example here. This Act adds a new dimension to the Merchant Marine Act of 1936 in that it reserves for American ships at least half of all freight generated in one way or another by US government agencies. If furthermore freight has been financed by an American government agency or by the Export-Import Bank, then all of it is reserved for US ships⁴. The Japanese — to name another developed nation that joins the ranks of the flag discriminators — are imitating the USA and strive for a share of at least 50 p.c. of their foreign trade to be transported by Japanese ships. This is a very serious development for the private shipping companies, particularly as Japan has up till now been a major customer of free international shipping⁵.

³ Shipping; Don't Discriminate. In: Economist, February 10, 1973, p. 56.

The bad example set by some developed nations, such as the USA, has induced more and more less developed ones to overcome their last political inhibitions and go all out for flag discrimination⁶. To make matters worse, an ever growing number of these "new" shipping nations begins to consider a 50 p.c. share as too moderate. Brazil for example insists that a much higher percentage of its most important cash crops, such as coffee and cotton, should be reserved for Brazilian ships⁷. Another Latin American country, Argentina, is currently entangled in a dispute with Brussels because of its petty and excessive flag discrimination practices⁸.

Most of the other South American countries — as well as members of the Latin American Free Trade Association LAFTA — argue for a further tightening of flag discrimination while simultaneously agreeing on exempting one another from this practice. The aim quite clearly is to exclude the established maritime nations of Europe as far as possible from the Latin American sea freight market⁹. A decisive factor — which makes it unlikely that the flag discriminators will reconsider in the immediate future — must be mentioned in this context, viz. the over-capacity in world shipping. With the exception of specialized ships such as liquid gas tankers, world sea transport has suffered for years from an imbalance of freight volume and shipping capacity. Too many ships wait for freight and thereby depress freight rates. The extent of this over-capacity is significant indeed, viz. 1973/74 roughly 17–21 mn tons¹⁰.

⁴ Economic Quarterly Review, op. cit.

⁵ Shipping; Don't Discriminate, op. cit.

⁶ Horn, op. cit., p. 247.

⁷ Economic Quarterly Review, op. cit., p. 17.

⁸ Shipping; Don't Discriminate, op. cit.

⁹ Economic Quarterly Review, op. cit.

¹⁰ Shipping; A Grain of Hope. In: Economist, September 2, 1972, p. 64.

Prior to contemplating what can be expected to happen in flag discrimination in the future it seems useful to stress that this practice is not an invention of our most recent past but has already a "tradition". Flag discrimination as a tool of government shipping policy dates back as far as 1381 when it was devised by England¹¹. This point deserves a short discussion if only because England 1974, together with Scandinavia, belongs to those established maritime nations of Europe which suffer most severely from flag discrimination¹².

Tradition of Flag Discrimination

Flag discrimination originated in 1381 and culminated under Cromwell in 1651 when the so-called First Navigation Act of England became law¹³. Already at that time it was the economically less efficient nation — England — which used this political weapon against its more efficient economic rival — Holland. Holland in 1651 was ahead of England in terms of commercial organization and shipbuilding and without the protecting umbrella of the First Navigation Act the merchant fleet of England would have been driven off the seas by the Dutch. The First Navigation Act of 1651 and its even more stringent amendments of 1660, 1662, 1664 and 1673 firmly installed a comprehensive system of flag discrimination practices in England; a system that ensured that goods shipped to England went in English vessels with English crews. If the goods came from Europe then ships flying the flag of the country of origin, respectively shipment of these goods, could as well be used but "third parties" were totally excluded. All shipping between and

¹¹ The Encyclopedia Americana, International Edition, American Corporation, New York, 1964, p. 32.

¹² Shipping; Changing Spots. In: Economist, March 9, 1974, p. 91.

¹³ The Encyclopedia Americana, op. cit.

around the British Isles was again exclusively reserved for English ships¹⁴.

The First Navigation Act achieved its aim, even though it was a major cause for some of the wars with Holland. While the volume of England's foreign trade was split 2:1 between England and Holland in 1668 this ratio had changed dramatically to 10:1 in favour of England by 1750. Only after the philosophy of *laissez-faire* had taken hold in England and the free enterprise system had become thoroughly entrenched by about 1850 did the English ports open up again. From 1850 onward, however, England must be seen as one of the most outspoken advocates for the freedom of international shippers to select the vessel of their choice¹⁵. It is thus almost an irony of economic history that Great Britain 1974 is among the major victims of a practice perfected by itself. Today once again the economically less efficient, e.g. Brazil, are fighting with flag discrimination against the more efficient, e.g. Great Britain, and the urgent question arises of what to do.

Anti-economic Rules

There are two obvious, even though diametrically opposed "solutions" to the problem of flag discrimination, viz. to re-establish the freedom for the international shippers to choose the vessel they like or to accept flag discrimination as the international norm and to institutionalize this practice. The last "solution" has now been adopted by the United Nations and the institutionalization of flag discrimination seems inevitable. The UN is currently engaged in sorting out the anti-economic rules by which this political game shall be played. In spring

1974 the Committee of the United Nations Conference on Trade and Development (UNCTAD) adopted the suggestion to reserve 40 p.c. of the volume of foreign trade of each country for its ships. At the moment this institutionalization of flag discrimination is aimed at shipping conferences and not — not yet at least — at tramp shipping¹⁶. The trend, however, is clear.

The UNCTAD suggestion implies that a majority of the UN member nations wants to closely correlate the shipping capacity of each country and the volume of foreign trade it generates, irrespective of whether or not individual nations enjoy a natural advantage in shipping and could carry sea freight at lower cost than others. Opportunity cost is apparently no consideration when it comes to national shipping policies and the stereotype argument is often put forward that national fleets have to be expanded in order to obtain much needed foreign exchange.

This argument can, however, not be accepted blindly at face value as it is often used without a thorough cost-benefit-analysis being conducted. American studies have rather stressed that the gains in foreign exchange are more than offset by the additional cost, due to reduced efficiency, that have to be paid for in national currencies¹⁷. Only by discounting these extra cost in national currencies as irrelevant and thereby indirectly putting a premium value on foreign exchange — a scarcity value over and above the value reflected by the exchange rates — can this pseudo-economic argument possibly be made to look logical. Its shaky character stands out clearly when it is put forward by nations such as Japan and it

seems safe to allege that the true motives behind flag discrimination are closely linked to "national vanity"¹⁸.

An analogy seems to exist to representation at the United Nations and national airlines, i.e. the political shopping lists of most countries — less developed ones in particular — seem incomplete without these vestiges of national being. It becomes an obsession to be present everywhere and it thus turns into a matter of national prestige to have ships flying one's national flag in as many ports of the world as possible.

Registration under "Cheap" Flags

The UNCTAD suggestion is furthermore bound to add fuel to a related problem that has worried European shipping nations since long, viz. to the registration of ships under "cheap" flags. Relative to countries such as Panama and Liberia the taxes payable and the safety and manpower regulations to comply with are stiff in Europe; a fact that can easily be verified by looking for example at the German SBAO — Schiffsbesetzungs- und Ausbildungsordnung — of 1970 and the corresponding legislation in Panama. Thus it has been a rather widespread practice in recent years to register European ships under these "cheap" flags and thereby cut cost considerably.

The registration under "cheap" flags has of course had no effect whatsoever on managerial control, i.e. a German ship which now flies the Liberian flag is still under German control. The usual practice is to set up branch offices in say Liberia which nominally now own the ships while the parent company in Germany manages them as sole agents. Another usual arrangement is to find some front

¹⁴ H. Heaton, *Economic History of Europe*, New York, 1948, pp. 276-277, 326-328 and 391.

¹⁵ Ibid.

¹⁶ Shipping; Changing Spots, op. cit., pp. 91-92.

¹⁷ Horn, op. cit., p. 248.

¹⁸ Shipping; Don't Discriminate, op. cit.

man in Liberia who "buys" the ships and then to charter them back at reduced cost ¹⁹.

As mentioned above, the UNCTAD suggestion will certainly add fuel to this process of re-registration of shipping capacity but simultaneously a new dimension will be added in the sense that it will be much more difficult to register under another flag and retain managerial control in European hands. After all, the flag discriminators are nationalists and will hardly be content to add to the list of "cheap" flags, so widely used to avoid taxes and inconvenient safety and manpower regulations. The nationalistic flag discriminators are bound to insist that the registration of say a German ship in Brazil entails full managerial control by Brazilians; a new dimension which will make re-registration of ships much less easy to stomach for their European owners.

A closer look at the UNCTAD suggestion reveals its rather simplistic basic idea as mentioned above, viz. to closely correlate the share of world shipping capacity registered in the respective country and the share of world trade that is generated by that country. On the basis of this simplistic idea an equally simplistic redistribution scheme of world shipping capacity can be devised, as done below, which will illustrate the far-reaching implications of fully adopting the UNCTAD approach to world shipping.

A Simplistic Scheme

The adoption of the UNCTAD approach to world shipping would result in a shift of shipping capacity from Europe, mainly to the less developed nations of the world. Such a shift would come to an end only once the respective national

shares of world shipping capacity are in equilibrium with the respective shares of world trade generated. Today this is not so. Britain for example only generates 11 p.c. of world trade while about 28 p.c. of world shipping capacity is registered in Britain. The other established maritime nations of Europe are equally out of step. Norway, to name another, generates a meagre 9 p.c. of world trade while 24 p.c. of world shipping capacity is registered in that country ²⁰.

A redistribution scheme à la UNCTAD would thus call for an agency which firstly would have to compute the total volume of shipping capacity to be redistributed. The established maritime nations of Europe would then have to transfer part of their merchant fleets to some sort of "redistribution pool" out of which secondly those countries would receive shipping capacity which generate a larger share of world trade than their present share of world shipping capacity. The idea is easily demonstrated by once again referring to Britain and Norway. Britain would have to transfer 17 p.c. of its shipping capacity to the "redistribution pool" because it generates only 11 p.c. of world trade compared to the 28 p.c. of world shipping capacity registered in Britain, as outlined above. Norway by analogy would have to part with 15 p.c. of its shipping capacity (24-9). The sum total of all these transfers of shipping capacity — 17 p.c. of the British merchant fleet plus 15 p.c. of the Norwegian, etc., — would then make up the "redistribution pool" out of which the countries presently "under-represented" in world shipping would be satisfied. Take for example a less developed country which generates 15 p.c. of world trade but has only 5 p.c. of world shipping capacity registered under its

national flag. Such a country could now claim 10 p.c. (15-5) of the shipping capacity amassed in the "redistribution pool". A simplistic scheme indeed.

Triumph of National Vanity?

Such a redistribution scheme would most probably be classified as "fair" by the flag discriminators but would as well be the death knell to an efficient low-cost world sea transport, quite apart from the tricky problem of the then necessary annual corrections of national shares of world shipping capacity, in view of potentially rapid shifts in the respective shares of world trade generated and the almost never ending redistribution of shipping capacity that this entails. Efficient low-cost world shipping, an economic goal par excellence, would have been sacrificed for good on the pedestal of national vanity. The freedom of international shippers to choose the vessel of their choice, irrespective of the flag it flies and low-cost world sea transport are truly inseparable twins.

The chances to stem the tide and guarantee the freedom of choice of vessel for the international shippers seem bad indeed but nevertheless all possible steps should be taken to avoid the worst, i.e. prevent that national vanity completely excludes economic considerations from the formulation of national shipping policies. Hope can be drawn from economic history, provided the institutionalization of the UNCTAD approach in its most rigid form can be prevented now. England in 1850 eventually overcame its flag discrimination mentality and by analogy one can expect that today's flag discriminators will as well "grow up" as time goes by and take a fresh look at the merits of the efficient low-cost world sea transport offered by the private shipping companies.

¹⁹ Schiffahrt; Fünfte Kolonne. In: Der Spiegel, No. 16/1973, pp. 54 and 57.

²⁰ Shipping; Don't Discriminate, op. cit.