# *ΑΚΑΔΗΜΙΑ ΕΜΠΟΡΙΚΟΥ ΝΑΥΤΙΚΟΥ*
# *Α.Ε.Ν ΜΑΚΕΔΟΝΙΑΣ*

# ΠΤΥΧΙΑΚΗ ΕΡΓΑΣΙΑ

**ΕΠΙΒΛΕΠΩΝ ΚΑΘΗΓΗΤΗΣ: ΠΑΝΑΓΟΠΟΥΛΟΥ ΜΑΡΙΑ**

***ΘΕΜΑ***

***P & I CLUB***

***(PROTECTION AND INDEMNITY)***

**ΤΟΥ ΣΠΟΥΔΑΣΤΗ: ΖΑΜΟΥΡΙΔΗ ΔΗΜΟΣΘΕΝΗ**

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***Ο ΔΙΕΥΘΥΝΤΗΣ ΣΧΟΛΗΣ :***

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# INTRODUCTION

Protection and indemnity (P&I) insurance, as administered by the P&I clubs, is probably unique in the way in which it operates. It could certainly be argued that P&I clubs don't really belong to the insurance industry at all but, rather, are part of the shipping industry.

P&I clubs are basically groups of shipowners which, although in commercial competition with each other, have agreed to co-operate and insure each other's liabilities in the spirit of mutuality on a non-profit making basis. For a proper understanding of how the clubs are structured, how they work and the risks covered, it is helpful to understand their historical development. Traditionally most marine liability insurance has been kept separate from the H&M *(Hull and Machinery)* policy. Again to understand the reason for this it is necessary to understand why and how the clubs came into existence.

# I HISTORY DEVELOPMENT

The roots of the P&I clubs can probably be traced back to the early days of the 18th century - the year 1719 to be precise. In that year the British Government passed an Act of Parliament which basically gave a monopoly to just two insurance companies, and certain individual 'names' at L1oyd's, to underwrite marine insurance business. Without the constraints which competition brings, the monopoly holders tried to take advantage of their situation and charge enormous premiums for their insurance cover.

At this point in history a shipowner's main insurance cover was in respect of the hull of its ship. The shipowners in the major maritime cities of Newcastle, Liverpool, Bristol and London decided that they were not prepared to pay these enormous premiums. Although they were acting illegally - the shipowners of those cities formed themselves into associations or 'clubs' with the purpose of agreeing to cover each other's losses or damage to their ships. It would appear that these mutual 'hull clubs' were rather informal organizations with meetings often being held in the back rooms of public houses.


*(1719-1793 LONDON, DOMINIC SERIES)*

When a member of the particular club suffered a loss and had a claim to present, then a 'call' was made around all the members, who would each contribute their share on a previously agreed percentage basis.

The most probable reason why the shipowners were allowed to operate in this illegal way was that their ships were needed by the government. The British Empire was

expanding, which led to considerable increase in trade and made the merchant fleet of Great Britain the largest in the world. Wars with other nations were still regular events, for which the merchant ships were required for carrying supplies and troops. Many merchant ships were indeed armed.

Eventually, in 1824, the government appears to have realised that the insurance monopoly was not working and the Act was repealed

Once competition re-entered the market place, many of the good quality shipowners found that they were able 10 purchase hull insurance on very reasonable terms from the market. This provided them with the security of not only knowing that they would not lose financially if their vessel sank but also they could build the costs into their operating budget and know exactly how much they would need to pay each year. This was something they had not been able to do with the mutual clubs since what they paid, and when, depended upon how many claims were made by the individual members of their club.

As time went on, more and more shipowners moved to the market for their insurance which left the clubs with only the bad tonnage which couldn't obtain insurance on the commercial market. Their future survival therefore looked rather bleak. However, a number of events occurred which were to put new life-blood into some of those clubs.

In 1836 the court was considering a collision incident- the case of ' De Vaux v. Salvador'. However, the interest was not so much in the collision itself but rather in the cover which was, or was not, provided under the standard hull policy in use at that time, particularly with regard to the liability for damages and compensation to the other vessel in the collision. The judge agreed with the hull underwriter that there was no cover provided for the liability damage under the hull insurance policy. This case raised considerable concern across the entire shipowning community for it meant that they had a very large exposure to such liabilities but had no insurance cover.

The shipowners subsequently met with the underwriters and a compromise was reached. The underwriters agreed to cover the collision or 'running down' risk but only to the extent of three fourths -leaving the shipowners to cover the remaining one fourth themselves. The idea seems to have been that the underwriters believed that the shipowners would be more careful with the navigation of their vessels if they were carrying a share of the risk. Indeed, this three fourths 'running down clause' (RDC) is still a standard clause in the usual hull insurance terms written on the London market.

However, the shipowners considered that the one fourth running down risk was potentially too large to carry themselves and they decided to rum to the mutual hull clubs to see if they would provide the insurance cover they required. The clubs appear to have been happy to oblige and cover the one fourth RDC.

Following on from the industrial revolution, a new group of people emerged - the so-called 'working class'. The working classes had very few rights and were often

exploited by those in control of the means of production. For example, if a worker was killed even as a result of clear negligence on the part of his employer the family could not obtain any compensation - any claim died with the worker. In 1846 Lord Campbell presented a paper to parliament increasing the rights of workers and making their employers more responsible. This Act was passed and employers, including shipowners, realised that they were now potentially exposed to these financial liabilities and for which they required insurance cover.

Other changes in legislation, such as the Factory Acts and Workmen's Compensation Acts were also introduced bringing sweeping reforms in the liberalism which was to dominate much of the reign of Queen Victoria. There were also large numbers of people travelling by ship at this time - often emigrating from Europe to the Americas, Africa, Australia and New Zealand. Such travelers also posed potential financial risks and liabilities to the shipowners should they be injured or killed when on board.

In 1847 another law was passed making shipowners responsible for damage caused to piers, jetties and another harbour property.

The shipowners seemed to feel that they could better control these risks and liabilities if they insured them themselves and they therefore again turned to the mutual hull clubs, which were prepared to provide the protection and cover necessary.

The entire nature of the business of those hull clubs had thus changed. Accordingly one of the firms of hull club managers, Peter Tindal Riley and Co., was asked to set up and run a mutual club specifically to provide protection against these risks. The Shipowners' Mutual Protection Society was formed in 1855. Tindal Riley is still a club manager today and manages the Britannia P&I club.

Cargo claims do not appear to have posed a serious problem for shipowners during the middle of the 19th century, which may appear a little strange since English law imposed an almost strict obligation as far as seaworthiness was concerned. This meant that if the cargo was damaged after it came into the custody of the shipowner due to some unseaworthiness, then it would be liable to compensate the cargo owner regardless of any mitigating factors.

However, there was another area of English law which allowed almost total freedom of contract. Shipowners therefore took advantage of that situation and inserted in their bill of lading contracts some extensive exclusion clauses. The clauses basically excluded the shipowners from liability for any loss or damage to the cargo howsoever caused. The shipowners were in a powerful position and basically if a cargo shipper wanted goods moved, then it would need to agree to the bill of lading terms.

But an incident occurred involving a vessel called the Westerhope, which came to be considered by the courts in 1870 and which was to pose a most serious challenge co the secure position which the shipowners believed they held. The Westerhope was

fully loaded with cargo and the bills of lading contained the usual wide exclusion clauses exonerating the shipowner from all liability for loss or damage to the cargo.

The vessel was bound for discharge ports in South Africa. However, she sailed past her scheduled discharge port and on up the East African coast for reasons involving the shipowner's business unrelated to the cargo voyage. On her way back to the scheduled discharge port, the vessel sank with the loss of the entire cargo. The owner of the cargo commenced an action against the shipowner for loss of the cargo. The shipowner pleaded the wide exemption clauses of the bills of lading. The judge decided that by sailing past the schedule discharge port the vessel had deviated unreasonably from the contracted voyage and, if it had not been for that deviation, then the cargo would, in all probability, have arrived safely at the intended destination. The deviation constituted a fundamental breach of the contract of carriage meaning that the contract came to an end once the vessel had deviated and consequently the shipowner could not rely upon the terms of bill of lading and in particular the exemption clauses. The shipowner was found liable and had to compensate the cargo owner for the loss of the cargo.

The shipowner turned to its protection club and asked the board to indemnify it for the claim. The club refused, pointing out that liability towards cargo owners was not covered.

A marine underwriter in Newcastle, J. Stanley Mitcalf, had been carefully following the Westerhope case and, once the judgment had been handed down, he wrote a detailed article which appeared in all the shipping press of the day. This drew the attention of shipowners to many risks and liabilities to which they were exposed with regard to potential cargo claims and for which they had no insurance. A number of shipowners took Mitcalf's article very seriously and asked him to form a mutual club to provide them with indemnity cover for these risks. The first indemnity club was formed in 1874, called The Steamship Owners Mutual Indemnity Association.

The protection associations and the indemnity associations continued to grow during the following years and existed side by side in the same cities and often with the same shipowners on the boards. Eventually in 1886 a group of shipowners in Newcastle recognised that it made sense to amalgamate the protection and the indemnity risks under one roof and agreed to a merger of the North of England Protection Association with the Steamship Owners Mutual Indemnity Association to form the very first full P&I club - the North of England Protecting and Indemnity Association.

The clubs continued to grow and develop and most of the current P&I clubs had been formed by the beginning of the 20th century. The increasing demand for ships to cope with the increase in trade and passengers / emigrants put increasing demands on the P&I clubs. As the clubs responded and strengthened, then more businessmen felt confident to venture into shipowning or to expand their existing fleets and thus each industry was leading to the development of the other. New laws were passed defining

the shipowners' legal liabilities and also providing them with a legal right to limit their financial liability. Initially the Harter Act in the US and later the Hague Rules and Carriage of Goods by Sea Act of 1924 provided a clear framework of liability and responsibility for the carriage of goods, which helped considerably with the provision of mutual P&I insurance cover for cargo claims.

All P&I clubs work on the same policy year running from noon GMT on the 20th February of one year to noon GMT on the following year. The clubs had in fact inherited this tradition from the mutual hull clubs. Historically ships trading from Great Britain into the Baltic Sea would lay-up on the River Tyne at Newcastle during the winter months while the Baltic was ice-bound. During this time they did not require their normal insurance since they were not trading. The 20th February became recognised as the first day when masters and owners could be sure of sailing from the Tyne and finding the Baltic ice-free. Consequently, they needed their normal insurance to resume on that date.

# II NATURE OF P&I CLUBS AND INDUSTRIES

The P&I clubs responded to the changes in legal obligations of their shipowner members by providing the relevant cover when necessary. However, the P&I clubs of today have not changed substantially from those early days when they were first formed. They are still groups of shipowners, insuring each other liabilities on a mutual, non-profit making basis with the shipowner members actually owning the club and comprising the board of directors. The only real difference is that no longer are the clubs made up just of the local shipowners of Newcastle, Liverpool, Bristol or London but rather are representatives of the entire international shipping community.

Most of the P&I clubs, while maintaining their independence and autonomy, agreed to co-operate with each other. This was to spread the financial risk of larger claims by sharing those risks across all the clubs and also to take advantage of the resulting bulk purchasing power to buy a single reinsurance for the very large potential claims. The first London Group of P&I clubs was formed in 1899 with the International Group being formally constituted in 1979.

There are currently 14 P&I club members of the International Group and between them they provide liability insurance for more than 90% of the world's shipowners. The current members of the International Group are as follows:

• Assuranceforeningen Gard (Gjensidig) (Norwegian)

• Assuranceforeningen Skuld (Gjensidig) (Norway and Denmark)

• The Britannia Steamship Insurance Association Ltd.

• The Japan Ship Owners' Mutual Protection and Indemnity Association

• Liverpool and London Steamship Protection and Indemnity

• The London Steamship Owners' Mutual Insurance Association Ltd.

• The North of England Protecting and Indemnity Association Ltd.

• The Shipowners' Mutual Protection and Indemnity Association

• The Standard Steamship Owners' Protection and Indemnity Association Ltd.

• The Steamship Mutual Underwriting Association Ltd.

• Sveriges Angfartygs Assurans Forening (The Swedish Club)

• The United Kingdom Steamship Assurance Association (The UK Club)

• The West of England Shipowners' Mutual Insurance Association

• The American Club

Each P&I club has its own individual identity and profile with its own group of shipowner members. Some clubs, such as North of England, employ their own managers and staff to run the club on a day-to-day basis. Other clubs employ a professional commercial management company; some of the well known managers include

• Tindal Riley (Britannia)

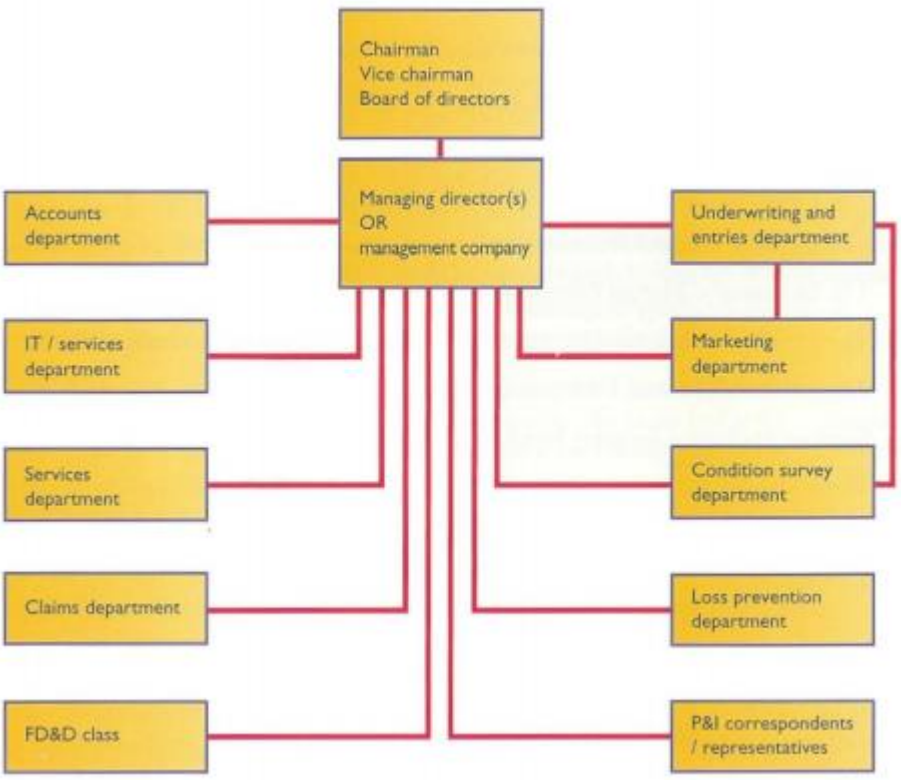
• Thomas Miller (UK Club)

• Charles Taylor (Standard)

• A Bilborough (London).

Most of the UK based clubs have registered offices in offshore centers such as Bermuda and Luxembourg and reference to those countries may appear in the full style of their name e.g. The West of England Shipowners' Mutual Insurance Association (Luxembourg). However, the day-to-day running of the club will be from a London or regional office.

Each individual club will have a board of directors who will be actual shipowner representatives of the club membership. The board will meet a number of times each year to consider important issues affecting their own club as well as the International Group generally. Depending upon how the particular club is structured, there will either be managers and staff directly employed by the club or else a firm of managers will be employed to run the club on a day-to-day basis. In either case they will have a similar internal structure. There is a typical department plan within the club: (Pic 2.1)




(Pic:2.1 *(Source: Google Images))*

Because P&I clubs are predominantly service orientated, the largest department is usually the claims department. Often this is staffed with experienced lawyers, ex-shipmasters and other suitably qualified professionals. There will also be an accounts department and an underwriting department, both very much involved in cash flow. In addition, a P&I club may also have further departments having special responsibilities such as loss prevention, ship inspection, services, quality assurance and marketing. There may be a separate department running the FD&D class - usually staffed by specialist lawyers. Another important pan of any P&I club is the network of correspondents and representatives in every major port and most minor ports around the world.

On board ship the master, and indeed the officers, should have available a list of the correspondents and representatives for the P&I club in which that particular vessel is entered (see Pic2.2).

Many of the correspondents around the world may represent all of the International Group clubs. They are not actually employed by the P&I clubs directly nor are they strictly speaking agents in the legal sense. They are more like an ad hoc newspaper correspondent, who are usually only paid when actually reporting.

The P&I correspondents tend to be experienced individuals, either maritime lawyers or commercial professionals such as average adjusters, ships' agents or surveyors with excellent local knowledge. Their value is often under-rated as they can make all the difference between a problem being handled in a controlled manner, resulting in the

shipowner's and club's position being protected while causing minimum delay to the vessel, and the problem getting out of hand leading to the ship being arrested or falling foul of local authorities.

The master should not hesitate to call in the local P&I correspondent at the first signs of a P&I incident arising. The correspondent is likely to be the best friend he has in that port and will be there to assist, protect and advisee the master in some very difficult situations. The master should always ensure that his officers also know where the P&I club list of correspondents is kept on board and to give them instructions that, in his absence, they should not hesitate to call in the correspondent if a P&I incident has happened or a situation is developing which looks as though it may turn into a P&I incident.

The local correspondent will have access to local surveyors, lawyers and other experts to provide 'first-aid' cover in the event of need and also the expertise available at the head office of the P&I club. If a correspondent is called in then the master should advise his owner / manager at the first opportunity, which in turn should advise the head office of the P&I club.

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**Africa Marine Services (Ghana)**
A/B 7, Community 11 PO Box CO. 1191, Tema — Capt. S D Darty

Tel 303 306619
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*In case of communication problems please contact Africa*

**GIBRALTAR (+350)** — **Gibra**

**Inchcape Shipping Services (Gibraltar) Ltd.**
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Tel 200 72 685/200 79 294
Fax 200 75 959
Email iss.gibraltar@iss-shipping.com
Web iss-shipping.com

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**GREECE (+30)** — **Athen**

**Shipserve (International) Inc**
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*(Pic 2.2 Source: https://www.yumpu.com/en/document/read/27495555/albania-355-algeria-213-angola-244-all-uk-pi )*

In addition to co-operation between the P&I club members of the International Group with regard to sharing the larger risks and purchasing the group reinsurance for the very large claims, the clubs also co-operate in many other ways. There are many group committees and sub-committees covering subjects as diverse as club correspondents, ship condition surveys, salvage contracts, passenger contracts, bills of lading and charterparties. The International Group will usually be involved with other organisations such as BIMCO(Baltic and International Maritime Council) , the ISU and IMO, where the group has consultative status when new documents are being drafted or changes in maritime legislation are being considered. There is also a formal agreement between the clubs covering various issues, known as the International Group Agreement (the IGA).

The IGA has come under some very careful scrutiny in recent years from the competition directorate (DGIV) of the European Commission because certain parts appear to contradict the freedom-of-trade provisions of the Treaty of Rome. The group clubs operate what some have considered a cartel. Under the IGA, for example, if a shipowner wishes to leave one group club and put its ships in another group club, there are a number of procedures which must be followed and restrictions which apply. The new club is not allowed to offer any financial inducement, such as reduced premium, to entice the shipowner across.

Indeed the new club is obliged to follow the premium being charged by the existing or 'holding' club, at least for the first year. The reason is that the holding club is in a much better position to assess the risk and potential claims level of that particular shipowner based upon its own knowledge of that owner's past claims record. The holding club is obliged to disclose details of the claims record of a particular member to another group club on request if that club has been asked to 'quote' for the business. The holding club must also provide the current call rating (the level of premium being charged) and loss ratio (the ratio derived from comparing the amount of money the particular member pays into the club in calls with the amount received in paid claims).

The shipowner will need to either pay a 'release call' to the holding club or otherwise provide a suitable guarantee to cover any future liability for calls to the club before it is allowed to leave. The reason for this is that P&I clubs work on a mutual basis of underwriting rather than the fixed premium of other types of insurances and, as such, will not know how much money they will need from their membership to pay claims for maybe four or five years after the calendar end of the particular policy year.

The new club will not be allowed to accept the new business until the holding club confirms that all outstanding debts, including release calls have been cleared. Some of this may appear, from the outside, to be rather unreasonable but it actually introduces considerable stability to the P& I industry. What must also be remembered is that more than 90% of the shipowners of the world actually want it to be like that.

There are a number of very respectable P&I clubs which exist outside of the International Group providing cover for shipowners which perhaps do not require the full range and very high levels of financial cover offered by group clubs - for example, the coastal and river barges of the Netherlands and Germany. There are other non-group clubs which are perhaps prepared to accept ships which the group clubs will not accept for various reasons. There are also a growing number of 'fixed-premium' facilities becoming available offering P&I type cover. Each individual shipowner or ship manager, possibly with the advice of professional specialised brokers, will need to decide which club or facility will be best for them.

# III P&I UNDERWRITTING

P&I clubs do not issue policies of insurance but rather provide each of their members with a rule book which sets out the terms of the relationship between the member and the club, such as defining the risks covered, the risks not covered and the rights, duties and obligations of the members and the club towards each other.

The member is also provided with a 'certificate of entry', which not only confirms that the particular ship / shipowner is entered but also sets out any special terms and any variations on the standard terms of entry as well as setting out the appropriate deductible. A copy of this rule book should be available on board every entered ship.

To appreciate fully the significance of P&I claims to the shipowner and the master, it is necessary to understand the way in which the underwriting is organised and how it works because it is very different from almost any other kind of insurance. The most fundamental difference is that a shipowner member of a P&I club does not know at the beginning of a policy year just ho,,· much his insurance will cost it for that year. Indeed it maybe four or five years before it knows.

When an individual insures his house or car, for example, he will be advised by the insurance company what the premium will be and what the risks are that will be covered for that premium. The individual pays that agreed fixed premium and can rest assured that he will be protected against those specified risks, with the financial limits agreed, for the agreed period of time. With P&I insurance, however, the P&I club underwriters will advise each shipowner member what they think they will need to pay - this figure is known as the estimated total call (the ETC).

The ETC has two component parts: the advance call and the supplementary call. It is anticipated that both the advance call and the supplementary will be required and consequently the shipowner should budget accordingly. What each individual member will have to pay will vary considerably even between members operating very similar vessels. The type, size and age of the vessels are certainly factors the underwriters will take into account when calculating what each individual member's call will be. They will also look at things such as the trade in which the vessel is involved, nationality of the crew, the flag, the classification society and similar factors.

However, the real influencing factor is the past claims record of that member. A member with a bad claims record will be paying a much higher call than a member operating similar vessels but with a good claims record. This method of calculation goes to the very heart of the principle of mutuality.

Basically the club needs to 'call' in sufficient funds to pay all the valid and legitimate claims which arise during a particular policy year, including contributions towards larger claims which are shared - or more correctly 'pooled' - across all group clubs together with a share of the reinsurance premium for the very large claims, plus the administration costs of the club. In addition to call income the club may have a fund of reserves invested, the income from which can be used to reduce the call levels.

Because the majority of the calls from the shipowner members will be used to settle claims arising during that particular policy year, those funds will not actually be required immediately. Most clubs would not need to call the full amount of the ETC at the beginning of the policy year, believing that the members would prefer to have the use of those funds until they were actually required by the club. Accordingly the club would ask for the advance call to be paid during the policy year - often as three instalments spread throughout the year.

At the end of the policy year an analysis is carried out looking at all claims notified to the club during the year and a financial estimate is placed against each claim as to what funds might need to be made available to settle it. Because many types of claims have a prescribed period within which a legal action would need to be commenced, for example cargo claims subject to the Hague-Visby Rules have a one year time limit, there may be a number of claims which have arisen within that policy year but which have not yet been notified to the club. These are known as *'incurred but not reported*' (IBNR). From past experience the level of IBNRs can be calculated with a reasonable degree of accuracy.

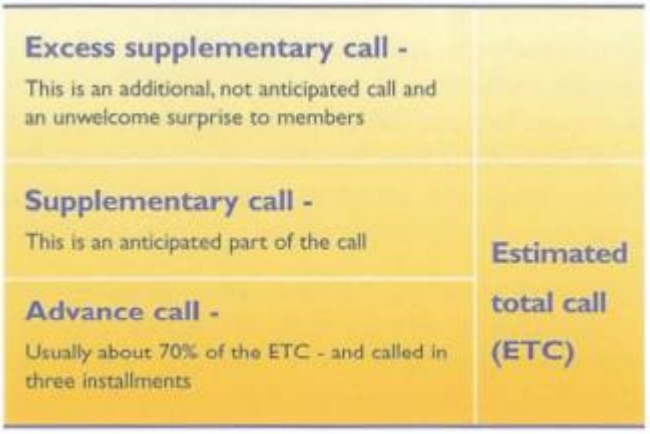
The total of the known claims and the IBNRs are calculated and this figure is then compared with the originally forecast figure to decide whether the original ETC was accurate. Based on the results of that assessment, it may be concluded that the original calculation was reasonable and therefore the supplementary call would be made, either in part or in whole. The important point to note though is that there is absolutely nothing unexpected in calling the supplementary. What would be unexpected, and indeed unwelcome, is if an 'additional' or 'extra supplementary call' had to be made. This would arise where the level of claims and IBNRs significantly exceeded the original forecast levels and consequently more money would have to be called in to settle all the liabilities. Alternatively the club could use some of its reserves.

The assessment of the policy year does not actually end at that particular policy year. The policy year will be left 'open' and will be reviewed again, usually after a further 12 months and 24 months with more frequent or further reviews as considered

necessary. At each assessment the member may be asked to pay further supplementaries or it may be reconfirmed that the original anticipated supplementary will not actually be required - it all depends upon the actual level of claims experienced by all the members of that club.

If there are more claims, all the members have to pay more; if specific members are the ones having the claims, then their loss ratio will increase and they will have to pay more into the club. h can therefore be seen that even though the shipowner does have an insurance for liability claims with its P&I club, more claims mean the shipowner will have to pay more to the club. Pic 3.2 shows the structure of the clubs calling system.

(*Pic 3.1ETC calls)*




Each club member of the International Group spreads the costs of the relatively smaller claims across its own membership, it then shares the cost of larger claims across all group clubs and jointly purchases what is one of the largest single insurance policies in the world - the International Group excess loss reinsurance policy for very large claims. There is another level of cover even beyond the upper limit of the reinsurance contract. This is called 'overspill', which would be covered by all the members of each club in the group.

The figures for the various layers can change from year to year. In 2012 they were as follows:

## Retention

The first layer is called the individual club 'retention'. This is where the vast majority of all the claims will fall and will be paid out of that clubs own funds, although it is not unusual for individual clubs to purchase additional reinsurance to cap the level of claims to which it might have to face within the retention through stop loss or excess of loss policies, for example. In 2012 the retention covered any individual claim up to a maximum of US$5,000,000.

## Pooling Agreement

The second layer is the 'pooling agreement'. This is where all the clubs of the group spread the risk, and the cost, of relatively high level claims. In 2012 the pooling agreement covered individual claims which fell between the retention of US$5,000,000 and USS30,000,000. Each club contributes to the pool in accordance with its relative size that is by number of ships and in terms of tonnage and also taking into account that club's own past claims record in the pool. Contributions are

called as and when they are actually needed. A small part of the pooling agreement actually extends up to US$50,000,000 but this is more by way of the group taking a share in the reinsurance contract.

### Excess Reinsurance Contract

The third layer is the excess reinsurance contract itself. This provides cover beyond the 30MillionsUSD of the pooling agreement up to a maximum of 500MillionsUSD in respect of pollution claims and 2BillionsUSD per claim for other categories.

For most of the history of the P&I clubs there was no upper limit of cover - it was, in theory at least, unlimited. However, in 1996, a decision was made to introducec an upper limit for the potential 'overspill' claims, that is a claim which might exceed the upper limit of the group reinsurance contract. The figure which was introduced is not a fixed figure, it is based on a percentage of the tonnage limitation figure of all the vessels entered in all the International Group clubs. In 2012 it was approximately US$4.25 billion.

The oil spill from the Exxon Valdez in 1989 actually resulted in claims exceeding 5BillionUSD but the P&I club exposure in 1989 was limited to US$400,000,000 and was not subject to the overspill provisions. The Exxon Company had to cover the bulk of the claims out of its own resources.

Approximately 70% of the funds called in by a P&I club are used up in paying claims within the 5MillionUSD retention. The other 30% (approximately) is used in contributions to the pooling agreement, the cost of the reinsurance contract and the administration of the club.

Within the context of P&I underwriting, it is worth remembering that the clubs need to call in sufficient funds to pay the claims. There is thus a direct relationship between the cost of P&I insurance and the claims actually experienced - particularly the relatively smaller claims falling within the retention. If those claims could be reduced or even avoided altogether, then significant reductions could be made in the cost of P&I insurance.

Money that is not needed for paying claims and calls could be used for much more useful purposes such as training, additional crew, maintenance, new buildings and maybe even higher salaries, better conditions and more leave for those on board. Every single person involved does have a very direct interest in working towards the reduction of claims.

## IV Scope of Cover

Another unusual fact about P&I clubs which also make them very different from almost any other insurance provider is that they do not actually know the full range of risks that are covered. The club will set out in its rule book certain risks and liabilities which are specifically excluded, such as risks that are normally covered under the

H&M policy and freight/hire, and they will set out a long list of risks that are included. However, that list of risks included is open-ended - it is only a list of the types of things covered. Within the club rules there will be an 'omnibus rule' covering risks incidental to shipowning. The inclusion of this rule provides the directors of the club with the discretion to approve claims from members for risks and liabilities which are not specifically 'included' in the rule book provided it is similar to the other types of risks covered by the club.

The directors of a P&I club do in fact have an considerable amount of discretion given to them under the clubs rules with regard to providing rather than denying cover to members. Again. it is these sorts of areas which make P&I clubs very different from any other type of insurances. It is the shipowners members sitting as directors, making the decisions as to what claim they will accept and which claims they will reject. Of course if a director has a personal interest in a particular case then he would not be allowed to use his own discretion or otherwise influence any decisions of his fellow directors.

The scope of cover provided by anyone P&I club member of the International Group will be almost identical with the cover provied by any other member club, although the specific wording may vary slightly. The reason for this is that all the clubs are sharing in the larger claims through the pooling agreement and also in the cost of the reinsurance contract. It would therefore he unfair and unworkable if each club was covering different risks and liabilities.

In addition to the heads of risk specifically identified in the rule book. the club also covers the costs of correspondents, lawyers, surveyors and other experts who may be needed to investigate or otherwise handle and deal with a particular problem. The claims will be subject to a deductible which the member will have agreed with the underwriters at the time of renewal. These deductibles - which are that part of the c1aim which the member will pay it - can vary from a few hundred or a few thousand dollars to many tens and even hundreds of thousands of dollars.

Set out below is a list of the heads of cover specifically identified by a typical P&I club:

- liabilities in respect of seamen
- liabilities in respect of supernumeraries
- liabilities in respect of passengers
- liabilities in respect of third parties
- stowaways
- diversion expenses
- life salvage
- person in distress
- quarantine
- liabilities arising from collisions

- non-contact damage to ships
- damage to property
- pollution
- wreck removal
- towage
- contracts, indemnities and guarantees
- liabilities in respect of cargo
- general average
- fine
- legal costs, sue and labour
- risks incidental to ship owning
- special cover
- special cover for salvors
- special cover for containers
- special provisions for charterer's entry.

The percentage breakdown of claims under the different liability categories will vary from club to club and will be influenced by the membership profile of the particular club. For example, a club with a large tanker entry may show a relatively large proportion of pollution claims and a c1ub with a large passenger ship entry may show a relatively larger number of passenger injuries.

The following figures (Pic 4.1 & Pic 4.2) show the experience of a medium-sized club with a fairly even spread of members for a particular policy year.

*Pic:4.1 Percentage breakdown of claims by number (Source North of England P&I - policy year 2012)*

*Pic:4.2 Percentage breakdown of claims by value (Source North of England P&I - policy year 2012)*


It can be seen that by far the largest single category of claims both in number and in total value are cargo claims, followed by personal injuries and illness. What is interesting is that the number of collisions and damage to property incidents is relatively small -representing a mere 7% of the total claims. However, together they represent about 25% of the total claims by value. The above list of liabilities can be shortened since most of the liabilities covered by a P&I club can probably be included under one of three general headings:

1. liabilities in respect of people
2. liabilities in respect of cargo
3. liabilities in respect of ships.

## Liabilities in respect of people

A shipowner has a general duty of care towards anyone who comes on board its ship or even finds themselves in proximity of the ship. It must provide a safe access to and from the ship it must not allow unauthorized people to wander around the ship, it must provide safe routes around the ship as well as a safe work place and generally a safe environment where all reasonable steps have been taken to prevent people being injured. If the owner fails in this duty of care and someone is injured as a consequence then, provided the c1aimanr can demonstrate that the owner was in some way negligent, they will be entitled in many jurisdictions to bring a claim for damages against the owner.

Such people might include members of the crew, passengers, supernumeraries and third parties such as stevedores, pilots, port officials, P&I surveyors and even people who should not even be on board such as stowaways. In addition to this general obligation of a duty of care, a shipowner will also have specific contractual obligations to certain categories of people such as the crew under the relevant crew contract and passengers under the passenger ticket contract. Crew contracts differ widely in the conditions of service offered and this includes compensation payments in respect of illness and injuries suffered. Passenger contracts may include the terms

of an international convention such as The Athens Convention, which sets out the respective responsibilities and liabilities including financial limits of liability.

The P&I club will cover the shipowner member for most liabilities to people in negligence and in contract, as well as under certain domestic laws and statutes such as health and safety at work acts, or the Jones Act in the US. It is essential that the P&I club managers be given the opportunity of reviewing the respective on tracts prior to agreeing financial terms for the insurance.

In addition to compensation to the injured individual or his or her family if deceased, along with all the hospital and other medical bills, the club will also reimburse the shipowner for the costs of any necessary repatriation expenses of the injured person and the costs of sending out a substitute. Neither the shipowner nor its P&I club operate private health insurance although the extend of cover being provided in some crew contracts could be viewed by some as getting very close to that position.

There may also be other incidental expenses which the shipowner may have, incurred such as the costs of fuel, wages and other expenses while diverting to land a sick or injured individual. In certain circumstances the club may also cover loss of or damage to the personal property of the crew if the shipowner has such a liability towards its crew.

Another important and significant head of claim which could fall into the category of liabilities in respect of people and which is becoming an increasingly difficult and expensive problem to deal with is that of stowaways. The P&I club would usually expect to see evidence that the member had taken reasonable steps to prevent stowaways coming on board and to detect them prior to sailing.

Subject to that caveat the P&I club will cover a member for the direct costs incurred in having the stowaways on board as well as the costs of supplying guards, when necessary, and the expenses involved in repatriating the stowaways back to their home countries. Sometimes this process of repatriation can not only be very expensive but also extremely frustrating when the stowaways have hidden or lost their identity papers, will not cooperate by declaring their true details such as name and nationality, and where ports and countries of call will not assist - which is becoming increasingly common. Sometimes the ship is even fined for having the stowaways on board, but usually the club would cover such a fine.

The costs of diverting the ship to a suitable port to remove the stowaways will also be covered by the P&I club. However, on this point, it is important to remember that if the ship is loaded with cargo and diverts to land stowaways, then this may very well constitute an unreasonable deviation from the contracted voyage and as such mean that there has been a breach of the contract of carriage. The shipowner may then lose the rights and exemptions of the Hague-Visby Rules, for example, as well as the right

to limit its financial liability for cargo claims which might arise in consequence of, or during, the deviation and may also prejudice and lose its P&I Insurance cover. This applies to any 'unreasonable deviation'.

If the deviation to land the stowaway is merely because it would be convenient to the shipowner to do that at the particular port then the deviation would probably, from a legal point of view, be considered unreasonable. If the deviation was to land 20 stowaways who were turning violent and dangerous on board a vessel with a crew of only 18 then it may very well be considered to be a 'reasonable deviation'. As such there would not have been a breach of the contract of carriage, no loss of rights and no loss of P&I cover.

## Liabilities in respect of cargo

The first important point to realise is that neither the shipowner nor the P&I club is a cargo insurer, and nor is the club offering cargo insurance to the shipowner. The prudent owner of cargo will need to insure its cargo properly. However, if the cargo becomes lost or damaged while in the custody of the carrier, usually the shipowner, then the carrier may very well have to compensate the cargo owner unless it can bring itself within one of the exemptions of the Hague-Visby Rules, for example.

The cargo owner may not wish to have the trouble of pursuing a claim against the carrier, even though this may preserve its own insurance record. It is usually much easier to present its claim to its cargo underwriter. However the cargo underwriter that has compensated the cargo owner can now bring a claim against the carrier in the name of the cargo owner. This right is known as subrogation.

The majority of cargo claims are brought against carriers by subrogated underwriters. These cargo claims are frequently dealt with by recovery agents acting on behalf of the cargo underwriter and the P&I club claims handler on behalf of its member.

As seen from Pic4.1 and Pic4.2, cargo claims generally represent by far the greatest number and value of any category of claim handled by a P&I club. As a result of this, the claims handlers in the club will have a considerable amount of knowledge about all different types of cargoes and all manner of problems with cargoes.

Under regimes which have incorporated the Hague or Hague Visby Rules into their domestic legislation, often under a carriage of goods by sea act (COGSA) or as part of their national commercial code, there are a series of obligations imposed upon the carrier. Article III, rules 1 and 2 of the Hague - Visby Rules set out the most important obligations and it is a failure on the part of the carrier which leads to most of the cargo claims handled by P&I dubs. If either of these rules are not complied with then it is very unlikely that the shipowner can rely upon the long list of defences which are set out in article IV rule 2.

To understand exactly what son of cargo liabilities the P&I club will be covering it is worth looking at what article III. rules 1 and 2 actually say.

*(Pic4.3: Cargo claims are the largest category of claims handled by P&l clubs)*

*Article III*

*Rule 1: The carrier shall be bound before and at the beginning of the voyage to exercise due diligence to:*

*a) Make the ship seaworhtly*
*b) Properly man, equip and supply the ship*
*c) Make the holds, refrigerating and coal chambers, and all other parts of the ship in which goods are carried, fit and safe their reception, carriage and presentation.*

*Rule 2: Subject to the provisions of Article IV, the carrier shall properly and carefully load, handle, store, carry, keep, care for and discharge the goods carried.*

The obligation in both these cases is one of 'reasonableness'. It is not a strict obligation of seaworthiness but the shipowner, usually through the activities of the master, officers and crew, must show that they did all that was reasonably and realistically possible to check and ensure that the ship was in all respects seaworthy and in a suitable condition to load the intended cargo.

If problems subsequently arise which do lead to the cargo being damaged and which would, from a legal and technical point of view, be considered as being the result of

some unseaworthiness, then the shipowner can still rely upon the various defences and exceptions provided it can prove that whatever happened could not have been discovered or detected by the exercise of reasonable care.

In reality it is very difficult to discharge the burden of proof completely. To what extent a claim can be defended will depend almost completely on the quality of the evidence available from the ship. Consequently most cargo claims tend to be settled on an amicable, out-of-court basis with each side arguing its own strong points until a reasonable compromise can be reached. The better the quality of evidence from the ship, the better the chance the club will have of either repudiating liability or of settling on nothing more than a nuisance-value basis.

On the other hand, if it is clear that the claim is indeed justified, then it may be more prudent to settle on the best possible terms without incurring any further legal or other expenses.

The most common types of problems which lead to cargo damage and consequently to claims include leaking hatch covers ventilators or other openings into the cargo compartments. In most cases it would be very difficult to prove that the proper checks and inspections had been carried out on these closing devices since, if they had been the subject of a reasonable check, then they would have revealed the problem - which is often the result of corrosion, defective or missing rubber gaskets or securing arrangements. An argument of 'heavy weather' or 'perils of the sea' is unlikely to succeed except in the most extreme of circumstances.

Other common causes of damage to cargo occurring after it has come into the custody of the carrier is dirty or inadequately prepared cargo carrying compartments. These may be the cargo holds of a bulk carrier or the tanks of a product carrier. Often it is the remnants of the previous cargo which damages the current cargo. This type of contamination can lead to enormous claims from the cargo owners for compensation - particularly with liquid cargoes - where the product may no longer be capable of being used for its intended purpose. This lack of preparation of the cargo compartments would render the vessel uncargoworthy, which is synonymous with unseaworthiness as far as Hague-Visby Rules are concerned, for example.

Cargo can often be damaged as a result of being inadequately ventilated. The ventilation may have been deliberately suspended, for example as a result of heavy weather, or the ventilation given may have been wholly inappropriate as a result of a lack of appreciation or understanding of the ventilation requirements of the particular cargo by those on board ship. Whether or not a shipowner will be able to raise a valid defence to a cargo claim in respect of damage from inadequate ventilations will depend entirely on the contemporaneous evidence available from the ship.

When cargo is loaded on board, a bill of lading will usually be issued and amongst other things, it will usually state the number of pieces or quantity of the cargo loaded. The carrier will be obliged to deliver this quantity of cargo to the cargo receiver at the

agreed destination. If there is a shortage then the shipowner will be obliged to compensate the cargo owner for this loss unless it can provide a very good explanation as to where the cargo has gone or why there may appear to be a shortage on paper.

Again, if the shipowner or club is to stand any chance of defeating such shortage claims, they must have available to them good quality evidence from the vessel by way of draught surveys, tally reports and similar contemporaneous documents confirming what quantity of cargo was loaded and what was discharged.

If the shipowner does have to settle claims for loss, shortage or damage to cargo then it will usually be provided with cover by the P&I club, subject to certain provisos.

Most cargo claims would fall into the category of loss and damage. However, there may be additional charges, expenses or losses with which the shipowner is faced in dealing with a cargo problem or potential problem. For example, a cargo of grain may be damaged, say due to leaking hatch covers, and additional expenses need to be incurred in trying to separate as much sound cargo from damaged cargo. These additional expenses would be covered by the club.

The damaged grain may have to be officially destroyed, say by incineration. These and related costs would be covered by the club. A situation might arise where a cargo may need to be resecured after sailing from the load port. It may be thart the ship and cargo are nor in immediate danger - and consequently it is nor a General Average situation - but if the resecuring is nor undertaken then a dangerous situation may very well develop during the ocean passage. The cost of diverting and of resecuring the cargo for the safe prosecution of the voyage would he covered by the P&I club.

Special arrangements may have been made with the P&I club, usually by paying additional premium, for the member to be covered for obligations under through transport or transhipment bills of lading that is for liabilities which might arise within a multi-modal transport system. If those special arrangements have been made with the club, then cover will he provided.

It is also worth mentioning that ships are frequently operating under charterparties.

Whereas there will be liabilities to he considered between the shipowner and the cargo owner under the terms of the contract of carriage evidenced by the bill of lading, there will also be various obligations between the shipowner and the charterer arising under the terms of the relevant charterparty. In many cases, if a shipowner is found to have a liability towards a cargo owner, or subrogated cargo underwriter, under the terms of the contract of carriage evidenced by the bill of lading the shipowner may very well have a legal indemnity claim against the charterer under the charterparty.

Consequently the shipowner would make a recovery from the charterer rather than from the P&I club. Alternatively, a charterer may be considered to be the legal carrier

under certain bills of lading and it may be the charterer which has to deal with cargo claims in the first instance. It may therefore be the charterer which brings the indemnity claim against the shipowner under the terms of the charterparty. Under normal circumstances the charterer cannot take advantage of the shipowner's P&I cover but rather would take out its own, independent, cover.

There are numerous charterparty forms but often there will be provision whereby the charterer has a responsibility with regard to the loading and stowing of the cargo. For example, in a GENCON Voyage charterparty form, there is a 'free in and out stowed and trimmed' (FIOST) clause, meaning that the charterer is undertaking these functions and not the shipowner. In time charters such as the NYPE form 'charterers are to load, stow, trim the cargo at their expense'. Again this is a charterer's operation and, as such, is likely ultimately to involve its liability if it does it wrongly or badly. Charterers can, and time charterers frequently do, take out their own P&I cover primarily to provide themselves with liability insurance cover for these risks.

Sometimes it is a matter that the operation of loading and discharging is a joint operation as between the shipowner and the charterer. I n such circumstances there is a propensity for disputes to arise as to who did what and consequently arguments as to who should pay what. This is indeed the case under the NYPE form. The cargo responsibility clause continues 'load, scow, trim the cargo at their expense ..... under the supervision of the Captain'. Sometimes an amendment is made to this clause to include the words 'and responsibility' after the word 'supervision'. The interpretation of this wording led to so many disputes that the International Group clubs drafted a mechanical formula which would be used to apportion cargo claims arising under the NYPE - the so-called NYPE Inter-Club Agreement.

A frequent problem which arises is with cargo that has been damaged as a result of had handling by stevedores. Bags may be torn, pipes may be bent and other similar damages. Usually the cargo is considered to have come into the custody of the carrier once it has crossed the ship's rail or possibly once it has been attached to the ship's gear. If the handling damage to the cargo has occurred prior to this point then it would usually be appropriate to record the damage on the mate's receipts and bills of lading.

However, the damage frequently arises after it has come into the custody of the carrier. In such cases it may be inappropriate to record it on the mate's receipts and bills of lading since the obligations and responsibilities under article III of the Hague-Visby Rules have now started and these are usually non-delegable.

The shipowner may have an indemnity claim against the stevedores or the charterer but in the first instance is likely to have a liability towards the cargo owner if the cargo was damaged after it came into the custody of the shipowner. The reason why there is a certain amount of hesitation in this situation is that if the stevedores are employed by the cargo shipper, as maybe the case under say FIOS terms, then the

situation may be quite different in that the shipowner's period of responsibility may not start until the cargo is stowed on board.

One of the most frequent problems which arises with the carriage of cargo, giving rise to potential claims and the risk of a shipowner losing its P&I cover, is where cargo is loaded on board not in 'apparent good order and condition' but so-called 'clean' bills of lading are issued.

The bill of lading performs a number of different functions. A very important and fundamental function is as a receipt for the cargo. To comply with the requirements and obligations of the Hague-Visby Rules, or similar, it should describe the apparent order and condition of the cargo at the time of loading and also state the number of pieces or weight of the cargo.

As a receipt it will be given to the shipper of the cargo, which will then use the bill of lading in another way: as a document of title or negotiable instrument. Under the contract of sale which will have been negotiated between the buyer and the seller of the cargo, there will have been established, in most cases, an irrevocable letter of credit (LOC) within an international banking system. Under the LOC the seller will be paid for the goods provided it produces certain documentation in a particular form. This will inevitably require a bill of lading, which will confirm that

- the goods have been shipped on board a particular ship at a particular port and bound for a particular port
- the goods were loaded by a particular date
- the goods were in apparent good order and condition, or in such a condition as allowed under the terms of the LOC
- a particular quality had been loaded.

The buyer of the cargo is thus relying on the statements in the bill of lading when handing over its money to the seller and, if these statements subsequently turn out to be inaccurate or untrue, then the shipowner will have to compensate the cargo receiver. If such a bill of lading was issued by the master or the shipowner (or with its knowledge) then the P&I cover may be prejudiced.

If the shipowner has accepted a so-called 'Letter of Indemnity' (LOI) to issue 'clean' bills of lading, then it could try and recover under that LOI. But if the shipper or charterer refuses to honor their promise, there isn’t much the shipowner can do. The courts will not recognize LOIs as having any validity since they came into existence to perpetrate a fraud and the shipowner is implicated in that fraud. It may therefore have to bear the loss out of its own resources and also lose its P&I cover.

In addition to describing the apparent order and condition of the cargo, the bill of lading will also state the date when the cargo was loaded. This date may be crucial

under the terms of the sale contract. If the date has not been correctly stated and consequences arise, then the shipowner is likely to be liable to compensate the cargo owner and may also lose its P&I cover.

Another problem which often arises and which can result in a shipowner losing P&I cover for cargo liabilities is in respect of a deviation under the contract of carriage. Usually the deviation will be a geographical deviation - a diversion from the normal route or contracted voyage with cargo on board for some specific purpose. There may however be other types of deviation such as a deviation by delay or time deviation, where the original contracted voyage is extended beyond what was reasonably anticipated.

If the deviation was 'reasonable' or 'justifiable' then there is unlikely to be any problem - the Hague-Visby Rules, for example, allow a 'reasonable' deviation without breaching the contract of carriage and, consequently, there is unlikely to be a problem as far as P&I club cover is concerned.

However, if the deviation is 'unreasonable' then this is likely to amount to a serious breach of the contract of carriage, resulting in the loss of any of the defences and rights to limit liability for example. It is also likely to lead to a loss of P&I cover for cargo claims arising as a consequence of or during the deviation.

What is meant by the term 'reasonable' is quite specific and is unlikely to extend to commercial reasonableness, no matter how sensible it may be. Under the Hague-Visby Rules, for example, it would certainly be reasonable to deviate to save life or property. To seek assistance for sick or injured seamen or other persons would be reasonable to go to the help of another ship in distress or requiring assistance would be reasonable; if a large number of stowaways were found on board, perhaps out numbering the crew, and who were perhaps becoming threatening or violent, then a deviation to a port where help could be obtained would probably be considered reasonable.

However, a deviation to effect a crew change, to land a repair squad or a stowaway at a convenient port are unlikely to be considered reasonable if the only reasonableness was the convenience of the shipowner - even if this was the most sensible solution commercially.

If the vessel is going to be involved in a deviation which is likely to be considered 'unreasonable' then the shipowner is strongly recommended to take out a separate 'shipowners liability' (SOL) insurance cover. This is available on the commercial market but it would usually be arranged by the P&I club on behalf of the member and at the member's expense.

It should be understood however that the only P&I cover which is lost is cover for cargo liabilities arising as a result of the deviation. For example, consider a vessel bound from Brazil το Japan which diverts into Cape Town to change some crew.

During the deviation she has a collision resulting in number 2 cargo hold being breached along with a bunker fuel tank. The H&M cover, and the P&I, for the RDC would remain in place. P&I cover would also be available for the consequences of any pollution and personal injuries which might arise. However, if the cargo owner brought a claim for damage to the cargo, then the shipowner is likely to have breached its contract of carriage and as such will not be able to rely upon, say, the error of navigation defence and any package limitation. As a consequence it would not be able to recover from the P&I club the compensation it may have had to pay to the cargo owner.

The P&I club would normally cover a shipowner member for the net losses and expenses incurred during a diversion to land a sick or injured person or to land a stowaway, or to go to a vessel in distress. Lost freight or charter hire is not covered but the cost of fuel, extra insurance, crew wages, port expenses and similar are covered. It is therefore very important to keep accurate records of any diversion.

A special type of deviation from the contracted voyage is frequently requested by charterers or possibly cargo owners and that is to deliver the cargo at a destination other than that stated in the bill of lading. Normally neither the shipowner nor the master are obliged to agree to such a request but the shipowner may do so for commercial reasons. If they do then it should be in the knowledge that they would be in potential breach of P&I club cover.

Similarly, requests may be made by the charterer or cargo owner to deliver the cargo without production of an original bill of lading or other document of title. Again, if the shipowner did agree to do this then it would be putting its P&I club cover at risk for any consequences which might arise. The consequences could be that the cargo is discharged at the newly nominated port in accordance with the charterer's request but the cargo receiver then demands that the cargo be delivered at the original destination. The additional transportation cost of on-forwarding the cargo and the risk of loss or damage during this transhipment would be for the shipowner's account without recovery from the P&I club.

If the cargo is delivered to an individual without an original bill of lading being produced, then there is always the risk that someone else may subsequently come along with an original bill and demand delivery. The shipowner may very well find itself liable to compensate this individual for the loss of his entire cargo - again there would be no P&I cover for such a liability.

To protect itself if it does decide to agree to these requests, a shipowner should obtain from the charterer a guarantee in the wording recommended by the P&I club. This should be countersigned by a first class bank. Such guarantees replace the shipowner's lost P&I cover.

P&I club cover for cargo liabilities assumes that all the shipowner members of the club will be contracting on basically the same terms, usually the Hague or Hague

Visby Rules. In this way no one shipowner is imposing a greater burden upon the mutuality of the club than any other. However, if the contracted voyage is from or to countries which have ratified the Hamburg Rules, and the Hamburg Rules compulsorily apply, then the club cover will remain in place. If the member voluntarily agrees to the incorporation of Hamburg Rules then its P&I cover will only extend to a level which the directors of the club believe would have existed if Hague or Hague Visby Rules had applied.

If a problem does arise with the cargo, the prudent master would immediately arrange for the local P&I correspondent to attend. It may be necessary to appoint a surveyor and perhaps a lawyer. The costs of these attending parties would normally be covered by the P&I club.

In a general average or salvage incident there are usually two interested and contributing parties - the ship and the cargo - although such things as freight or time charterer's bunkers may also be contributing parties. Thus the costs of the GA losses and expenditure and sacrifice or the salvage expenses would be shared between the shipowner and the cargo owner(s). The shipowner would be insured for these contributions with its H&M underwriter and the cargo owner would be insured under its cargo insurance policy. In normal circumstances therefore the P&I club would not be involved.

However, if the cargo owner (or subrogated cargo underwriter) can demonstrate that the occurrence which caused, or led to, the GA or salvage incident was as a result of some breach of the contract of carriage - usually some unseaworthiness - then it may withhold its contribution. If its allegation proved to be correct and the shipowner cannot demonstrate that it exercised due diligence at the start of the voyage to make the vessel seaworthy, then the P&I club will cover the cargo owner's contribution to GA and salvage.

It is therefore crucial that the P&I club be advised immediately in the event of a GA or salvage incident. This enables the club to consider whether it needs to carry out its own investigation at the time of the event and thus put itself into a position whereby it can respond to allegations of unseaworthiness which may come forward from the cargo owner / underwriter some considerable time after the event.

*(Pic4.4 Cargo interests may challenge their obligations to contribute to GA if the vessel was unseaworthy)*

If the cargo interests simply refuse to pay their contribution then that would be a bad debt - for which the shipowner would not have any insurance cover. However, if the shipowner did have FD&D cover then the FD&D lawyers may assist the shipowner with the debt recovery exercise.

## Liabilities in respect of ships

It could be said that P&I insurance covers those risks which have not been covered under the H&M policy. To some extent this is true and particularly so when considering risks specifically relating to the ship itself in contrast risks related to people and cargo.

Most P&I clubs assume that their members will be contracting for their H&M cover on L1oyd's Marine Policy with Institute Time Clauses (Hulls). However, whereas these particular H&M policy terms are very popular, shipowners will make their own choice as to the terms and policy under which their hull and machinery risks are covered.

There are other popular H&M policy terms in place in other insurance markets around the world such as, but not limited to, Scandinavia, Germany and the us. These may differ significantly from the standard forms used on the L1oyd's market.

It is extremely important for the shipowner to know what is covered under its H&M policy for two related reasons. Firstly, if certain risks are covered under the H&M policy then those same risks do not need to be covered under the P&I insurance. This reduced risk should be brought to the attention of the P&I underwriter, who should take it into account when calculating the call level for that particular member. Secondly, within the rules of the P&I club, there will probably be a 'double insurance rule', which says that if a particular risk is covered under some other insurance policy, then it is not covered by P&I. Of course the master also needs to know the terms of the H&M policy since, if there is an incident involving the ship, he needs to know whether to call in the P&I correspondent or the H&M representative.

The risks covered in this section include:

- collisions
- non contact damage to ships
- damage to property
- Pollution.
- wreck removal
- towage.

The extent to which a P&I club will provide cover for liabilities arising out of a collision will depend very much upon the terms of the hull and machinery policy.

Under the ITC (Hulls) - 1.10.83 H&M policy terms, three fourths of the collision liability (3/4 RDC) will be covered. The other 1/4 RDC would be covered by P&I. Damage to the shipowner's own ship falls under H&M insurance.

There are a number of H&M policies which do not follow the traditional split of 3/4 and 1/4 on the collision liability clause, such as certain Scandinavian, German and American policies where the whole of the collision liability is covered. It is also possible for the P&I club to agree to cover the whole 4/4 of the collision liability, in which case the H&M underwriter will need to be advised in order to adjust its terms and relevant premium.


*(Pic4.5: Collisions may include cargo damage, pollution and injuries)*

In a collision there may be many others losses, injuries or claims in addition to the physical damage to the ships(Pic4.5). There are certain liabilities and losses arising out of a collision which are not covered under ITC (Hulls) - 1.10.83, such as personal injuries and death both on the insured ship and on the other ship, damage to cargo on the insured ship and pollution as well as wreck removal. If these types of liabilities arise in consequence of a collision, and if they are not covered under the H&M policy, then they would be covered under P&I.

Exactly how the RDC liability cover is split between H&M and P&I also becomes very important when considering the provision of security. Following a collision the owners of both ships are likely to arrest or threaten to arrest, the other vessel in order to obtain security - usually by way of a guarantee to cover the potential claim pending the legal apportionment of liability. The danger is that the ship may be the only asset of value belonging to the particular shipowning company and, if security is not obtained, then the ship may sink or otherwise be lost or disposed of before a judgment is given.

It may subsequently be extremely difficult, if not impossible, to enforce an award / judgment and have the claim paid. If security has been posted then the guarantor will

have to settle any such liability When security is demanded, following a collision, it is quite normal for the shipowner to ask its P&I club to provide its own letter of guarantee as security. The same facility may be offered by the P&I club for the owner of the other vessel.

However, if the H&M policy is on normal ITC (Hulls) - 1.1 0.83 terms then the P&I dub will need to obtain counter security from the H&M underwriter for its 3/4 RDC exposure. It may also be appropriate to obtain additional counter security from the shipowner for the H&M and P&I deductibles - which may be very significant.

Although the H&M underwriter will be involved in the whole of the damage to the shipowner's ship (although some recovery should be possible from the other ship in the collision) and 3/4 RDC, the P&I club will probably be the single biggest underwriter involved in any collision. The reason for this is that the H&M cover is probably shared out amongst many individual underwriters and insurance companies - each taking its own 'line' or percentage of the total risk. It is therefore quite normal for the P&I club to take over the handling of the collision case - at least as far as defending the claim from the other vessel is concerned. This also means that the P&I club claims handlers acquire a considerable amount of experience in handling such claims.

Other issues will also need to be taken into account when considering the question of providing security, such as the reasonableness of the amount of security being demanded. In this respect joint surveys may be carried out on each other's vessels and, hopefully, the surveyors can agree an approximate quantum of damage although obviously this will be done without prejudice to legal liability.

That legal liability will be decided in due course by the courts or will otherwise be agreed through amicable negotiations. Jurisdiction and choice of laws can also be decided at this time. This can have a significant bearing on the end result of a collision dispute - particularly in the event of a major incident where questions arise relating to the right to limit financial liability are concerned. In jurisdictions which still apply the 1957 limitation convention, then a much smaller financial limit will apply but the opportunity to 'break' limitation, which is to disallow the party trying to limit, is relatively easy.

On the other hand, in countries which have ratified the 1976 limitation convention, the limitation figures will be much higher but the chances of breaking limitation will be very small indeed. There may be other reasons for choosing one particular jurisdiction over another; for example, the Admiralty Court of England has considerable experience of dealing with such legal cases whereas the courts in some other countries may be perfectly suited for dealing with local domestic law issues but have no experience of the much specialised field of Admiralty law. Very rarely is one ship ever held 100% to blame in a collision. In almost every case there will be some degree of blame to attach to each vessel; it may be 50/50 or 70/30 or 95/5, for

example. However, the final apportionment will be influenced considerably by the quality of the evidence produced from the vessel and this point cannot be over-emphasised.

A collision occurs when two ships come into physical contact with one another. Often, however, considerable damage can be caused by one vessel against another even though there has been no physical contact - the so-called non-contact damage incidents. The most usual scenario would be where one vessel was secured alongside a berth, say in a river or canal, and another vessel passed by at excessive speed. The wash from the passing vessel could cause the moored vessel to surge on her mooring, causing damage to herself and to other property or even people.

It maybe that the incident is very serious indeed. Consider a situation where the moored vessel was loading say oil and the surging caused the loading lines to break with serious pollution of the river. Such potential liabilities to the other ship in such an incident would not be covered under an H&M policy such as the ITC (Hulls) - 1.10.83 or similar, although it is possible that some other H&M policies could cover some of these third party liabilities. Again it will be a matter of checking the particular terms of the H&M policy in use. It is however much more likely that these third party liabilities would be covered by the P&I club.

As far as the moored vessel is concerned then attempts should he made to recover from the passing ship whose wash caused the damage. Physical damage to the ship would of course he covered under the owner's H&M policy. Any personal injuries or damage to third party property would be covered by the owner's P&I c1ub but it should try and protect its claims record with the c1ub by claiming from the other vessel.

Those on board the ship which has suffered damage need to act quickly in such situations. Initially. of course, they need to identify the offending ship and immediately advise the shipowner / shipmanager. Urgent steps will need to be taken to serve .a formal notice on the offending ship holding it, its master’s and owners’ responsible for all damages and to obtain adequate security, bearing in mind that any other third party claims for damages as a result of the surging incident will probably be brought against the vessel which was alongside in the first instance.

Another liability risk which is not usually covered under the H&M policy, although it may be under certain policies. is damage to third party property. Such damage can often arise when the ship comes into physical contact with the third party property. For example, the ship may run into a wharf, jetty or pier or hit the arm of a container gantry crane or a navigational marker buoy - plus an almost unlimited range of other so-called 'fixed and floating objects' (FFO) incidents.

This physical contact by the ship and the third party property is not a collision in a technical or legal sense. The English language does not have a similar word for such an event. However, there are words in other languages and the Americans have

coined the word 'allission' to describe the physical contact between the ship and the third party property which is not another ship. This liability towards damage done to third party property and the consequential losses is normally covered by the P&I c1ub.

A typical list of the potential risks under the FFO cover would be as follows:

*"Loss of or damage to any harbor, dock, pier, quay, jetty, land or anything whatsoever fixed or movable (not being another ship or cargo or other property therein or cargo or other property carried in the Entered Ship) by reason of contact between Entered Ship and such harbour…etc"*

This list is deliberately open-ended and no-one can say with any degree of certainty exactly how long that list might be. It is really a matter of assessing each incident which might arise and considering whether the damage is to some similar third party property and, if it is, then it should be included. If necessary the so-called 'omnibus' rule of the P&I club could be invoked whereby if an unusual claim did arise then it could be referred to the club directors to exercise their discretion. Other examples of FFO type incidents might include

- Damage to an underwater electricity cable running from the mainland to an off-lying island, perhaps as a consequence of the cable being pulled up by a ship's anchor. The P&I cover would not only cover the cost of repairs and restitution of the electricity cable but also the legal claims which might come forward from factories, hotels, island residents and others who could show that they had suffered a financial loss as a direct consequence of having their electricity supply cut off.
- An explosion occurs on board a ship and hatch covers and other parts of the ship land on property ashore. Many windows are also blown out by the shock-wave. Such damages would be covered.

Consequential loss claims which can accompany FFO type incidents can be considerable. Consider, for example, the consequential losses of a ship hitting and knocking over a container gantry crane in a major container terminal. Such an incident could bring the terminal to a standstill for weeks while repairs were carried out. In addition to consequential loss claims from the port or terminal operators, there could also be claims from other shipping lines and container operators whose operations become seriously hampered because of the incident.

However, as far as the allowable extent of consequential loss claims is concerned then this really does vary from one jurisdiction to another. The important point to note, though is that if the shipowner is legally liable, then the P&I club will probably provide the shipowner with the insurance cover needed.

Pollution is included here because many of the potential liabilities arising from a pollution incident are basically in respect of damage to third parry property - except that in this case it is likely to involve cleaning the property rather than rebuilding a physical structure.

It is natural to think of thick black oil when the word pollution is mentioned, but there can be many more different types of pollution - from chemicals and garbage to smoke and hold sweepings. The P&I club provides insurance cover for most types of pollution, including claims for damages, c1can up and fines. However, the financial level of cover available within the P&I club for oil pollution is limited at 500MillionUSD.

Most leading maritime nations around the world have ratified the Civil Liability Convention (CLC) which is a strict liability regime whereby 'the polluter pays' (except in very exceptional circumstances) regardless of how or why the pollution happened. Nevertheless the shipowner is entitled to limit its financial liability, based on the tonnage of the vessel, to reasonable levels.

Even in the largest ULCC, the CLC limitation figure would not come anywhere near the 500MillionUSD cover provided by the P&I club. If the pollution claim did exceed the CLC limitation figure then another source of funding would be made available - the so-called Fund Convention. This is literally a fund of money which is built up from a levy made against the main oil traders and importers.

*(4.6: Oil Polluted Beach at  Iran)*

There are a few countries around the world that are not signatories to the CLC and Fund Conventions - most notably the US, which enacted the Oil Pollution Act of 1990 (OPA'90) following the Exxon Valdez incident. There are limits available under OPA'90, for example, but it would be quite easy to break limitation. Consequently, the amount of liability insurance cover required by tankers trading to the US could well exceed the limit of P&I club cover. Such tanker owners would need to make additional insurance arrangements as well as obtaining a document demonstrating to the US authorities that they do in fact have the necessary insurance cover.

Another related liability which is covered by the P&I clubs, and which is relatively new, is cover for special compensation payments to salvors. For many years the Lloyd's Open Form of Salvage Agreement was on terms of 'no cure - no pay'. In other

words, if the salvor was not successful in saving the ship and cargo then it did not get paid. Thus if it became apparent to a salvor during a salvage operation that it was not going to succeed, for example it was clear that the ship was going to sink, then there was no incentive for it to continue its work and it may as well just leave the ship and its cargo to its fate. However, that would also mean in many cases that the sinking vessel would pose a serious pollution risk - as well as possibly posing a potential wreck removal risk. If such a situation occurred then it would be the P&I club that would cover the pollution claims, clean-up costs and fines. It therefore made sense for the P&I clubs to come to an agreement with the professional salvors such that, if the salvors found themselves in a position whereby they knew they could not save the ship but by continuing their efforts they could prevent a pollution incident - for example by towing the vessel away from the coast where she could sink in deep water - then the salvors would be compensated for their work. This provision was incorporated as article 14 of the International Salvage Convention of 1989 and forms part of the standard terms of the Lloyd's Open Form (LOF) Salvage Agreements.

There have been some problems experienced with the actual working of the article 14 compensation, which required complex accounting to work out exactly what compensation the salvor was entitled to. There were also disputes as to the reasonableness of the particular action taken. Accordingly the International Group clubs have worked out an agreement with the International Salvage Union and others, whereby a tariff rate for all types of clean-up equipment have been agreed in advance. The shipowner and cargo owner(s) will be entitled to have their own monitor on board during the salvage operation to agree, or otherwise, what is reasonable and the salvor will be entitled to receive a minimum amount by way of security. This is the so-called SCOPIC clause and, if it is successful, is likely to replace the article 14 special compensation provisions.

If a ship sinks or otherwise becomes a wreck, the local harbour master or other local official may declare that the wreck is in a dangerous position and issue a order to the effect that the wreck must be removed. The most usual reasons for such an order are that the wreck either poses a danger to navigation or is a potential pollution risk. In either case the order will be served on the last owner of the vessel and the legal obligation to remove the wreck would usually be upon that owner. This is one of the main reasons why H&M underwriters will never accept responsibility or ownership of a ship when it becomes an actual or constructive total loss. They will pay the insured for the loss under the policy but will then divest themselves of any further interest or involvement.

Consequently, if the shipowner is legally obliged to mark or remove the wreck, this liability will be covered by the P&I club. Wreck removals can be some of the biggest financial claims with which a P&I club has to deal. Wreck removal cover provided by a P&I club can also extend to items of cargo - for example where drums of highly toxic chemicals are lost overboard and an order issued for the drums to be recovered from the sea bed.

During the normal trading of a ship it is very likely that tugs will be engaged either entering and leaving port, during river and canal transits, or possibly to assist going alongside or leaving a berth. This is normal harbour towage. The terms of most standard harbour towage contracts are very onerous against the ship being towed - basically making the tow responsible for any damaged caused or other liability incurred, even if it arose as a result of some fault on the part of the tug.

Similar liabilities may also arise in other situations where the vessel is being towed. Perhaps the vessel has broken down and a tug has been contracted to take the vessel to her destination. Maybe the vessel is being towed as part of a salvage incident. There is potential for damage to be caused to third party property, to people or to the tug itself. P&I clubs do not provide cover for the cost of towage nut if the member incurs a liability during a towage operation - provided the P&I club managers have approved the terms of the towage contract - then the club will cover that liability.

During its employment a vessel or the people operating it may find themselves being fined for all manner of alleged or actual offences. These could include fines for failure to maintain safe working conditions, customs fines for short or over-landed cargo or for smuggling, for having illegal immigrants on board (e.g. an undeclared stowaway), as a punishment following a pollution incident and for many other violations and offences. All of these fines will be covered by P&I although the directors of the club may need to be satisfied that the members were not privy to the incidents for which the fines were being levied. It is possible under this particular head of risk that the P&I club, rather than the H&M underwriters, may have to compensate the shipowner for the loss of its ship. This could arise if, for example, customs or police found a large consignment of drugs which were being smuggled on board the ship. As a consequence, and by way of a punishment, the local authorities or court confiscated the ship by way of the fine or penalty.

As stated, P&I cover is open-ended. Because of the unique way in which the clubs are structured they can, and do, respond to new risks and liabilities which arise or changes in the law which may occur. The aim is to provide the protection the shipowner members of the club require during the commercial operation of their ships. If a risk or liability arises and, provided it is not specifically excluded and it is of a P&I nature, then the claim can be referred to the board of directors of the club under the omnibus rule for approval.

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