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LOGISTICS INSIGHTS

THE CHANGING TRADE LANDSCAPE IN ASIA – ARE YOU READY?

OBOR, TPP, RCEP, FTAAP. The list of existing and nascent free trade agreements and initiatives in Asia at times appear never-ending. Whilst the proliferation of free trade agreements does not necessarily lead to greater trade opportunities, as traders struggle to comply with a noodle-bowl of regulations, it is indicative of the region's aspirations for free, and more integrated, trade and supply chains.

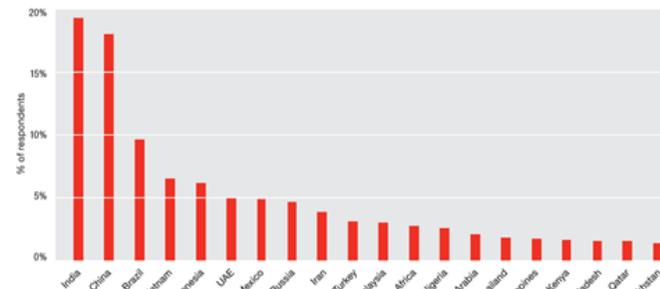
In this article, we look at some of the opportunities and challenges this changing trade environment is likely to bring to Asia in 2017 and beyond.



New logistics hubs emerging

Emerging markets are becoming an ever-attractive investment for logistics companies. Research shows that of the 20 top emerging markets for growth in logistics over the next 5 years, 9 are in Asia.

Emerging markets with most potential to grow as logistics markets over the next five years



Note: Results are based on a survey of over 800 supply chain professionals

Source: Agility Emerging Markets Logistics Index 2017

China's potential is seemingly being driven by the introduction of the Belt and Road Initiative ("BRI") by the Chinese government in 2013. The formerly remote area of China's Western borders has seen an increase in manufacturing and logistics activity due to this initiative.

The dry port at Khorgos, on the border between China and Kazakhstan, is just one example of how the BRI is shifting logistics centres further west, into Central Asia. Major logistics players such as DP World and Kerry Logistics have already expanded their networks into Central Asia to take advantage of the current minimal presence of professional, globally integrated logistics service suppliers in the region.

The proliferation of "free trade zones", perhaps in response to the BRI, is also attracting investment from global logistics players. Yusen Logistics recently announced the opening of a logistics centre in Myanmar and DHL have announced that they will be looking to invest €70 million in South East Asia by 2020. Added to that is the growing number of port development projects in the region with 5 projects currently underway in the Malacca Straits alone.

Whilst new investments in logistics are welcome, the entry into emerging markets will not be without its hurdles. These can take the form of mandatory local requirements for foreign investors, undeveloped legal protections, arbitrary implementation of contracts and laws, and in some instances, endemic corruption. Ensuring that these factors are thoroughly assessed, priced in and insured against are the key to successful entry into emerging markets.



E-commerce – the next logistics boom?

The expected huge growth of e-commerce in South-East Asia in the next few years is being touted as the next frontier for logistics companies.

The region's growing middle class with its increasing disposable incomes, is a tantalising prospect but certain infrastructure limitations persist. Access to reliable internet and cashless payment systems on the technology side and, perhaps more fundamentally, the lack of the required warehousing and transport services to be able to respond to a sustained increase in e-commerce across the region on the infrastructure side.

However, the physical infrastructure restraints look set to be addressed with the entry into the market of the behemoths Alibaba and Amazon. Amazon, having built their largest warehouse in an urban setting in Singapore and Alibaba, is working to set up the world's first "Digital Free Trade Zone" in Malaysia.

The rapid rise of e-commerce in the region may leave regulators behind as last mile delivery technology is introduced and further mergers and buyouts proliferate. The legal implications of this, and other issues relating to e-commerce, will be the subject of a forthcoming special edition of this newsletter.

On-going legal reforms in emerging markets

Emerging markets are making strides towards reforming their customs, tax and trade laws, bringing them in line with international standards. Whilst such reforms do not always translate to reductions in trade costs or increased efficiencies in practice, they are at least a first step in the right direction. Some recent examples of legal reforms relevant to the logistics sector in Asia are:

- a. India's GST overhaul – it is estimated that the standardisation of India's tax laws across the country will substantially cut the cost of moving goods between states. Consequently, this will lead to a re-calibration of the logistics network as companies look to gain efficiencies and economies of scale by consolidating and centralising inventory, rather than having separate warehouses in each state.
- b. Implementation of the World Trade Organisation's Trade Facilitation Agreement ("TFA") – the TFA entered into force in February 2017, requiring WTO members to implement an array of reforms designed to facilitate the efficient movement of goods across borders, reduce the time spent at border-crossings and provide for transparent and accessible customs regimes. The vast majority of countries in Asia are already signatories. Whilst full implementation is a number of years away, it is estimated

that the TFA could lead to substantial gains in world trade, reducing average import times by over a day and a half and reducing average exporting times by up to 2 days.

- c. In August 2017, Bangladesh, Cambodia and China became the first signatories to the UN Framework Agreement on Facilitation of Cross-border Paperless Trade in Asia and the Pacific, signalling an increasing commitment by the region to implementing the reforms necessary to allow for paperless trade, and building on the ASEAN Single-Window initiative.
- d. China signing up to TIR – In July 2016 China acceded to the TIR Convention, ostensibly easing the flow of goods by road to and from China. The IRU cites a report that estimates that this could reduce transit time by as much as 80 percent and increase total exports by up to USD 7.86 billion, with trade along the BIR route estimated to increase by up to USD 13.5 billion.



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LEGAL ROUND UP: WHOSE FAULT IS IT ANYWAY?

In this article we run through a trio of recent cases from the English courts on carrier liability, with a focus on containerised cargoes.

Court of Appeal clarifies who bears burden of proof in inherent vice cases - Volcafe Ltd and others v. Compania Sud Americana de Vapores SA [2016] EWCA Civ 1103

The case concerned a claim for damage to a shipment of coffee beans carried from Colombia to Germany by the defendant container line. The bills of lading incorporated the Hague Rules and recorded receipt of the cargo in apparent good order and condition.

Held:

- the Hague Rules applied to the stuffing of the containers where the carrier has assumed an obligation to stuff the containers as part of the loading services, to which the Hague Rules applied;
- if the carrier wants to rely on the inherent vice defence in the Rules, it does not have to first establish that it has not been negligent;

- the inherent vice exception can apply to entirely normal (i.e. not defective) cargoes as long as the loss resulted from the natural properties of the goods; and
- in proving that it had employed a sound system in the carriage of goods, the carrier is entitled to rely on evidence of standard industry practice for the carriage of this cargo.

Key implications:

- Carriers, forwarders and other cargo agents should ensure that their contracts make it clear when their responsibility for the cargo begins and ends.
- To prove that goods are carried under a “sound system” it is important to ensure that your operatives and employees are fully aware of the up to date industry standards for the carriage of that particular cargo.

Guidance provided for package limitation for containerised cargoes - Kyokuyo Co Ltd v A.P. Møller–Maersk A/S (Maersk Tangier) [2017] EWHC 654 (Comm)

The case concerned a claim for damage to a consignment of tuna, being shipped in three refrigerated containers from Spain to Japan, without additional wrapping or packaging, and without consolidation. The key issue was how the package limitation in the Hague-Visby Rules was to be applied.

Held:

- The Hague-Visby Rules could apply compulsorily to sea waybills where a waybill was issued in place of a bill of lading, where the contract of carriage contemplates the issuing of a bill of lading.
- The definition of “unit” in the Rules applies to the individual units of tuna loins or bags; containers are not of themselves units of cargo.
- It is sufficient for the physical items of cargo to be listed or enumerated, and not necessarily stipulated in the bill of lading “as packed”, as long as they are accurately documented for the purposes of the Hague-Visby Rules.



- Cargo limits should be calculated as per unit, not collectively across the containers, and the balance cannot be carried over, reflecting the actual damage suffered.

Key implications:

- Those dealing with contracts of carriage should be aware that in certain circumstances, their sea waybills will be deemed automatically subject to the Hague Visby Rules under English law. If a different liability regime is preferred, then the contract of carriage will need to be drafted accordingly.



Electronic release system leaves carrier exposed - MSC Mediterranean Shipping Company SA v. Glencore International AG (MSC Eugenia) [2017] EWCA Civ 365

The case concerned a claim for misdelivery, following the theft of two consignments of cobalt briquettes from containers discharged at Antwerp Port. The cargo was to be delivered via the electronic release system (“ERS”) at the port that was designed to replace the need for a carrier to issue paper delivery orders or to release cargo in return for bills.

Held:

- A release note containing a PIN code and issued via an electronic release system did not constitute a “delivery order” either as required by the bill of lading or within the definition of a “ship’s delivery order” under the Carriage of Goods by Sea Act 1992.
- The stand-alone release note containing the PIN code served as no more than an instruction to the terminal to permit delivery rather than constituting delivery as required.
- In the context of bills of lading, delivery must amount to physical delivery, not delivery of a means of access.

Key implications:

- The decision is of interest because ERS is being increasingly used in large container ports. This case, therefore, serves as a warning to carriers using the ERS system that they may be exposed to liability if cargo in their possession is misappropriated by the unauthorised use of a PIN code that they have issued.
- Those using the ERS system going forward may consider incorporating into their contracts specific provisions dealing with the status of release notes and PINs and whether they should be treated as the equivalent of a delivery order by the parties.
- The allocation of risk for the misuse of PINs should also be considered.

If you would like any further guidance on how these cases may affect your business and steps you can take to ensure your contractual terms and conditions are up to date, then please do not hesitate to contact us.



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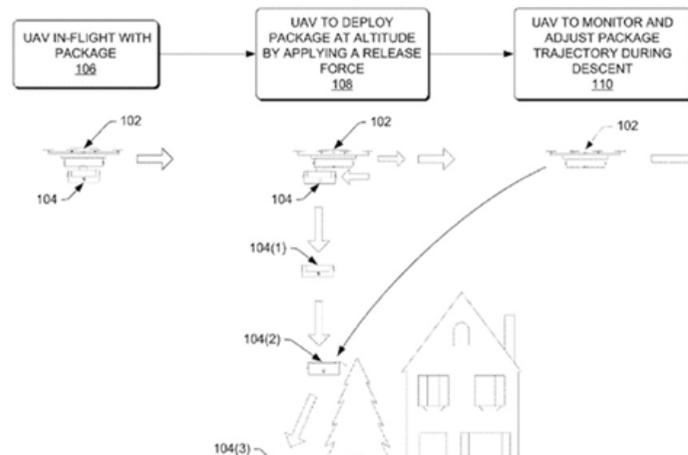
DELIVERY OF PACKAGES BY DRONES – FACT OR FICTION?

There has been a lot of debate over the possibility of delivery of packages by drones. Some have even started testing the technology. In early 2016, Foodpanda tested delivering meals in Singapore by drones and later in the year, a 56 s video of a can of Asahi beer being delivered by a drone to a rooftop in Hong Kong went viral. But, is delivery of packages by drones in Hong Kong possible or even legal?

Before analysing the legalities of this issue, let's first take a long at how delivery by drones can take place. The picture below demonstrates how Amazon anticipates delivery by drones will generally work.

The idea is to use of magnets, trees and parachutes to make sure that the packages land on the proper place. This may prove difficult in Hong Kong's densely populated concrete jungle.

Hong Kong does not have specific legislation regulating the use of drones for commercial purposes. Currently, drones (or, otherwise referred to as Unmanned Aircraft Systems (UAS)), regardless of size or weight, are governed by Article 48 of the Air Navigation (Hong Kong) Order 1995. This order stipulates that a person shall not recklessly or negligently cause or permit an aircraft to endanger any property or person. The use of drones for hire/ reward i.e. for commercial purposes is subject to a licensing regime governed by Regulation 22 of the Air Transport (Licensing of Air Services) Regulations.



Source: Amazon

However, the Civil Aviation Department has issued the following guidelines for the commercial use of drones in Hong Kong.

- Every drone over 7kg in empty weight requires an air permit for every flight.
- You may not fly within 50 meters of any person, vessel, vehicle, or structure not under control of the drone operator except during take off and landing

- You must not fly your drone within 30 meters of any person other than the operator
- The drone operation site must be under the operators full control
- The drone take off/landing area should be properly segmented from public access
- Drone operator must maintain visual line of sight during the flight
- Drone operator is responsible for ensuring that no person or property would be endangered by the drone and shall not fly the drone unless he is reasonably satisfied the flight can be safely made
- No hazardous material may be carried on board the drone
- No objects may be dropped from the drone
- The drones return to home mechanism must be fully functional
- Drone operator must maintain records of each flight
- A site safety assessment must be performed by the drone operator and maintained
- Permission of the land/property owner whose land/property the drone is intended to operate on must be obtained
- Operation of the drone must be carried out in accordance with the equipment operations manual



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- Drone operations should be conducted during daylight hours only
- No more than one drone will be permitted at any one time within the same block of designated airspace
- Ground visibility of not less than 5km is required
- Cloud base may not be lower than approved altitude of operations
- Surface wind may be no more than 20 knots unless otherwise specified by the manufacturer
- Drone operator must have a hand held anemometer to monitor surface wind speed on site
- Drone operator must not fly when there is a rainstorm warning, tropical cyclone warning, or a strong monsoon signal is in force
- Evidence of pilot competency is required when making an application for permission to operate a drone. Basic national UAS certificate – small unmanned aircraft (BNUC-S) or equivalent
- Drone operator is required to submit an operations manual covering the procedures to be followed for all envisioned operations of the drone. This document is key in the authority granting permission. A guidance to preparing an operations manual can be found here
- The drone operator is required to seek approval from the Office of the Communications Authority on the use of radio frequencies and to ensure that no RFI is caused to air traffic operations and air navigation equipment.

So, the use of drones in Hong Kong for commercial purposes is legal. That said, the guidelines are long and the restrictions make it difficult to deliver packages in populated areas i.e. most of Hong Kong. Furthermore, the current legislation is inadequate to deal with commercial usage of drones, much less delivery of packages by drones. If the delivery of packages by drones in Hong Kong is to become a reality, Hong Kong should follow the lead of jurisdictions like Singapore and the EU in introducing drone specific legislation to regulate the safe use of drones for both recreational and commercial purposes.



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REGULATORY AND COMPLIANCE CHECKLIST: HOW DO YOUR INTERNAL POLICIES FARE?

Whilst logistics companies are no strangers to regulatory compliance, in recent years, the scope and pace of regulations have increased significantly. As a result, companies should be looking to continually update and broaden their internal compliance policies.

Typically, any robust regulatory and compliance policy should:

- Start with an assessment of the risks specific to your business;
- Be designed to address those specific risks;
- Be embedded in the culture of the company – from the board room down;
- Be employed in relation to third party suppliers; and
- Be reviewed periodically and amended to take into account new business risks, developments and any gaps found in the operation of the policy.

Below we outline some of the key current regulatory and compliance risks that your internal policies should be addressing:

Bribery, corruption and anti-money laundering

Requests for “facilitation payments” from customs officials are nothing new, but the international prohibition of such payments is growing, with substantial fines imposed on companies in breach.

Key questions:

- How does your anti-bribery and corruption policy deal with facilitation payments?
- What advice does it provide as to how a request for payment should be dealt with?
- Have you checked the anti-bribery policy of your agents?

Cyber-security, digitalisation and data protection

International freight transport is becoming ever more digitalised. Whilst this can provide significant benefits and cost-savings, it also opens up a whole new front of risks. In June 2017, AP-Moller Maersk became the latest high profile victim of a ransomware attack.

Key questions:

- What, if any, cyber-security and data protection policy and protocols do you have in place?
- When were these last reviewed?
- Have you tested your systems for vulnerabilities?
- Have you confirmed that your insurance policies cover data loss or breach?

Anti-trust

The majority of developed countries have implemented stringent laws regulating and sanctioning behaviour that is deemed anti-competitive. Authorities have shown a low tolerance approach to breaches as has been demonstrated in the multiple investigations relating to cartels in the freight and logistics markets.

Key questions:

- Is your company a member of a trade association?
- At trade association meetings, are topics such as pricing, timing of changes to pricing policies or costs and profits discussed?
- Do you have any formal or informal agreements in place with your competitors?



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Sanctions and other import / export controls

In the current political landscape of nationalist policies, logistics companies need to be prepared for and alert to sudden changes in the trade regulation environment. These include sanctions against specific goods, countries, entities and individuals; trade defence measures such as import bans or quotas; and restrictions on points of entry.

Key questions

- What procedures are in place for performing due diligence on new customers / transactions / countries of import and export?
- Do your standard terms and conditions include a sanctions clause?

If you have any questions relating to the above or need help in assessing the robustness of your current policies, please contact Rory Macfarlane, Asia Head of Regulatory and Compliance, or your usual Ince & Co contact.



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