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Inside This Issue

THE PASSENGER VESSEL SAFETY ACT OF 1993 AND THE RISKS OF RECREATIONAL VESSEL CHARTERS

By Theresa Bennett*

The sharing economy and the desire to monetize pleasure vessel ownership has spurred increased U.S. Coast Guard enforcement of vessel charter and inspection regulations. Through ignorance, mistake or design, many recreational vessel owners run afoul of coastwise trade laws by impermissibly carrying passengers for hire in violation of the Passenger Vessel Safety Act of 1993 (PVSA). Such violations carry stiff penalties, and repeated violations can result in criminal prosecution and vessel forfeiture. This article summarizes the history of the PVSA as applied to recreational vessel chartering; reviews USCG recent crackdowns on illegal charters; explains how PVSA regulations are typically violated; and outlines the various fines and penalties triggered by illegal charters.

Understanding the exposure to USCG fines and penalties first requires a discussion of the Passenger Vessel Safety Act of 1993 and its application to pleasure vessels.

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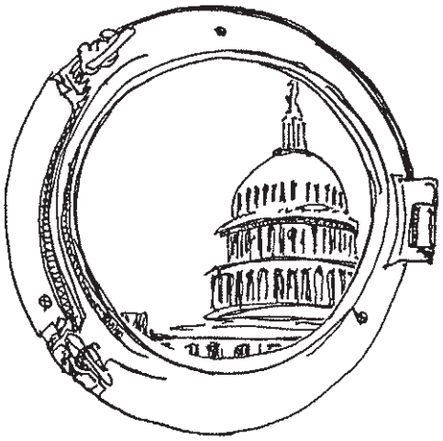
WINDOW ON WASHINGTON



READY, SET, IMO 2020!

Bryant E. Gardner*

Effective January 1, 2020, MARPOL Annex VI amendments adopted by International Maritime Organization (IMO), which reduce global marine fuel sulfur limits from 3.5% to 0.5%—an 86% reduction, will come into effect.[1] From that date, vessels will need to operate on more expensive low sulfur fuels, or operate with exhaust gas scrubbers. And effective March 1, 2020, vessels will not be permitted to carry fuel for use on board the ship in excess of 0.5% sulfur content.[2] Although Emission Control Areas (ECAs) requiring sulfur limits of 0.1% have been in effect in some areas for several years, IMO 2020 is a major change with significant issues for everyone involved with the maritime industry. Questions abound regarding compliance options, fuel availability and global fuel market impacts, allocating compliant fuel costs among shippers and carriers, implementation timelines, enforcement, and other legal issues.

The IMO announced the transition to 0.5% fuel in October 2016, and immediately carriers, refiners, and bunker suppliers began plans to meet the deadline. In the fall of 2018, the Trump Administration suggested that there would be an "Experience Building Phase" to gradually transition to compliance, in lieu of a hard start on January 1, 2020. However, the IMO's Marine Environment Protection Committee (MEPC) rejected the proposal, and the Administration ultimately backed away from it as well. Faced with a potential U.S.-led defection from the planned start date, refiners, oil producers, carriers, labor, and other U.S. domestic interests mobilized through the Coalition for American Energy Security, which continued to press for on-time implementation through 2019.[3] In April 2019, a group of

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[1] Marine Environment Protection Committee, International Maritime Organization, Effective Date of Implementation of the Fuel Oil Standard in Regulation 14.1.3 of MARPOL Annex VI, Resolution MEPC.280(70) (Oct. 28, 2016). "MARPOL" is the common short-hand for the International Convention for the Prevention of Pollution from Ships, 1973, as Modified by the Protocol of 1978 Relating Thereto.

[2] Marine Environment Protection Committee, International Maritime Organization, Prohibition on the Carriage of Non-Compliant Fuel Oil for Combustion Purposes for Propulsion or Operation on Board a Ship, Resolution MEPC.305(73) (Oct. 26, 2018) (Annex).

[3] Coalition for American Energy Security, https://americanenergysecurity.com/. Members include, *inter alia*, the American Petroleum Institute, United Steel Workers, American Fuel and Petrochemical Manufacturers, World Shipping Council, Valero, the Center for Liquefied Natural Gas, and the Domestic Energy Producers Alliance.

14 Republican Senators, many from states leading in oil production and refining, wrote to President Trump urging support for IMO 2020, stating "The U.S. is well-positioned to benefit from these standards, because we are already the world's leading producer of low-sulfur fuels. Additionally, many foreign refiners lack the complexity required to process heavy crude oil into IMO-compliant fuel and could turn to U.S.-produced low-sulfur crude, increasing domestic oil exports."[4]

A June 2019 economic analysis of the U.S. economic benefits of IMO 2020, produced by Charles River Associates for the Coalition for American Energy Security, concluded that the shift to low-sulfur fuel will not impact gasoline prices, will increase diesel prices by no more than 2% citing the U.S. Energy Information Administration (EIA), will benefit U.S. refiners, and that "of the non-energy sectors in the U.S., only the relatively small marine transportation sector sees an economic output change greater than 0.2% in either direction."[5] Additionally, the study concludes that petroleum product prices are more sensitive to crude market developments than to changes in IMO 2020 implementation levels, noting a 19% price drop from 2018 to 2019 in diesel, compared with the 2% impact expected by the EIA in connection with IMO 2020. Much of the additional literature put out by the Coalition supports the notion that the refining industry will be adaptable enough to meet demand without major economic or operational disruption, referencing EIA findings and the capability shown by the industry when road transport fuel regulations tightened with a focus on sulfur content, and touting the substantial investments made by the industry to meet expected demand.

Many in the maritime sector remain deeply concerned about the transition and how best to navigate the rocks and shoals of implementation. Planning the lead-up to IMO 2020, shipowners face the decision of installing scrubbers or operating with compliant fuels. Each alternative has its pluses and minuses. Operating with compliant fuel appears to be the favored approach as of this writing. Compliant fuel has been estimated to cost approximately 55-65% more than high sulfur fuel oil (HFSO). There are multiple solutions to achieve compliant fuel, including: very-low sulfur fuel oil (VLSO) which has sulfur content of 0.5% or less; ultra-low sulfur fuel oil (ULSFO) which has a sulfur content of 0.1% suitable for ECAs; distillates such as marine gasoil (MGO), which may have sulfur content below 0.1% but can have sulfur content up to 1.5%; or switching to vessels capable of operating on liquefied natural gas (LNG).

Vessel owners and operators are acutely concerned about the availability of compliant fuels—especially during the initial transition phase when many fear there may be shortages or price spikes. Additionally, owners fear that compliant fuels may not be available at more remote ports off of major trade routes. Perhaps most of all, owners facing already-thin margins are struggling with whether, and to what extent, they will be able to pass-on a 50% or more fuel cost increase to shippers through some kind of premium bunker adjustment factor (BAF) and how long that will take, particularly given various contracts of affreightment or service contracts with fixed rates which may tail into and past January 1, 2020. Finally, because marine gasoil and other distillates are relied upon by non-marine users such as long-haul trucks and rail, and by inland waterways users, these markets are also concerned about the impact of a massive uptick in marine use effective 2020. Currently, distillates count for less than 25% of the marine sector, and so a large shift to those fuels would set-up a collision with other users. However, because VLSO is cheaper than MGO, that seems less likely than many have posited.

Scrubbers pose different challenges. Initial costs to install scrubbers have been reported to range between $2 million and $10 million. Obviously, the choice of whether to install scrubbers depends in part upon the economics of the vessel in question: Its age, size, and trade in particular. Many have opined that it will be more difficult to allocate scrubber costs between owners and charterers and between shippers and operators. The choice of whether to install scrubbers is a classic prisoner's dilemma—if few owners install them, then LSFO demand will be high and the scrubbers will return the investment quickly, but if everyone installs scrubbers then there will be less fuel market disruption and it will take longer to return the investment.

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[4] Letter from Senators Cassidy (R-LA), Inhofe (R-OK), Wicker (R-MS), Portman (R-OH), Kennedy (R-LA), Capito (R-WV), Hoeven (R-ND), Rounds (R-SD), Cramer (R-ND), Cotton (R-AR), Boozman (R-AR), Lanford (R-OK), Scott (R-FL), and Young (R-IN), to President Trump (April 29, 2019).

[5] Charles River Associates, Economic Analysis of IMO 2020: The Benefits to the U.S. Economy of Full Participation and Compliance (June 2019).

Although, as stated above currently the favored approach appears to be compliant fuel by a substantial margin. This, in turn, raises another novel fear: If the vast majority of owners migrate to compliant fuel, will the presumption of today's pre-IMO 2020 HSFO availability and price range still be true at bunker ports going forward? Some owners have gone all-in for scrubbers, others all-in for compliant fuels, and others—including liner operators and other large fleets—are relying on a mix to help spread risk. Trade press estimates have suggested that no more than 5% of vessels will be fitted with scrubbers. Many very- and ultra- large crude carriers are reported to be relying upon scrubbers because the economics of long-haul journeys and large vessels sizes make them more palatable, purportedly leading to increases in rates for these tankers in the second half of 2019 and into early 2020 as many of them spend time in the yards for the outfit. It seems that many owners are taking a wait-and-see approach.

Scrubbers present other problems as well. Scrubbers take up space, and some captains have reported difficulty with aft visibility from the bridge, leading to camera installations to compensate. There are additional concerns regarding scrubber impact on power availability and maneuverability, with some experts opining that scrubbers may cause as much as a 5% loss in power—which may cause problems with speed and consumption warranties in charters, and further erodes the purported environmental benefit of the low sulfur requirement. Owners also must decide whether to install closed-loop or open-loop scrubbers. Open-loop scrubbers rely upon the circulation of seawater, although they have tended to have problems operating in fresh or brackish water. Closed-loop scrubbers rely upon contained freshwater treated with chemicals. A growing list of ports, including Singapore, much of China, and Fujairah, have begun banning scrubber wastewater discharges, which may present problems for open-loop scrubbers, although those vessels presumably will be able to rely upon VLSO kept on board for ECA purposes when in these ports. In the U.S., scrubber wastewater discharges are regulated by individual states, often through their permitting authority under the Clean Water Act and are generally spelled-out in the Vessel General Permit (VGP). The California Air Resource Board bans scrubber use entirely. Because vessels outfitted with scrubbers will still have HSFO on board, there are likely greater enforcement risks associated with failures to change-over or operate the scrubber due to break-downs or operational or economic incentives, or for there to be recordkeeping and sampling issues which may trigger additional penalties arising out of alleged false statements to government investigators and associated conspiracy or obstruction of justice charges.

Industry observers have expressed a wide range of views about what the future of IMO 2020 enforcement will look like as it comes into effect, although consistent with other areas of MARPOL, enforcement will likely be led by port states such as the U.S. and Europe. On the one hand, some in the industry fear that Annex VI will become the new Annex I—in other words, that the stack and scrubber will become the new "magic pipe" resulting in a surge of civil and criminal prosecutions for violations of MARPOL (or the port or flag state's domestic enactment) or the companion recordkeeping violations which have been such fertile ground for the U.S. Department of Justice over the last two decades.[6] On the other hand, in the U.S., where the North American ECA has been in place for over three years, the U.S. Coast Guard and a number of other observers have suggested that the enforcement of IMO 2020 will look little different than the enforcement of the current ECA, since that requirement is more stringent anyway and vessels calling the U.S. are already used to managing switch-over to compliant fuel, and associated record-keeping of bunker notes, etc. The Coast Guard, for its part, has indicated that the more significant date, from its perspective, is the March 2020 deadline after which vessels will no longer be able to carry HSFO on board unless fitted with a scrubber. The service does not anticipate issuing new regulations to address IMO 2020, other than some operational guidance to the local Captains of the Port regarding the handling of situations in which vessels are caught with non-compliant fuel on board, i.e., can it be ordered off, where will it go, etc.

Despite the industry angst, leadership in the Coast Guard have opined that they do not expect there to be significant fuel availability issues—at least in the U.S.—referencing the ECA implementation in 2015 and significant refinery upgrades. Previously, EPA and the Coast

[6] These Annex I cases have generally revolved around failures to properly manage and discharge engine room wastes, including oily bilge and sludge from on-board fuel purification, and the use or failure to use the oil water separator or the incinerator, and related failures to keep an accurate oil record book.

Guard had developed a Fuel Oil Non-Availability Report (FONAR) for use in reporting instances of non-availability of compliant fuel under Annex VI Reg. 18.2.4, but effective June 28, 2019, the Coast Guard announced the end of FONARs and directed industry to instead self-report non-availability to the appropriate Captain of the Port.[7] Contrary to some perceptions, the FONAR never was a "get out of jail free" card—merely a means of self-reporting non-compliance. The elimination of the FONAR helps erase this misconception. The Coast Guard expects appropriate voyage planning to ensure access to compliant fuel, without consideration of economic factors. Speaking before the Connecticut Maritime Association in April 2019, Admiral John Nadeau, Assistant Commandant for Prevention Policy, expressed some concern that the cost differential between compliant and non-compliant fuel could be an incentive not to comply, and concern over how to manage "de-bunkering" of non-compliant fuels during the transition period.[8]

As a yardstick for what IMO 2020 may have in store for the industry, North American ECA enforcement has been a lot tamer than what the industry witnessed under Annex I. Consistent with other areas of MARPOL enforcement, the U.S. Coast Guard generally is the one out on the deck plates on the front line of Annex VI enforcement. For more serious allegations, the Coast Guard will refer the case to the U.S. Environmental Protection Agency (EPA), or potentially to the U.S. Department of Justice for prosecution.[9] In the first three and a half years of the North American ECA, the Coast Guard found approximately 80 deficiencies leading to over a dozen enforcement actions, leading to civil fines which have tended to be in the tens of thousands of dollars' range, as opposed to the multi-million dollar fines seen in the Annex I cases. One exception, however, is the *Ionian Shipping & Trading Corp.* case,[10] which appears to be the first reported criminal prosecution of an ECA violation. The parties entered into a settlement in April 2019, relating to allegations that a Panamanian-flagged vessel transferred petroleum cargo to bunker tanks, failed to maintain an accurate record book reflecting the transfer, and maintained false bunker notes evidencing low sulfur fuel loading when in fact the vessel was bunkering from her cargo tanks. The United States alleged that the owner and operator obstructed justice in violation of 18 U.S.C. § 1505 by falsely stating that the vessel had taken on low-sulfur fuel, and instructed lower level crew members to lie as well. The defendants pled to violations of the Act to Prevent Pollution from Ships (APPS),[11] the U.S. domestic enactment of MARPOL, and obstruction of justice, resulting in a fine of $1.5 million each, four years' probation, implementation of an environmental

[7] U.S. Coast Guard, New Procedure for Shipping Industry to Notify the U.S. Government of Non Availability of Compliant Fuel Oil, Marine Safety Information Bulletin, MSIB No. 005-19 (June 28, 2019). Notably, the notice indicates "There is no specific format at this time for a FONAR. Until the International Maritime Organization (IMO) adopts one, it is suggested ships use the format provided in the Annex to PPR 6/8/2 ('Consistent Implementation of Regulation 14.1.3 of MARPOL Annex VI: Proposed Template to report compliant fuel oil non-availability')."

[8] Coast Guard Maritime Commons, https://mariners.coastguard.dodlive.mil/2019/04/03/4-3-2019-cma-shipping-2019-keynote-remarks-on-countdown-to-compliance-of-imo-2020/ (April 3, 2019).

[9] The Coast Guard and the EPA operate under a 2011 Memorandum of Understanding governing cooperation and referral of Annex VI cases. Memorandum of Understanding Between the United States Coast Guard and United States Environmental Protection Agency Regarding Enforcement of Annex VI as Implemented by the Act to Prevent Pollution from Ships (June 27, 2011). *See also* U.S. Environmental Protection Agency & U.S. Coast Guard, United States Coast Guard and United States Environmental Protection Agency Revised Protocols on Referrals Under MARPOL Annex VI as Implemented by the Act to Prevent Pollution from Ships (Mar. 4, 2015); U.S. Environmental Protection Agency, Interim Guidance on the Non-Availability of Compliant Fuel for the North American Emission Control Area (June 26, 2012); U.S. Coast Guard & U.S. Environmental Protection Agency, MARPOL Annex VI Air Pollution Prevention Requirements (June 27, 2011); U.S. Coast Guard, Guidelines for Ensuring Compliance with Annex VI to the International Convention for the Prevention of Pollution from Ships (MARPOL) 73/78; Prevention of Air Pollution from Ships, CG-543 Policy Letter 09-01 (Feb. 4, 2009).

[10] Plea Agreement, *United States of America v. Ionian Shipping & Trading Corp.*, No. 1:19-cr-009 (April 23, 2019, D.V.I.).

[11] 33 U.S.C. § 1908.

compliance plan, and a $1600 "special assessment." The case is noteworthy because the Government brought charges against not just the technical operator and the Chief Engineer, but also against the owner, the commercial manager, the Master, and the Chief Officer. Moreover, the case demonstrates that, as with Annex I "magic pipe" cases, the harshest penalties will likely be doled out to those who actively try to deceive the U.S. authorities. Owners and operators need to be vigilant over their air emissions compliance, particularly as the regulated community adjusts to the new IMO 2020 regime over the next couple of years.