

# Legal Briefing

Sharing the Club's legal expertise and experience

**A quick overview  
of maritime  
cabotage regimes**



## Authors

### Alexander Geoghegan

Claims Executive



Alexander joined Thomas Miller in October 2016, shortly after completing his degree in History. He is currently working in London Syndicate J1.

Direct +44 20 7204 2409  
alexander.geoghegan@thomasmiller.com

### Kelvin Lam

Senior Claims Executive



After graduating in shipping technology from Hong Kong Polytechnic University, Kelvin worked for a firm of average adjusters and P&I

correspondents before joining Thomas Miller in 2005. He holds a LLB and handles P&I and Defence claims. Kelvin speaks Cantonese and Mandarin.

Direct +852 2832 4418  
kelvin.lam@thomasmiller.com

## Legal Briefings Team

### Jacqueline Tan

Legal Services Manager



Jacqueline is a lawyer handling P&I and FDD claims. She is also responsible for coordinating the production of contractual, legal and regulatory advice for the UK P&I Club's Members. Jacqueline speaks Hokkien, Malay and French.

Direct +44 20 7204 2118  
jacqueline.tan@thomasmiller.com

### Dr Chao Wu

Legal Director



Chao leads the Clubs' Legal and Environmental team. She is responsible for the legal aspects of Club documentation and cover for Members' contractual arrangements, the Club's Rules and Bye-Laws and general legal advice.

Direct +44 20 7204 2157  
chao.wu@thomasmiller.com

# Sharing expertise

This briefing is one of a continuing series that aims to share the Club's legal expertise with our Members. A significant proportion of the expertise in the Managers' offices around the world consists of lawyers who can advise Members on general P&I related, legal, contractual and documentary issues. These lawyers participate in a virtual team, writing about topical issues under the leadership of our Legal Director, Chao Wu.

If you have any enquiries regarding the issues covered in this briefing, please contact the team via Chao Wu (chao.wu@thomasmiller.com or +44 20 7204 2157) Or Jacqueline Tan (jacqueline.tan@thomasmiller.com or +44 20 7204 2118) and we will be pleased to respond to your query. The team also welcomes suggestions from Members for P&I related legal topics and problems that would benefit from one of these briefings.

#### Previous issues

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# Maritime cabotage regimes

A quick overview of the laws and regulations governing the maritime cabotage trades in China, India, the United States, Argentina, Brazil, Colombia and Peru.

Maritime cabotage is defined as the sea transport of passengers and goods between two sea ports located in the same country.

Coastal trade, particularly in archipelagic countries and countries with long coast lines can be an important and lucrative trade. It is therefore unsurprising that countries try to restrict the commercial transportation of goods and services between their ports and islands to nationally owned vessels.

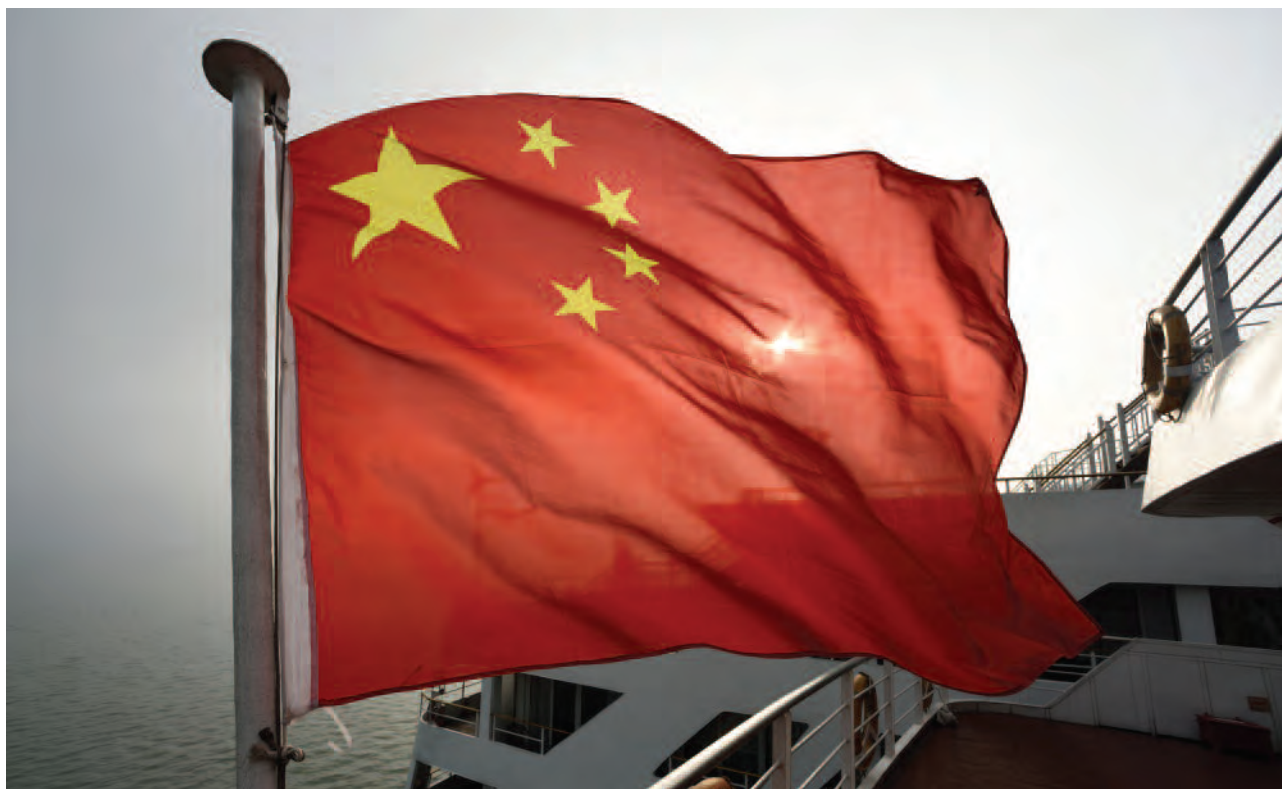
Although the protection of cabotage trade remains a high priority for most countries, not all countries are able to develop sufficient shipping capacity to service their coastal shipping trades. It is also recognised that improved marine transport connectivity, particularly in containerised liner shipping, increases competition which can lead to reductions in trade cost and growth in trade volumes. So, most countries have today relaxed restrictions in their cabotage regimes by entering into

trade agreements with other countries incorporating exceptions and waivers into their regimes for foreign flagged vessels to participate in their cabotage trades.

This Legal Briefing provides a quick overview of the cabotage regimes in Argentina, Brazil, China, Colombia, India, Peru and the United States, highlighting the restrictions, the exceptions, and penalties for violating these regulations.



# Cabotage trade regulations in China



## What laws govern the maritime cabotage trade in China?

China does not allow foreign flagged vessels to conduct domestic transport or domestic transshipments unless the prior approval of the Ministry of Transport (MOT) is obtained. There are a number of concurrent laws and restrictions that regulate maritime cabotage in China, the most relevant of which are:

- The Maritime Code of China ("CMC") – Article 4 – *"maritime transport ...between the Chinese ports shall be undertaken by ships flying the Chinese flag, except as otherwise provided..."*
- The Regulations on International Maritime Transportation ("IMT Regulations 2016 Version") – Article 24 – *"Foreign operators of international shipping services shall not operate a shipping business between Chinese ports, neither may they operate a shipping business between Chinese ports in disguised forms such as using rented Chinese ships or shipping space, or Slot exchanging of the shipping space, etc."*
- The Regulations on the Administration of Domestic Water Transport ("The Water Transport Regulations") –

Article 2 – *"The term 'domestic water transport'...refers to the commercial transport of passengers and cargoes in navigable waters, where the port of origin, the port of call, and the port of destination are all within the jurisdiction of the People's Republic of China."*

The general position in China, from the provisions above, is that carriage of goods wholly within China is classified as "domestic transport" and can be performed only by Chinese carriers.

## What are the exceptions to the above?

There is however an exception to the general position for voyages on particular routes between Shanghai and other Chinese ports by non-Chinese flagged vessels which are fully or partly owned by Chinese-funded companies registered in China. However, these Chinese funded shipping companies may not sublet their vessels to any third party.

Cargo loaded at, or destined for, a foreign port is not captured by the restrictions – even if a part of the voyage is conducted between two Chinese ports.

The voyage stages are invariably conducted under a contract of carriage,

evidenced by the bill of lading, seaway bill or waterway bill. The location of the port of loading and of the ultimate discharge port or place in the contract of carriage will determine whether a particular voyage leg, within China, is to be deemed part of international carriage or of domestic transportation.

While a transshipment of an international trade at a Chinese port is not strictly classified as domestic water transport, local authorities in China have statutory authority to interpret the relevant legislations and regulations and may adopt a restrictive interpretation of the legislations and regulations. Until such time as there is a uniform application of the legislations and regulations, a risk remains for non-Chinese flagged vessels transporting cargo between two Chinese ports, notwithstanding that the cargo is carried under an international contract of carriage.

Some international container carriers regularly load and discharge international cargoes between Chinese ports. Whilst the MOT has not taken action against these vessels, the risk remains that it could do so and it is recommended that the MOT's prior approval is obtained.



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### What are the penalties or sanctions for breach of the cabotage regime?

According to Article 41 of the IMT Regulations 2016, foreign operators of international shipping services trading between Chinese ports, or operating between Chinese ports by using chartered Chinese flagged vessels or cargo spaces thereof, or by way of slot sharing of cargo spaces, shall:

- Be ordered to terminate operations by the competent MOT of the State Council, or the authorised transportation department of the local government
- Be confiscated their illegal income, if any
- Be fined 2-5 times the illegal income if such income is RMB 500,000 and above

- Be fined RMB 200,000-1,000,000 if the illegal income is under RMB 500,000
- Have their vessel refused entry to Chinese ports if they do not comply with the operation termination order
- If non-compliance is considered to be severe, their international liner operation licences shall be cancelled

Those who illegally engage in the following activities shall be investigated for criminal liability in accordance with Criminal Law on illegal business operations (Article 50 of IMT Regulations 2016):

- Illegal international maritime transportation business operations to and from ports of China

- Illegal auxiliary business operations relating to international maritime transportation

### How are disputes or claims from maritime cabotage trade handled?

Claims or disputes arising from maritime cabotage trade shall be handled according to the Special Maritime Procedure Law or the Civil Procedure Law.

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The above has been contributed by:

#### He Yufeng, Hai Tong & Partners

Suite 1106, Ruifeng International Tower,  
No. 248, Yang Shu Pu Road,  
20082 Shanghai, China  
Dir: + 86 21 5580 2612  
Mob: + 86 13918 2468 08  
Tel: + 86 21 5588 2939

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## Special regulations on domestic transport for services across the Taiwan Strait, between mainland China and Hong Kong or Macau

The cabotage regulations in the Special Administrative Regions of Hong Kong and Macau differ from those in China. Following the transfer of sovereignty from Hong Kong and Macau to China in 1997, the MOT clarified that maritime carriage between Hong Kong or Macau and Mainland China is to be regarded as domestic carriage. Thus foreign-flagged vessels may not carry cargo originating in Hong Kong or Macau to Mainland China without the prior approval of the MOT.

As for Taiwan Strait trading, the MOT has determined that a foreign-flagged vessel may not carry, or tranship, cargo across the Taiwan Strait without the prior approval of the MOT<sup>1</sup>. An exception is made for foreign shipping lines solely owned by companies registered in mainland China or Taiwan, and for joint venture shipping companies set up between mainland Chinese registered companies and Taiwanese registered companies.

Any carriage must however be conducted under a License for Waterway Transport Across the Taiwan Strait or a Certificate For Shipping Operation Across the Taiwan Strait issued by the MOT together with a Special Seal of Waterway Transport Across the Taiwan Strait.

The MOT issued an announcement<sup>2</sup> which came into effect on 6th August 2004, tightening the restriction on crossing the Taiwan Strait. Under the same, a foreign flagged liner vessel may only cross the Taiwan Strait if it is not involved in any form of cargo trade between China and Taiwan, including the transshipment of cargo to or from foreign countries.

To conclude, the cabotage trade in China, Hong Kong and Macau is restricted to Chinese-flagged vessels. There are

regulations restricting foreign carriers from transporting or transshipping overseas cargo between Chinese ports. The application of the Maritime Code of China (CMC) and its interaction with subordinate regulations is subject to the interpretation of the local administration (e.g. the MOT). Foreign shipping companies are therefore recommended to take particular care when setting up their trade routes between Chinese ports, including ports in Hong Kong and Macao, which routes may involve crossing the Taiwan Strait.



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<sup>1</sup> MOT's Order 1996 No.6    <sup>2</sup> Ref: 2004 No.9

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# Cabotage trade regulations in India

Under the present Merchant Shipping Act 1958, only Indian flagged vessels or foreign flagged vessels as licensed by the Director General of Shipping ("DGS"), can ply the coasting trade of India. 'Coasting Trade' is defined as the carriage of goods or passengers from any port or place in India to any other port or place in India or Sri Lanka or the Continent of India.

## What laws govern the maritime cabotage trade in India?

The Indian cabotage rules are contained in Sections 406 and 407 under Part XIV of the Merchant Shipping Act 1958. The starting position is that only Indian flagged vessels can be used in the Indian cabotage trade.

## Can foreign flagged vessels participate in the Indian Cabotage trade?

There is no express bar for foreign flagged vessels to operate in the

coasting trade of India. However, foreign flagged vessels will need to be granted licences by the DGS in order to participate in the Indian coasting trade. Such a licence will be granted only if there is no Indian vessel available for the said purpose or operation. The licence granted may be a general licence, a licence for the whole or any part of the coasting trade, or a licence for a specified period or voyage. The licence will be subject to any terms and conditions that the DGS may impose, as well as to the provisions of circulars and public notices issued by the DGS from time to time.

The procedure for an Indian or a foreign charterer to obtain a licence for a foreign vessel to be engaged in the coasting trade of India is for the charterer or operator to circulate a requirement to the INSA (Indian National Shipowners Association) seeking availability of Indian ships. If INSA does not respond confirming availability within 48 hours,

an application can then be made under Sections 406 or 407 as the case maybe, to the DGS with a copy of the request to INSA and the response received from INSA. The DGS may then grant a licence allowing the foreign vessel to operate in the coastal trade of India during the period of the licence.

## What are the penalties or sanctions for breach of the cabotage regime?

There are no specific penalties but without a licence, the Customs Authorities will not give the vessel port clearance.

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The above has been contributed by:

**V. Subramanian (Kumar), Advocate,**  
**Venky's Chambers,**  
114, Maker Chambers, 3 Nariman Point,  
Mumbai 400021, India  
Mob: +91 9920375143  
Email: subrama@vsnl.com





# Cabotage trade regulations in the United States



## **What law(s) govern maritime cabotage trade in the United States?**

The Merchant Marine Act of 1920 (commonly known as the “Jones Act”) generally prohibits foreign vessels from engaging in coastwise trade within the United States. Specifically, the Jones Act provides that a vessel may not “provide any part of the transportation of merchandise by water, or by land and water, between points in the United States” unless the vessel is U.S. owned, U.S. built (or re-built), U.S. flagged and U.S. crewed.

The Passenger Vessel Services Act (of the “Passenger Services Act”) imposes similar restrictions on vessels that transport passengers.

## **What are “points in the United States”?**

The requirements of the Jones Act apply to all points within the United States, including (i) all points in the territorial sea, within three miles of the coast, (ii) points in internal waters of the United States, and (iii) the island territories and possessions of the United States. Pursuant to the Outer Continental Shelf Lands Act, the Jones Act requirements also apply to structures attached to the

U.S. outer continental shelf for the purpose of exploration, development, or production of natural resources.

By statute, the provisions do not apply to American Samoa, the Northern Mariana Islands and the United States Virgin Islands. In addition, certain other U.S. territories (including Guam) are exempt from the U.S. built requirement.

## **May a foreign vessel be used for part of a coastwise movement, if a U.S. vessel is used at the coastwise points of the movement?**

No. The Jones Act prohibits the use of foreign vessels for “any part” of a coastwise movement. Thus, if a cargo movement is, as a whole, subject to the Jones Act (that is, if it is between two U.S. points), then each part of the movement must be made with a Jones Act-compliant U.S. vessel.

## **What is “merchandise” under the Jones Act?**

The term “merchandise” is construed very broadly, to include not only goods and wares, but also “valueless materials” including scrap, rocks, dredge spoil and mud.

The Jones Act does not apply to the transportation of vessel supplies and equipment, which includes, inter alia, articles necessary and appropriate for the navigation, operation or maintenance of the vessel, and for the comfort and safety of persons on board the vessel. Determination of what constitutes “equipment” is subject to a case-by-case determination by the United States Customs and Border Protection (CBP).

## **Who is a “passenger” under the Passenger Services Act?**

U.S. courts have construed “passenger” to include any person aboard a vessel who is not involved with the vessel’s operation, navigation, ownership or business.

## **How is U.S. ownership of a vessel determined?**

A vessel satisfies the Jones Act’s U.S. ownership requirement if it is owned by one of the following “eligible owners”:

- An individual who is a U.S. citizen
- An association, trust, joint venture, or other entity, if each member of the entity is a U.S. citizen



- A partnership, if each general partner is a U.S. citizen and the controlling interest in the partnership is owned by U.S. citizen(s) or
- A corporation, if the corporation is (a) incorporated under the laws of the United States or any state; (b) the corporation's CEO and board chairman are U.S. citizens; and (c) no more than a minority of the number of directors necessary to constitute a quorum are non-citizens

In addition to the above requirements, partnerships, corporations and associations are deemed to be U.S. citizens for Jones Act purposes only if the entities are at least 75% owned by citizens of the United States, which is determined by looking at: (1) whether title to 75% of the corporation's stock is owned by U.S. citizens; (2) whether U.S. citizens have at least 75% of the corporation's voting power; (3) whether there is a contract or understanding that permits non-citizens to exercise, directly or indirectly, more than 25% of voting power; and (4) whether there are "other means by which control of the corporation is given to or permitted to be exercised by a person not a citizen of the United States." Where there are multiple layers of corporate ownership of a vessel, the interests will be "traced" through the corporate layers to the ultimate, human owners of the vessel.

Finally, even if a vessel satisfies the technical requirements for showing U.S. ownership, a violation of the Jones Act may be found if it can be shown that, substantively, the vessel is under the "actual control" of non-citizens.

### How is U.S. citizenship of a vessel's crew determined?

Under the Jones Act, only a U.S. citizen may serve as Master, Chief Engineer, Radio Officer, or Officer in charge of any Deck Watch or Engineering Watch on a vessel engaged in coastwise trade. In addition, each unlicensed seaman must be either a citizen of the United States, a permanent resident of the United States, or a foreign national who is enrolled in the United States Merchant Marine Academy. No more than 25% of unlicensed seamen on a vessel may be non-citizens.

### What is a "U.S. built" ship?

A vessel satisfies the "U.S. built" requirement if "all major components of its hull and superstructure are fabricated in the United States" and assembly of the vessel occurs "entirely in the United States." A component is "major" if it exceeds 1.5 percent of the vessel's steelweight. A component is deemed part of the hull if it forms part of the watertight envelope of the vessel.

### Can a vessel lose Jones Act eligibility?

A U.S. built vessel may lose Jones Act eligibility if it is subsequently documented under a foreign flag, sold or transferred to a person or company that does not qualify as a citizen for Jones Act purposes, or is rebuilt outside of the United States. A vessel is considered to have been "rebuilt" if "any considerable portion of its hull and superstructure" – generally 7.5% of the vessel's steelweight – "is built upon or substantially altered outside of the United States," or if any non-U.S. built

major component of the hull or superstructure is added abroad.

### May the Jones Act's restrictions be waived?

The Jones Act may be waived if doing so is "necessary in the interest of national defense." There are two types of Jones Act waivers available: waivers requested by the United States Secretary of Defense and discretionary waivers granted by the United States Secretary of Homeland Security.

The Secretary of Defense may request waivers of the Jones Act "to the extent the Secretary considers it necessary in the interest of national defense." Such waivers are automatically granted. In practice, such waivers are typically only requested to address immediate needs of the Department of Defense, such as urgent transportation of military equipment.

In addition, requests for Jones Act waivers may be submitted to the Secretary of Homeland Security, which has discretion over whether to grant such waivers if the Secretary deems it to be in the interest of national defense. Further, such waivers may only be granted if the Secretary determines that there are no Jones Act-qualifying vessels available to meet the needs. In practice, such waivers have been granted following natural disasters such as Hurricanes Katrina, Rita and Sandy, as well as certain other events (for example, the Exxon Valdez oil spill).

### What are the penalties for violations of the Jones Act?

Violation of the Jones Act can result in severe penalties, including a civil penalty or fine in an amount equal to the greater of the value of the merchandise transported in violation of the Jones Act or the value of the charter or freight paid for such transport. In certain instances, criminal sanctions are also a possibility.

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The above has been contributed by:

#### Oliver Beiersdorf, Partner

Email: OBeiersdorf@ReedSmith.com  
Tel: +1 212 549 0415

#### Lonnie E Klein, Associate

Email: LKlein@ReedSmith.com  
Tel: +1 212 549 0276

#### Reed Smith New York

599 Lexington Ave, New York,  
NY 10022, USA  
Tel: +1 212-521-5400



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# Cabotage trade regulations in four South American States

## Argentina

### What is the legislation for maritime cabotage trade and what does it state?

Domestic trade in Argentina is regulated by Decree 19,492/44 which establishes that cabotage navigation, communication and trade shall be undertaken by Argentinian vessels only.

Decree 19,492/44 does, however, allow for a temporary “exception” for cabotage trade to be granted to foreign vessels.

### What are the parameters to obtain a temporary “exception”?

Temporary permits are granted on a case by case basis and only under exceptional circumstances such as where it would not otherwise have been possible to supply goods of “first necessity” to a coastal area, or a contract cannot be complied with for lack of suitable/available Argentinean vessels.

Section 6 of the Decree provides the following guidance in relation to goods of “first necessity”: *“When, due to exceptional circumstances, it is not possible to supply a coastal zone with goods of first necessity or to comply with a contract because there are no Argentinean*

*vessels in conditions to provide the corresponding service, the National Port Authority is authorized to provide a temporary permit, in each case, to foreign vessels to provide the service, as long as those force majeure circumstances are maintained. The National Port Authority is entitled to regulate the corresponding procedure and to delegate the aforementioned authorization.”*

The application for the “exception” to the cabotage law is run through the Undersecretary of Ports and Waterways (USPW). The shippers or interested party would have to specify the type of vessel, its main particulars, specific particulars for the operation, cargo to be shipped, ports or area involved and dates on which the vessel would be needed.

This has to be circulated to the National Chambers of Shipping, as indicated by the Authority, with no less than 10 working days’ notice. If more than one shipment or offshore operations are required, 20 working days’ notice is needed. The Chambers will circulate the application within their members and they have to provide an answer within two working days. If there is no national vessel availability or interest in the shipment, the interested party will be able to obtain the “exception” from the USPW.

### What actions would the Coastguard take if they believe Decree 19,492/44 has been infringed and how to avoid it under the “exception”?

If a vessel trades contrary to the cabotage law it might be subject to a fine equivalent to three times the value of the freight or the services performed. In addition, the Coastguard would be entitled to detain the vessel if it considers that the cabotage law has prima facie been infringed. The detention of the vessel could be substituted by a cash guarantee or any other guarantee to the satisfaction of the Ministry of Transport. The sanction can be challenged through administrative proceedings and furthermore appealed to the Federal Courts.

To avoid the above, a vessel trading under an “exception” to the cabotage law should have on board the corresponding certificate.

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The above has been contributed by:

**Sebastián A. Trigub**  
**Pandi Liquidadores S.R.L.**

Viamonte 494, 8vo. piso  
(C1053ABJ) Buenos Aires, Argentina  
Tel: (+5411) 4313 3500  
Email: [sebastian.trigub@pandi.com.ar](mailto:sebastian.trigub@pandi.com.ar)





## Brazil

*Please note that the regulations below do not apply to petroleum cargoes.*

### What do the regulations regarding maritime cabotage trade in Brazil stipulate?

The main regulation governing cabotage trade is set forth in Law No. 9432/97. It establishes that the transport of cargoes in cabotage trade should be made by Brazilian shipping companies and preferentially Brazilian flagged vessels.

### Can foreign built/flagged vessels obtain a waiver to conduct maritime cabotage trade?

A foreign flagged vessel may trade in cabotage in Brazil if it is under charter to a Brazilian shipping company and is authorised to do so by the government navigation authority (ANTAQ). This authorisation can only be obtained if there are no Brazilian flagged vessels available for the intended transport.

### How are disputes or claims from maritime cabotage trade handled?

All cargoes transported in Brazil should be covered by an electronic Bill of Lading (known as a CTe). Brazilian Courts handle all claims relating to the transport of cargoes in cabotage trade and Brazilian law therefore applies.

The parties may agree to submit their disputes to a foreign jurisdiction and/or to arbitration (either in Brazil or abroad) but such an agreement should be expressed and duly signed by both parties. Printed clauses on the reverse side of a Bill of Lading (or an accompanying CTe) are not deemed valid in Brazil for the purpose of establishing jurisdiction and arbitration.

### What are the penalties for foreign flagged vessels breaching cabotage restrictions in Brazil?

As advised above, foreign flagged vessels can only trade under cabotage in Brazil if chartered to a Brazilian shipping company (duly authorised to trade by the competent governmental agency).

The regulation currently in force establishes the following fines, in addition and without prejudice to, a procedure seeking the eventual

cancellation of the authorisation for the Brazilian shipping company:

- To operate in cabotage trade without authorisation from the National Agency – R\$ 1 million
- To charter a foreign flagged vessel without authorisation from the National Agency – R\$ 600,000

The above mentioned fines are imposed by the National Agency and do not exempt any individual indemnity lawsuits from companies who might consider themselves to have been prejudiced by the violation of the law and regulations in force.

As a final note, it is worth mentioning that a foreign shipping company would not be able to load a cargo in a Brazilian port under cabotage trade due to the system and documentary restrictions.

The above has been contributed by:

**Antonio Francisco Sobral Sampaio Porto Sampaio Silva – Advogados**  
Rua Primeiro de Março 23, Andar 20  
Rio de Janeiro, RJ, 20010-000 Brazil  
Tel: (+55 21) 2111-8118



# Colombia

## What are the existing regulations for maritime cabotage trade in Colombia?

By Decree 390 of 2016 a new Customs Statute was issued, but the same has entered into force only partially. According to the Colombian Maritime Authority (DIMAR), matters associated with cabotage under the previous Customs Statute (2004) are still valid.

The previous Customs Statutes (2004) defined cabotage as the customs transit mode that regulates the transportation of merchandise under customs control, whose circulation is restricted – via water or air – between two authorised ports or airports within the national customs territory.

Access to the maritime cabotage market is limited to companies constituted by legal entities with their main domicile in Colombia or by legal entities incorporated in Colombia. In both cases, the company must have at least one Colombian flagged vessel.

## Can foreign flagged vessels participate in the Colombian Cabotage trade?

The Customs Statute (2004) contained

rules for the participation of foreign flagged vessels in the Colombian Cabotage trade (called Special Cabotage). These rules on Special Cabotage have actually disappeared in the new statute but they are still being applied for the time being.

Special Cabotage was defined as the mode of customs transit regime, which regulates the transfer of merchandise under customs control between two maritime or river ports, which after having entered the national customs territory will be transported (after changing the transportation mode) to the national destination port, but the ship must have a foreign country as its final route.

In accordance with stipulations of the Customs Statutes in force, foreign maritime lines are authorised to provide cabotage under what is known as special cabotage, as long as they comply with certain requirements.

Cabotage must be carried out by transportation companies that are duly registered and authorised to carry out these types of operations by the Tax and National Customs Directorate.

The transporter or its maritime agent can directly request authorisation for this operation after constituting a global

guarantee for a value equivalent to 500 minimum legal monthly salaries in force, which covers the finalisation of this mode under the term authorised by the departure customs. As the current minimum legal monthly salary is USD 276.64, the global guarantee amount is therefore USD 138,320.

## What are the penalties for foreign flagged vessels breaching cabotage restrictions in Colombia?

Carrying out cabotage without complying with Colombian law will not only entail the sanction of seizure of the cargo, but also sanctions against the shipping company due to their supplying transportation services in areas in which they have not been authorised by DIMAR (Dirección General Marítima).

The above has been contributed by:

**Erick Grandjean I. CEO  
Pandi Colombia S.A.**

Tel: +57 (5)360 0524

+57 (5)368 0482

Mob: +57 301 780 3763

+57 315 721 3016

erick.grandjean@pandicolombia.com.co

Centro Empresarial de las Américas

Office 213, Calle 77B No. 57-141

Barranquilla, Colombia



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## Peru

### **Under Peruvian Law what are the requirements for maritime cabotage trade?**

Cabotage trade is regulated by the Law to Reactive and Promote the National Merchant Marine No 28583 as amended under No 29475 and Mo 30580. It demands that cabotage trade is performed by Peruvian flagged vessels owned by Peruvian companies.

Peruvian owned shipping companies can also conduct such trade under bareboat Charterparty or financial leasing, providing there is an obligation for the shipping company to purchase the vessel.

### **Can Peruvian shipping companies charter in foreign flagged vessels for cabotage trade?**

If there are no vessels available that comply with the regulations for maritime cabotage trade then Peruvian shipping companies can charter foreign flagged vessels for a period of three years. This is valid from the date the General Direction of Aquatic Transport grants an operation permit. A maximum of one year's extension can be obtained.

### **Can foreign flagged vessels participate in the Peruvian Cabotage trade?**

Foreign shipping companies cannot participate in Peruvian cabotage trade unless they form some sort of association with a Peruvian shipping company.

### **What are the penalties for foreign flagged vessels breaching cabotage restrictions in Peru?**

Under Peruvian Law it is considered a very serious infraction, which is

sanctioned with a fine in the range of Peruvian Soles S/. 83,000.00 up to Peruvian Soles S/. 207,500.00 (In U.S. currency, the fine will be in the range of USD 25,696.59 up to USD 64,241.49).

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The above has been contributed by:

**Jean Pierre Guembes, Lawyer**  
**Andes Pacific Services S.A.**  
Ca. Federico Recavarren 131 Of. 404  
Miraflores, Lima, Perú  
Lima 15074  
Tel: (51+1) 242-0138  
(51+1) 243-0033  
(51+1) 241-8355  
Mob: (51) 99851-4616  
Email: legal@pandiperu.com  
www.pandiperu.com

