

SUBMISSION BY THE INTERNATIONAL GROUP OF P&I CLUBS

**“IMO JAKARTA MEETING ON THE STRAITS OF MALACCA AND
SINGAPORE: ENHANCING SAFETY, SECURITY AND
ENVIRONMENTAL PROTECTION,”**

7 AND 8 SEPTEMBER 2005

1. Summary

The member associations of the International Group of P&I Clubs (IG) collectively provide liability insurance to about 90 per cent of the world's ocean going fleet.

This Submission comments upon the loss prevention activities of P&I Clubs and the levels of P&I insurance generally available to shipowners, including those whose vessels transit the Strait of Malacca.

Loss prevention is a core concern of P&I Club Boards and collectively the members of the International Group produce an extensive library of information designed to improve safety of ships.

Additionally, P&I Clubs' boards view the provision of adequate levels of marine risk and supplemental war risk P&I insurance as essential to marine transport in the Strait of Malacca and world wide. At this time, IG P&I Clubs also offer Special War Risks P&I Cover (which includes terrorism risks) with a limit of USD 500 million above defined excess points. This Special War Risks P&I Cover relies on reinsurance markets in which there are mechanisms for declarations of exclusion areas requiring additional premium. At this time no port adjacent to the Strait of Malacca and Singapore or the strait itself is a named exclusion area for the Special War Risks P&I Cover.

The IG continuously monitors the risks present and reinsurance available in order to provide shipowners with cost-effective insurance. The continued availability of reinsurance therefore influences the ability of IG P&I Clubs to provide the current level of terrorism coverage for ships transiting and calling at ports in the Strait of Malacca, and indeed anywhere else in the world. The International Group welcomes measures which improve safety and security in the Strait of Malacca. A significant deterioration in security would ultimately be reflected in insurance conditions and costs.

2. The Composition and Role of the International Group

The International Group is an NGO attending by invitation.

Each of the thirteen constituent P&I Clubs is an independent, non-profit making mutual insurance association (or "Club"), providing cover for its shipowner and charterer members against liabilities arising from the owning or operation of ships. Each Club is controlled by its members through a Board of Directors (or Committee) elected from the membership; the Board (or Committee) retains responsibility for strategic and policy issues but delegates to full-time managers the day-to-day running of the Club.

Together the Clubs insure over 90 per cent of the world's blue-water tonnage.

The principal role of the IG is the operation and regulation of the Clubs' claims-sharing pool, and the very extensive reinsurance programme which protects the pool. Much of the IG's work is devoted to defining and refining the scope of cover for pool claims and getting rules and guidelines for the Clubs' mutual interests.

2.1. What is P&I Insurance?

P&I stands for Protection and Indemnity. P&I is insurance in respect of third party liabilities and expenses arising from owning ships or operating ships as principals. The risks typically covered by P&I Clubs relate to personal injury or death, wreck removal, cargo loss or damage, pollution and other environmental damage, and damage to third party property such as docks, cranes, pipelines, or other ships in collision.

The P&I clubs play an important role in providing certificates of financial responsibility required by States parties to the International Convention on Civil Liability for Oil Pollution Damage (CLC), 1969 as amended by the 1992 Protocol (such as the Strait of Malacca littoral States).

P&I insurance is not hull insurance which pays for loss of or damage to the ship itself, nor is it loss of profit/freight insurance, detention insurance, strike insurance or uninsured legal expenses (Defence) cover.

The scope of coverage for P&I risks is set out in the Rules of a Club. A Club's Rules will also contain exclusions of certain third party risks that are not treated as normal P&I. Of particular relevance to this submission is the exclusion of P&I War Risks,

which are P&I liabilities arising from certain defined warlike occurrences or events, including acts of terrorism, or arising from the use of weapons of war. An example of a current P&I Club exclusion of war and terrorism risks is appended to this submission.

2.2. Loss Prevention and Contribution to Safety

The P&I Clubs collectively produce an extensive range of loss prevention material addressing nearly all aspects of ship operation. Material is distributed to shipowner members of the clubs, and a large body of material is designed to be provided to crew operating the ships. The materials draw upon lessons learned from past accidents as well as analyses by experts. Within the International Group, loss prevention material is produced on a weekly basis. Most Clubs also conduct inspection activities.

Taken as a whole, loss prevention activities are a core function of International Group P&I Clubs and the International Group plays an important role in promoting safety at sea.

2.3. The Insurance Pool

Although the Clubs compete with each other for business, they have found it beneficial to pool their larger risks under the auspices of the International Group. This pooling is regulated by a contractual agreement which defines the risks that are to be pooled and exactly how these are to be shared between the participating Clubs. The Pool provides a mechanism for sharing all claims in excess of USD 6 million up to about USD 4.5 billion (or USD 1 billion for oil pollution). For a layer of claims between USD 50 million and USD 2.050 billion the International Group Clubs purchase reinsurance from the commercial market. The Pooling system provides participating Clubs with reinsurance protection at cost to much higher levels than would normally be available in the commercial reinsurance market.

International Groups prepare extensive loss prevention and safety material, but the Boards of Clubs seek to provide high levels of coverage in the event of accidents.

3. Commentary on War Risks and Terrorism P&I Insurance Coverage

Safety and security issues cover a broad spectrum of risks and topics, as demonstrated by the range of issues addressed in the agenda to the meeting. Statistically, liabilities arising from acts of piracy or terrorism make up only a fraction of the claims dealt with by International Group P&I clubs, including in the Straits of Malacca and adjoining regions. The vast majority of claims there arise from more conventional origins, including all manner of human errors in the maintenance, operation or navigation of ships. Nonetheless, the threat of liability claims arising due to acts of piracy or terrorism exists and, in line with the Meeting agenda, the International

Group wishes to describe the role of the International Group Clubs in relation to insurance coverage for such risks.

3.1. Primary Layer Hull and P&I War Risk Insurance

Within the broader marine insurance market there are separate sectors dealing respectively with hull insurance, P&I insurance and War Risk insurance, among others. Making generalisations about the war risk market can be difficult as conditions and terms vary by policy, underwriter, national market and other factors. The summary which follows will not therefore apply in all circumstances and is for illustration purposes only.

War risks have traditionally been excluded from policies of hull insurance or P&I insurance, and have instead been covered under dedicated war risks policies. A shipowner's War Risk policy would normally cover both his hull war risks and his primary P&I War Risks, and would be underwritten either by a hull underwriter or by a dedicated War Risk underwriter. This primary War Risk cover would typically be limited to a sum equivalent to the value of the hull, or in the case of some specialist war risk insurers to a higher fixed policy limit.

War Risks generally include risks arising from acts of terrorism. War Risks policies generally exclude claims arising from Piracy, which may be covered under the regular marine risk hull policy or P&I policy.

A common feature of primary layer war risk insurance is that on short notice underwriters may designate geographical exclusion areas. Ships entering the exclusion area will not have War Risk insurance. However, the owners may generally re-instate the primary War Risk insurance for an Additional Premium. Designation of an area as an excluded region rests with the discretion of underwriters.

Commonly the Additional Premium is for a seven day ship presence within the designated war zone, and premium costs can be substantial.

Commercial shipping contracts deal extensively with War Risks and the allocation of additional War Risk insurance premium. At any given time it is likely that some geographic area in the world is an excluded area requiring additional premium to reinstate primary War Risk insurance.

A sector of the war risk market dealing with Hull insurance is advised or consulted by the Joint War Risk Committee. The Joint War Risk Committee comprises insurers from both the London Companies Market and the Lloyd's Market, and the role of the JWC is purely advisory. The International Group is not in a position to express views on behalf of primary war risk underwriters.

3.2. International Group 1988 Creation of a Secondary Layer of P&I War Risks Cover

Since 1988, the Clubs in the International Group have offered Special P&I War Risks cover, providing a second layer of additional protection in excess of the limit of primary P&I war risks cover. This was initially to a limit of USD 50 million, but is currently to a limit of USD 500 million. The cover is currently subject to an excess equivalent to the proper value of the ship or, if higher, the amount recoverable by the assured under any primary P&I war risks policy.

The cover is backed by reinsurance. The availability of this level of cover in the future will depend on the continued willingness of the reinsurance market to accept this degree of risk. For example, this Special P&I War Risks cover was limited to USD 50 million for named accommodation vessels operating in Athens for the period of the Olympic Games.

3.3. Development and Change in Club Rules Relating to Piracy and Terrorism

In the 1980's the P&I war risk exclusion was intended to be clarified based on mechanism of damage and not motivation; hence, the exclusion adopted in part an exclusion for claims arising where the cause was damage by "weapons of war."

During the 1980's and indeed to the present, damage or loss inflicted by Piracy has, other things being equal, been regarded as being within the scope of P&I coverage, with various technical aspects beyond the scope of this summary. For example, if pirates injure or kill a crewman and the shipowner is subsequently liable to provide compensation to dependants, the claim is generally eligible for indemnity by the P&I Club.

During 2001 reinsurance markets reacted to events by introducing clearer exclusions for loss caused by Terrorism. P&I Clubs implemented rule changes at the start of their 2002 policy year to expressly exclude losses caused by Terrorism. The text of a Club War Risk exclusion for the current 2005 policy year is appended to this submission.

At the risk of over-simplification, under a standard marine risks P&I policy, a Club may indemnify an owner for a claim caused by piracy but not a claim caused by terrorism. A claim caused by terrorism would first be dealt with by the primary layer War Risk underwriter. If the claim exceeded the defined excess point (the ship's value or limit of the primary war risks layer), the balance of the claim may be eligible for indemnity under the International Group's Special War Risk P&I Insurance.

In recent years war risk policies have themselves been made subject to a new exclusion, in respect of bio-chemical attacks. Further details are provided below.

3.3.1. P&I Clubs' Definition of Piracy and Terrorism

P&I insurance conditions operate such that there is a distinction between claims arising because of Piracy, and claims arising because of War Risks including Terrorism.

A Club Board or Committee has discretion under Club Rules where necessary to decide if an event was an act of Piracy or Terrorism. The definitions of Piracy found in article 101 of the 1982 United Nations Convention on the Law of the Sea (UNCLOS) could be used as an advisory guideline, but decisions by a Club board could be made on a case by case basis.

3.4. Shipowner Defences to Third Party Claims Resulting From Intentional Acts

Many laws and conventions governing maritime transport protect owners from liability where a loss is caused by the intentional act of a third party.

The International Convention on Civil Liability for Oil Pollution Damage (CLC), 1969 as amended provides that following a terrorist attack on a tanker the shipowner would have a defence to CLC liability based on Article III.2 (clause b) if it can be proved that the damage "was wholly caused by an act or omission done with intent to cause damage by a third party." It should be noted that where the Owner successfully relies on this defence, the IOPC Fund will be responsible for paying all proper pollution liabilities from the ground up to the IOPC Fund maximum. The Club as guarantor under the "Blue Card" system will also be able to avail itself of the owner's defence under CLC.

However, these defences may not always be available where there are uncertainties about causation or mixed causes to a loss. For this reason it is important for shipowners to have proper War Risk insurance.

3.4.1. International Group Reliance on War Risk Reinsurance

The International Group relies on commercial reinsurance – primarily placed in the London market – to provide the additional layer of Special War Risk P&I insurance.

3.4.2. Bio-Chem Cover

There is an exclusion in nearly all reinsurance contracts globally for claims arising from bio-chemical attack. This exclusion applies to both primary P&I War Risks cover, as well as the IG's secondary layer, Special War Risks P&I cover. The exclusion first generally appeared in reinsurance markets affecting marine insurance in 2003.

For the current policy year the International Group Clubs decided to provide cover for “Bio-Chem” claims in respect solely of crew risks and legal costs relating to all P&I liabilities that are excluded from the War Risks P&I cover by virtue of the “Bio-Chem” exclusion, with a limit of USD 30 million. Claims on this cover will be pooled with the International Group clubs in excess of a Club’s retention of USD 6 million.

The principal provisions are that:

- Cover is from the ground-up (in excess of a Member's usual deductible), but limited to USD 30 million any one event or occurrence (or series of occurrences arising from the same event) each vessel.
- The limit of cover applies to all interests for each vessel in aggregate regardless of the number of interests and regardless of whether or not they are entered in different P&I Clubs (e.g. Owners, charterers and sub-charterers).
- To avoid excessive aggregation of risk, the cover has a cancellation provision (24 hours notice).
- No additional premium is charged for the cover.

3.5. Rating of P&I Club Cover Relating to Piracy, War, Terrorism and Standard Marine Risks

IG Clubs have extensive historical claims information, as well as detailed information about vessels and fleets applying for prospective Membership. Premium ratings for standard marine risk P&I cover are determined by each Club relying on this information.

P&I Clubs view piracy and armed robbery with concern and are aware from information provided by governments, their boards and others of the magnitude of the threat to shipping and the lives of seafarers. Historical patterns of loss combining all claims paid under Club rules assist P&I club underwriters in assessing premium ratings: past losses caused by piracy are therefore reflected in part in P&I premium ratings assessed by individual P&I clubs.

The risk of loss to primary layer War Risk insurance and the IG’s secondary layer of Special War Risk P&I insurance is different, and from time to time the pricing and rating of risk will therefore be different. Claims falling on the primary War Risk layer may not necessarily result in payments under the secondary, Special War Risks P&I insurance.

Both primary and Additional P&I War Risk insurance depend upon, and are influenced by reinsurance markets. Reinsurers make their own assessment of risks, and the occurrence of war or war-like operations, threats of terrorism and other risks.

At the moment, some primary layer War Risk underwriters have followed the market and declared the Straits of Malacca an excluded area, but are not charging an

Additional Premium. Some, it is understood, do not charge an additional premium for transiting the Strait of Malacca but charge an additional premium for certain port calls.

The Special War Risks P&I cover secondary layer offered by the IG does not currently name any geographic exclusion areas for the Strait of Malacca or its ports. The risks of piracy in the Strait of Malacca are not currently excluded, either.

3.6. Summary

P&I Club boards have viewed the provision of adequate levels of marine risk and supplemental war risk P&I insurance as an essential condition to marine transport in the Strait of Malacca and world wide. At this time, IG P&I Clubs offer additional War Risk P&I cover (which includes terrorism risks) of USD 500 million above defined excess points and subject to other relevant policy terms and conditions. The combination of the primary layer and the IG's secondary Special War Risks P&I cover will therefore, subject to Club rules, provide cover for a P&I War Risk up to USD 500 million in excess of the value of the ship, or more where the limit of primary cover exceeds the ship's value.

A significant deterioration of safety or security in the Strait of Malacca, or indeed any other navigational area, would ultimately be reflected in P&I insurance conditions.

Therefore, the International Group welcomes attention and actions which will improve safety and security.

4. Actions Requested of the Maritime Safety Division

The Maritime Safety Division is invited to take note of the information in this Submission.

5. Appendix: Text of a Club's War Risk exclusion for the current 2005 policy year.

E. EXCLUSION OF WAR RISKS

The Association shall not indemnify an Owner against any liabilities, costs or expenses (irrespective of whether a contributory cause of the same being incurred was any neglect on the part of the Owner or on the part of the Owner's servants or agents)

when the loss or damage, injury, illness or death or other accident in respect of which such liability arises or cost or expense is incurred, was caused by:

- i War, civil war, revolution, rebellion, insurrection or civil strife arising therefrom, or any hostile act by or against a belligerent power, or any act of terrorism.
- ii Capture, seizure, arrest, restraint or detainment (barratry and piracy excepted) and the consequences thereof or any attempt thereat;
- iii Mines, torpedoes, bombs, rockets, shells, explosives or other similar weapons of war (save for those liabilities, costs or expenses which arise solely by reason of the transport of any such weapons whether on board the entered ship or not), provided always that this exclusion shall not apply to the use of such weapons either as a result of government order or with the written agreement of the Directors or the Managers where the reason for such use is the avoidance or mitigation of liabilities, costs or expenses which would otherwise fall within the cover given by the Association.

PROVIDED ALWAYS that:

a In the event of any dispute as to whether or not an act constitutes an act of terrorism, the decision of the Directors shall be final.

b The exclusions in this paragraph (E) shall not apply to liabilities, costs or expenses of an Owner insofar only as they are discharged by the Association on behalf of the Owner pursuant to a demand made under

- (i) a guarantee or other undertaking given by the Association to the Federal Maritime Commission under Section 2 of US Public Law 89-777, or
- (ii) a certificate issued by the Association in compliance with Article VII of the International Conventions on Civil Liability for Oil Pollution Damage 1969 or 1992 or any amendments thereof, or
- (iii) an undertaking given by the Association to the International Oil Pollution Compensation Fund 1992 in connection with the Small Tanker Oil Pollution Indemnification Agreement (STOPIA),

to the extent that such liabilities, costs and expenses are not recovered by the Owner under any other policy of insurance or extension to the cover provided by the Association, and

c where any such guarantee, undertaking or certificate is provided by the Association on behalf of the Owner as guarantor or otherwise, the Owner agrees that any payment by the Association thereunder in discharge of the said liabilities, costs and expenses shall, to the extent of any amount recovered under any other policy of insurance or extension to the cover provided by the Association, be deemed to be by way of loan and that there shall be assigned to the Association all the rights of the Owner under any other insurance and against any third party.

d The Directors may resolve that special cover be provided to the Members against any or all of the risks set out in Rule 2 notwithstanding that those liabilities, costs or expenses would otherwise be excluded by this paragraph (E) and that such special cover should be limited to such sum or sums and be subject to such terms and conditions as the Directors may from time to time determine.