

# DO YOU CLEARLY SEE WHAT'S COMING?

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## **U.S. Maritime Alert**

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Starting on January 1, 2020, most oceangoing commercial vessels (regardless of the cargo or purpose of the voyage) that burn fuel oil will be required to use fuel oil with a sulfur content of not more than 0.5%. This is when MARPOL's new global sulfur cap goes into effect, lowering the maximum allowable sulfur content of fuel oil used in most oceangoing vessels from 3.5% to 0.5%. That should create an immediate demand for as much as 6 to 8 million barrels of fuel oil per day. [1] This is the latest wave of increasingly challenging environmental regulatory requirements faced by the shipping industry. [2] It generally applies to vessels globally, unless a vessel is operating in an Emissions Control Area, in which case even stricter limits apply. With fuel oil often representing the single biggest vessel operating expense, these new requirements are sure to impact the shipping industry and its customers.

Given the worldwide implementation of this new requirement, many industry experts believe that there will be insufficient supplies of compliant fuel available on January 1, 2020 to supply the demand, [3] and alternative technologies and sources of compliant fuel (e.g., scrubbers, LNG, and fuel blends) may not be sufficiently advanced, available, reliable, or economical to fill the gap for at least a year or more. Accordingly, the risk of non-compliance due to the unavailability of compliant fuel is high. At the same time, the U.S. Coast Guard, U.S. Environmental Protection Agency, and U.S. Department of Justice continue to vigorously enforce the provisions of MARPOL. [4] Liability for failing to use compliant fuel can take many forms in the United States, including civil penalties for unintentional violations and criminal penalties for knowing or intentional violations. At a minimum, regardless of intent, penalties start at levels that are designed to remove any "economic benefit" of failing to obtain compliant fuel—that is, the cost avoided by not obtaining compliant fuel. As this new global gap moves closer to implementation, it appears the International Maritime Organization ("IMO") is on the verge of adopting a prohibition against the mere carriage of noncompliant fuel, which will allow port states and flag states the ability to more easily enforce the new global sulfur cap. [5]

There is a great deal of uncertainty whether there will be adequate supply of compliant fuel, at least in the near term, what that will mean in terms of the cost of the fuel, and how port states and flag administrations will handle non-compliance in the face of inadequate supply. Notwithstanding potentially inadequate supply, regulators and industry stakeholders appear to be in agreement that there must be a practical and consistent approach to enforcement.

The IMO is holding an Intersessional Working Group meeting in London, consisting of flag and port state representatives, who will implement and enforce these requirements, along with other industry stakeholders. The purpose of the meeting is to consider measures that promote consistent and effective implementation of these requirements globally, and to address industry concerns in this regard. In particular, they will address the following issues:

1. The preparatory and transitional issues that may arise with a shift from the 3.50% sulfur limit to the new 0.50% limit;
2. The impact on fuel and machinery systems that may result from the use of fuel oils with a 0.50% sulfur limit;
3. Verification issues and control mechanisms and actions that are necessary to ensure compliance and consistent implementation;
4. A draft standard format (a standardized system) for reporting fuel oil non-availability that may be used to provide evidence if a ship is unable to obtain compliant fuel oil;
5. Developing guidance, as appropriate, that may assist Member States and stakeholders in assessing the sulfur content of fuel oil delivered for use on board ship, based on the consideration of mechanisms to encourage verification that fuels supplied to ships meet the specified sulfur limit as stated on the bunker delivery note;
6. Requesting ISO to consider the framework of ISO 8217 standard for fuels supplied on a world-wide basis for consumption on board ships, with a view to keeping consistency between the relevant ISO standards on marine fuels and the implementation of regulation 14.1.3 of MARPOL Annex VI; and
7. Any consequential regulatory amendments and/or guidelines necessary to address issues raised or otherwise considered necessary to ensure consistent implementation of regulation 14.1.3 of MARPOL Annex VI.

What must those impacted by these questions think about? The adage, “where you stand depends on where you sit” is particularly apropos here. Consider the following:

- Can the expected increase in the cost of this fuel be passed on? By whom and how?
- What kind of pre-2020 planning will be needed in order to ensure that if one cannot obtain compliant fuel after that date, authorities will find that sufficient good-faith, best efforts were undertaken? If one segment of industry is already seeking contracts for fuel, will that become the industry standard for good-faith, best efforts?
- Will development and adherence to ship-specific implementation plans be sufficient?
- What will the format and administrative burden be for such implementation plans, and will they be required for all vessels? Will flag states approve them?
- Will there be a globally acceptable fuel oil non-availability report (FONAR) form available to utilize for all port states?
- If the obligation to use compliant fuel (or use best efforts to obtain it) falls on vessel owners and operators, but fuel purchasing is undertaken by charterers, to what extent can the owners/operators rely on the charterers' best efforts and when submitting FONARs?
- How can one be sure that the fuel is deemed compliant? Will bunker delivery notes still suffice?
- How will port states and flag states interact in order to enforce these requirements?

- What recourse will a vessel operator have against a fuel supplier if fuel delivered as compliant is not, and the vessel is prosecuted?
- Will vessels be expected to purchase and use compliant fuel, regardless of price—and will excessive cost and price gouging by suppliers be a consideration in determining whether compliant fuel is truly available?
- At this time, it is not known the extent to which fuels compliant with the 2020 global sulfur cap will be purpose refined or blended. Accordingly, are there safety and machinery impacts associated with the use of blended fuels, and how should these be addressed?
- Do existing standard contracts between owners and charterers, and those that extend beyond 2020, sufficiently define the allocation of risk, liabilities, and rights of the parties with respect to obtaining compliant fuel?

Many of these questions, and more, will be discussed by enforcement authorities and perhaps addressed in the guidelines developed at the July Intersessional Working Group meeting and presented to the IMO Marine Environmental Protection Committee (MEPC). The approach IMO develops in regard to implementation and enforcement undoubtedly will shape industry plans for compliance, the demand for compliant fuel, and the price of that fuel potentially for years to come.

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#### Notes:

[1] Philip K. Verleger, *Limit Sulfur in Shipping Fuel, But Not So Fast*, BLOOMBERG (April 18, 2018), <https://www.bloomberg.com/view/articles/2018-04-18/limit-sulfur-in-shipping-fuel-but-not-so-fast> (last visited July 2, 2018).

[2] For examples of the many other environmental regulatory requirements that have been imposed on the shipping industry, see: <http://www.klgates.com/european-union-may-adopt-more-stringent-sulfur-content-limits-for-marine-fuels-06-13-2012/>; <http://www.klgates.com/epa-issues-2013-vessel-general-permit-04-02-2013/>; <http://www.klgates.com/epa-and-coast-guard-disagree-on-how-to-address-industry-obligations-to-meet-january-1-2014-implementation-deadline-for-new-ballast-water-discharge-limits-01-06-2014/>; <http://www.klgates.com/epa-announces-timeline-for-vgp-30-11-02-2016/>; <http://www.klgates.com/federal-appellate-court-stays-initial-date-for-meeting-new-ballast-water-discharge-limits-but-only-for-canadian-shipowners-association-members-04-11-2014/>; <http://www.klgates.com/maritime-industry-faced-with-new-proposals-for-regulating-air-and-water-discharges-as-a-result-of-environmental-group-action-comment-opportunities-limited-07-28-2010/>; <http://www.klgates.com/international-maritime-organization-imo-approves-authority-for-us-to-impose-stringent-new-air-emission-standards-for-large-oceangoing-vessels-04-06-2010/>; <http://www.klgates.com/the-winds-of-change-continue-to-blow-coast-guard-proposes-new-ballast-water-discharge-limitations-09-09-2009/>; <http://www.klgates.com/the-winds-of-change-continue-to-blow-coast-guard-proposes-new-ballast-water-discharge-limitations-09-09-2009/>; <http://www.klgates.com/the-perfect-storm-continues-proposed-ballast-water-and-air-emissions-regulations-present-more-new-challenges-for-the-maritime-industry-opportunity-to-comment-is-limited-08-28-2009/>; <http://www.klgates.com/epa-proposes-new-air-emission-standards-for-large-us-flag-vessels-08-06-2009/>; <http://www.klgates.com/epa-seeks-to-create-emission-control-areas-to-limit-vessel-air-emissions-along-coastline-of-united-states-04-24-2009/>; <http://www.klgates.com/winds-change-for-the-maritime-industry->

[with-new-climate-change-legislation-04-20-2009/](http://www.klgates.com/files/Publication/4f83c3c4-e08c-4661-b8a9-79530f1257af/Presentation/PublicationAttachment/1eb259b2-f28c-44c6-84c9-7fe59f300a48/Barry%20Hartman%20_Presentation.pdf); [http://www.klgates.com/files/Publication/4f83c3c4-e08c-4661-b8a9-79530f1257af/Presentation/PublicationAttachment/1eb259b2-f28c-44c6-84c9-7fe59f300a48/Barry%20Hartman%20\\_Presentation.pdf](http://www.klgates.com/files/Publication/4f83c3c4-e08c-4661-b8a9-79530f1257af/Presentation/PublicationAttachment/1eb259b2-f28c-44c6-84c9-7fe59f300a48/Barry%20Hartman%20_Presentation.pdf); <http://www.klgates.com/the-perfect-storm-ballast-water-discharges-face-potential-new-regulatory-legislative-and-judicial-rules-09-05-2007/>

[3] Ned Molloy, *The IMO's 2020 Global Sulfur Cap*, S&P GLOBAL PLATTS (Oct. 2016), <https://www.platts.com/IM.Platts.Content/InsightAnalysis/IndustrySolutionPapers/SR-IMO-2020-Global-sulfur-cap-102016.pdf>. While there is theoretical production capacity, refineries must alter production processes, storage capacity must be gradually converted, and demand must be balanced.

[4] See <https://www.justice.gov/enrd/vessel-pollution-enforcement>.

[5] See <http://www.imo.org/en/MediaCentre/MeetingSummaries/PPR/Pages/PPR-5th-Session.aspx>.

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