

Executive summary

LEVEL PLAYING FIELD FOR SUSTAINABLE SHIPBUILDING

Challenges and proposals

2022



La Fundación MarInnLeg se crea para generar, gestionar y transferir conocimientos jurídicos marítimos y pesqueros mediante asesoramiento, formación, un observatorio y apoyo a la investigación académica. Es la mejora de ese conocimiento la que sentará las bases sobre las que estimular la innovación, el desarrollo y el crecimiento económico a medio y largo plazo.

PATRONATO PÚBLICO-PRIVADA DE LA FUNDACIÓN MARINNLEG



MARINNLEG
EDIFICIO DE SESIONES, 1º PLANTA

MUELLE DE TRASATLÁNTICOS

36210 VIGO (PONTEVEDRA)

www.marinnleg.org

info@marinnleg.org

Autora del informe: Annina Cristina BÜRGIN
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STRATEGIC IMPORTANCE OF SHIPBUILDING

It is a historical fact that ships are strategic assets - and remain so because they are indispensable for a wide range of blue economic activities such as maritime transport, marine resource extraction, security and defence or for the generation of marine renewable energies. The shipbuilding sector in sensu lato will also be key in the (near) future as a strategic driver in the green and digital transition by contributing substantially to the fight against climate change through the development of new propulsion systems reducing greenhouse gas (GHG) emissions, bringing innovations to sustainable ocean exploration and exploitation, marine renewable energy installations, oceanographic research, etc.

The strategic value of ships and the high degree of internationalisation of the whole sector are the reasons why some countries have an industrial policy that gives the sector a key role. In many cases, however, these policies do not favour fair competition but are rather protectionist and market-distorting, which is why PÉREZ GARCÍA points out that in shipbuilding "[t]he normal conditions of competition typical of an open market have never existed". European companies are exposed to strong international competition which is often distorted by state interventions resulting in them not being able to produce on a level playing field with their international competitors. By way of example, the following state barriers faced by European companies in third countries are worth noting:

- All types of massive state subsidies (direct and indirect)
- State-owned / State-controlled enterprises (SOE)
- National or local content purchase requirements
- Discriminatory product classification/approval procedures
- Import substitution
- Forced technology transfer
- Investment barriers
- Obligation to create joint ventures
- Exclusion from a public procurement procedure
- Exclusion from state-linked financing modalities

Many of the restrictions limit business activity or the requirements are difficult to meet. In some countries this is the result of a position of undisputed protectionism that is at odds with European Union (EU) trade policy in two respects. In the internal market itself, there is a strict competition law to which EU operators are subject in order to ensure fair competition, while external

trade relations are characterised by a stance of openness (foreign trade accounts for almost 35% of GDP, and the value of foreign direct investment accounts for 40% of GDP). What this means in practice is that companies from a certain country with extensive restrictions can easily invest and/or trade with the EU, while EU companies face obstacles of all kinds in the same country. That said, it is important not to misunderstand that a return to greater protectionism would be desirable, but to stress that the **absence of reciprocity and the consequent lack of fair competition leads to the undermining of a level playing field.**

Specifically, **a level playing field in the blue sectors**, whose production chains are extremely internationalised and complex, **encompasses all production factors** such as environmental standards, state aid, trade conditions, tax policies or labour conditions. Discrepancies in just one of these factors can lead to unfair treatment between products from different origins. Moreover, it also jeopardises sustainability in its three dimensions, i.e. the economic, social and environmental sustainability of an entire sector. It is important to point out that no state or the EU itself can demand that other states have exactly the same set of rules because there are, of course, major social or economic differences. The **point of reference must be international law** because it is international treaties that set internationally accepted rules and guarantee a lowest common denominator of standards, regardless of whether it is a question of fundamental protection of workers or guaranteeing environmental standards. The international legal framework sets the ground rules, providing legal certainty and ensuring peaceful international relations. Demanding compliance with international conventions is the only way to achieve a level playing field - otherwise differences lead to imbalance and severely disadvantage those who abide by the rules.

Contribution of the shipbuilding sector to the **SUSTAINABLE DEVELOPMENT GOALS:**

SDG 7 Affordable and Clean Energy

* Decarbonisation of the maritime sector. All kinds of innovations to decarbonise the maritime sector.

* Support to lower carbon emissions. IMO supports projects in developing countries to promote capacity building to address maritime energy efficiency.

SDG 8 Decent Work and Economic Growth

* Building safer and more habitable ships. In accordance with international standards such as compliance with ILO C-188 or Maritime Labour Convention (MLC, 2006).

SDG 9 Industry, Innovation and Infrastructure

* Sustainable Blue Growth in multiple senses, among others:

- Contributing to a more interconnected, efficient and robust/resilient supply chain.
- Intermodal links and connection to the hinterland
- Sustainable fisheries
- Offshore energy production
- Tourism
- Port handling
- Autonomous ships

SDG 12 Responsible Consumption and Production

* Waste management on ships. In accordance with international standards (London Convention and Protocols), construction of sustainable waste management systems on board to prevent water pollution from waste disposal.

* Ship recycling. The sector contributes to ship recycling e.g. through ship conversion activities to give ships a new lease of life; support the implementation of international standards such as the Hong Kong International Convention for the Safe and Environmentally Sound Recycling of Ships (IMO, 2009).

SDG 13 Climate Action

* Innovations for greater energy efficiency. The sector contributes with innovations to promote the use of alternative propulsion systems such as the use of LNG.

* Reducing greenhouse gas (GHG) emissions. The shipping sector was the first industry sector that had to comply with mandatory norms and standards to lower GHG emissions developed by the IMO.

SDG 14 Life Below Water

Improve safety, security and efficiency of maritime activities. Improve the safety of ships to prevent accidents, reduce their impact on biodiversity through the reduction of all types of emissions (including noise), contribute to a sustainable use of marine resources (e.g. fishing vessels with more selective fishing gear, safe offshore vessels, etc.),

development of collision prevention systems (including between ships and marine mammals), waste management, etc.

INTERNATIONAL STANDARDS and their (NON)COMPLIANCE

A rich international regulatory framework is in place and will be even more so in the future. The **value chain of ship production, repair and marketing is extensively regulated by a set of rules at national, EU and international level.** There are sectoral rules as well as cross-cutting regulations, such as labour, environmental or taxation rules, which condition shipbuilding.

The most important international regulations affecting the level playing field in shipbuilding can be categorised into 3 groups:

- In the field of **SAFETY and ENVIRONMENT** the International Maritime Organisation (IMO) plays a key role. In relation to shipbuilding *sensu lato*, there are 3 essential Conventions which are SOLAS, MARPOL and the Training Convention (1995). In addition, there are at least 25 other Conventions which are mainly grouped into the following categories:
 - Maritime safety and security (10 conventions)
 - Prevention of marine pollution (7 conventions)
 - Liability and compensation (8 conventions).
- In the area of **WORKING CONDITIONS**: the reference framework are the fundamental treaties drawn up by the International Labour Organisation (ILO), which are 12 fundamental conventions and 8 governance conventions.
- In the area of **TRADE**, the World Trade Organisation (WTO) is the lead organisation, and it is worth highlighting the set of standards it has developed in recent years around the **Marrakesh Agreement**. The **Multilateral Agreements on Trade in Goods** are binding on all WTO Members (**14 Conventions**, e.g. GATT). However, **Plurilateral Trade Agreements** are only binding on Parties that have accepted the Agreement in question. This is the case for the **Government Procurement Agreement (GPA)** which binds 21 Parties - 1 of which is the EU itself and thus makes a total of 48 parties - at the moment China, Russia and Turkey are only observers.

From an international law point of view the following **4 realities cause the lack of a LEVEL PLAYING FIELD:**

(1) ... There are agreements that are not ratified by all and this imbalance in the ratification of international treaties means that states that have ratified them are self-limiting by accepting more restrictions. This results in higher production costs and, consequently, in a situation where there is a lack of a level playing field.

(2) ... And although states have ratified agreements, there are **breaches of the established rules**. For example, in the WTO framework, Japan communicated in February 2020 a request for consultations with the Republic of Korea on a series of measures "affecting trade in commercial vessels". Japan specifically accuses Korea of granting state aid with apparently distorting effects, which is prohibited under the WTO Agreement on Subsidies and Countervailing Measures to which both states are parties.

(3) ... In the event that a party to an agreement violates common rules, there are mechanisms in place to mechanisms exist to complain about violations. Unfortunately, **many international procedures are ineffective for specific shipbuilding cases** in remedying the damage caused by a violation. The ineffectiveness of trade or investment defence instruments is due to the fact that they are inoperable due to the specific characteristics of shipbuilding. As an example, it should be noted that - even if an award is made in favour of the company that has suffered injury from a prohibited subsidy and it is decided that, for example, the offending state has to withdraw the injurious subsidies, such an outcome is irreversible because, as mentioned above, in most cases the construction of a ship is a one-off event and it is very likely that no more identical ships will be built in the future.

(4) ... In addition, there are still legal loopholes at international level which result in each State applying its own national policies and rules contributing to a lack of a level playing field.

PROPOSALS to ensure a *LEVEL PLAYING FIELD*

Ensuring, and sometimes re-establishing, a level playing field for the EU and its businesses **is important because**

- without international rules, the achievement of common goals of international society, such as the fight against climate change, is highly questionable,
- the European Union must ensure its strategic autonomy and self-sufficiency, and this can only be achieved with a strong industry at the forefront of the latest innovations, and
- the socio-economic sustainability of the European business fabric must be protected.

To this end, this study makes PROPOSALS to strengthen the regulatory framework and, in the case of unfair practices, to provide instruments to remedy distortive effects to the detriment of European sectors. A selection of proposals is presented below:

1) In relation to the presence of powerful **state-owned enterprises (SOEs)**, the EU should

→ **promote the OECD recommendations on competitive neutrality** adopted in 2021 in general, and more specifically when signing trade agreements to reinforce competitive neutrality and its application, and consequently ensure a true level playing field.

→ consider creating a **Complaints Office on Competitive Neutrality** at EU level to allow legal entities to communicate their observations of market events through easy tools.

2) As regards the frustrated OECD Agreement on Normal Competitive Conditions in the commercial shipbuilding and ship repair sector, the EU should

→ Within the framework of the OECD, the **EU should push for a new discussion on an agreement to ensure competition rules in shipbuilding**. It should be noted (!) that a new agreement would be needed and not just a revival of the 1996 agreement because it is totally outdated.

→ **amend Regulation 2016/1035 on protection against injurious pricing practices in shipbuilding and decouple it** from the entry into force of the OECD Agreement.

3) The EU should continue to promote an **Environmental Goods Agreement** which, apart from trade benefits, would be a recognition of the strategic importance, effort and innovation of the shipbuilding sector for sustainable development.

4) The EU should continue to actively promote in the UN framework the creation of a **Multilateral Investment Court** which would not only contribute to increase legal certainty for all investors but also strengthen the level playing field by establishing a common set of rules for the settlement of investment disputes.

5) The EU should **consistently apply the amended Regulation (EU) No 654/2014 and thus respond to breaches by third States** to ensure a level playing field at international level.

6) The assessment made in the Trade Barriers 2020 Report is shared, whereby the **EU should act forcefully against local content requirement (LCR) practices.**

7) In line with SEA Europe's ideas, the EU is invited to consider the possibility of

- creating a system of aid linked to the greening of the fleet
- establishing a temporary tax reduction scheme to promote the maritime side of the implementation of the European Green Pact.