CURRENT P&I CHALLENGES – *22 FEBRUARY 2012*

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ABSTRACT

The International Group of P&I Clubs ("the IG") comprises 13 not-for-profit mutual insurance associations which collectively insure the third party liabilities of over 90% of world ocean-going tonnage.

Via the knowledge sharing role of the IG the Clubs have been active in addressing issues for their shipowner Members in China and the United States, and with regard to the question of limitation of liability.

In China work has focussed on the recent introduction of a requirement for shipowners to contract with oil spill response organisations.

In the United States the Clubs have been closely involved in the aftermath of the Deepwater Horizon event, with particular regard to liability, compensation and contractual issues. There has also been increased cooperation with the Department of the Interior.

Some States have sought to have the limits of liability under the main convention raised. The Clubs have provided data to IMO in an effort to demonstrate that such action is not warranted. As with many changes to oil spill response and liability and compensation regimes in the past the occurrence of major casualties play a major part in driving such changes.

INTERNATIONAL GROUP

The International Group of P&I Clubs comprises 13 not-for-profit mutual insurance associations which individually insure third-party liabilities relating to the use and operation of ships. Group Clubs between them insure over 90% of the world's ocean-going tonnage and over 95% of ocean going tankers. The Group Clubs provide cover to virtually every type of vessel and owner/operator worldwide. Governments, maritime organisations and authorities around the world recognise the strength of, and the uniqueness of the cover offered, by, the Club system and the Group. As such, the International Group is uniquely positioned to assess and discuss the needs of and represent the views of shipowners on all matters relating to marine liability insurance and associated safety issues.

The individual Group Clubs provide the broadest and most extensive cover of any P&I insurer, up to (each and every claim) US$1 billion for oil pollution and approximately US$6.9 billion for other types of claim e.g. cargo, collision, personal injury etc. To provide for these high levels of cover, Clubs have a pooling or sharing arrangement whereby claims in excess of individual Club's retained risk, currently US$ 8 million, are pooled and shared between all of the Clubs up to the limits stated above. The pooling arrangement is then underpinned by a reinsurance programme which is the largest marine insurance placement in the world and involves many of the world's major reinsurers. By bringing together in this way the risks of the great majority of the world's tonnage, the Group is able to obtain the maximum reinsurance capacity on the best terms available worldwide.

THE SHARING OF KNOWLEDGE

One of the benefits of Group system is the ability to share knowledge and experience between the Clubs for the benefit of the wider shipping industry. This is achieved through a system of Sub-Committees and Working Groups that encompass representatives from all of the 13 Group Clubs and provide a forum for the exchange of information and views across a wide spectrum of topics as well as offering a single point of contact for industry to engage with the Clubs.

This includes a Pollution Sub-Committee and the closely related Vessel Response Plan Working Group. The VRP Working Group is especially active in vetting contracts from a broad variety of spill response service providers in order to ensure that the contract terms fall within P&I cover.

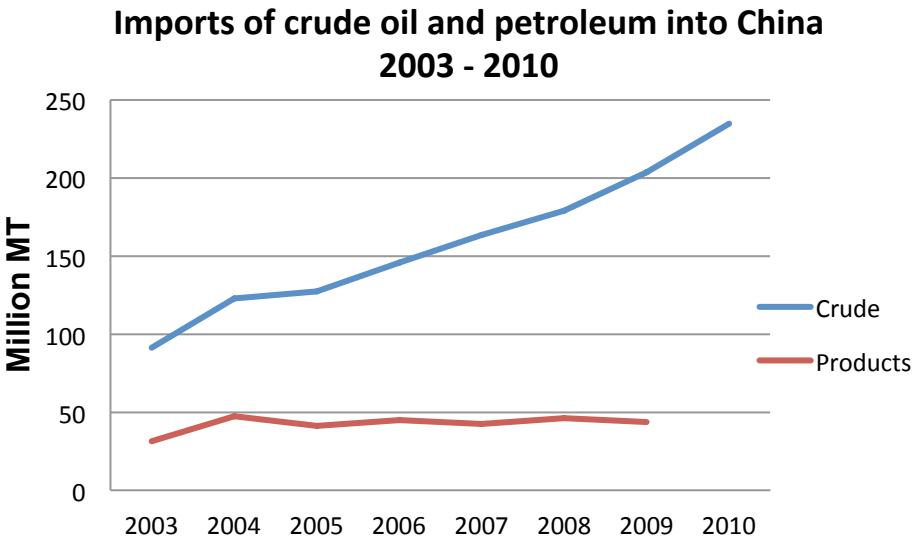
CURRENT CHALLENGES

The Clubs have been dealing with a number of challenges on various international fronts concerning pollution response and liability and compensation.

The principal challenges currently stem from China, the United States and on the question of limitation of liability at the behest of States. Many of these issues have arisen as a response to major casualties but it was ever thus – from “TORREY CANYON” to “EXXON VALDEZ”, milestones in pollution response planning and liability regime change have largely come about as a result of public and political outcry over oil spills and their effects.

CHINA

But we start with an exception to that rule. China has not suffered a major ship-borne oil spill in recent years, certainly not on the scale of the "HEBEI SPIRIT" spill in South Korea in 2007. However, in order to fuel her continuing economic growth China continues to be a significant importer of both crude and petroleum products, as the following graph shows:



Source: BP Statistical Review of World Energy/IEA Energy Stats of non-OECD Countries

With this in mind and one eye no doubt firmly fixed on the systems other countries such as the United States have adopted to counter the pollution threat, China has enacted various domestic laws concerning, amongst other things, the planning for and performance of pollution clean-up.

Principal amongst these has been a mirroring of the US requirement for a shipowner to have retained a clean-up contractor (termed a "SPRO" – Shipowners Pollution Response Organisation) before a vessel is allowed to enter a Chinese port. After a number of delays this requirement took effect on 1st January 2012 and applies to all vessels greater than 10,000gt and all those carrying oil or other

hazardous liquid cargo in bulk.[1] The regulations do not apply to Hong Kong or Macau.

With no real history of a widespread, planned response capability within the private sector the regulations have proved to be a catalyst for the creation of a large number of response organisations – more than 120 and still growing. The SPROs trade as standalone entities but have also coalesced into geographic consortia, so that the shipowner is faced with a complex web of organisations and consortia he can choose from depending on the vessel's intended ports of call.

The Clubs have spent the last few months engaging with this new industry and with their regulator China MSA. The work has been on three fronts. Firstly the Clubs have helped to promote a common contractual framework for response contractors, based around the requirements of the MSA but also ensuring that the contracts fall within long standing IG guidelines and thus within an owner's standard P&I cover.

Secondly, those response contracts call for the contractor to maintain limited insurance cover for his potential liabilities to the shipowner under the contract. The Clubs have been active in helping local insurers to develop products to meet these needs with advice on policy wordings.

Finally ITOPF[2] have kindly assisted in looking at each SPRO's response tariff on behalf of the Group to ensure that the rates charged are reasonable and to advise the SPRO where necessary on the capability and equipment gaps in their inventories.

[1] Guidance on all the requirements and lists of approved SPROs, consortia and agents can be found at: http://www.westpandi.com/Other/China-Pollution-Regulations/

[2] International Tankers Owners Pollution Federation – www.itopf.com

Whilst it is too soon to say that all the problems have been surmounted considerable progress has been made. It does though remain something of a nascent industry and the true test of capability and preparedness will of course only come with the next significant spill in Chinese waters.

As regards liability and compensation it largely remains status quo. China is a State Party to the Bunkers Convention[3] and to the 1992 Civil Liability Convention[4] ("CLC") but not to the 1992 Fund Convention[5]. Other than imposing a limited re-ranking of the priority of claims under CLC, the only other change as a result of these regulations has been the creation of China's own domestic fund intended to provide a further tier of compensation to the victims of oil pollution on top of the main conventions. Like the 1992 Fund and America's Oil Spill Liability Trust Fund, China's domestic fund will be financed via a levy of oil imports but in comparison to its Western counterparts the fund – and therefore the amount of compensation available to victims of oil spills not fully compensated by CLC – will be small.

UNITED STATES

In much the same way that "EXXON VALDEZ" was the precursor to OPA '90[6], so the Deepwater Horizon ("DWH") event has the potential to be the catalyst for a fresh round of regulatory and legislative scrutiny in the US – certainly so far as the offshore industry is concerned. For the P&I Clubs the aftermath of DWH has raised concerns in two areas:

[3] International Convention on Civil Liability for Bunker Oil Pollution Damage, 2001
[4] International Convention on Civil Liability for Oil Pollution Damage, 1992
[5] International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1992
[6] Oil Pollution Act of 1990 (33 U.S.C. 2701-2761)

Legislative changes to the liability & compensation landscape

As the leak from the well continued the legislators on Capitol Hill sought to reflect the public mood and both sides of Congress held hearings into the adequacy of the existing oil pollution legislation. A variety of alternative – and more stringent – bills were put forward. Potential measures included a significant raising or even removal of the limits of liability, repeal of the 1851 Limitation of Liability Act and changes to other legislation such as the Death on the High Seas Act and the Jones Act which could directly impact on shipowners.

The IG undertook a great deal of lobbying on behalf of the shipowning community and an IG representative testified before the House Committee on Transportation and Infrastructure in June 2010. It was argued that OPA '90 has served the US people well with regard to ship-borne spills by providing adequate compensation in all cases and that creating a system based on unlimited liability would render the risk uninsurable by the Clubs and their attendant reinsurance markets. Such a system, or even one with very much higher limits of liability, is in any event unfounded where the largest potential ship-borne oil spill is a bounded risk – say the loss of a fully laden VLCC[7] – as compared to an unquantifiable maximum release from a runaway well like DWH.

Once the well was capped however and the vast majority of oil naturally dissipated, the story began to move away from the front pages and with it the immediate clamour for legislative change. To-date no bills in either House have moved beyond the initial stages but the IG maintains in close contact with regulators in Washington DC.

[7] Very large crude carrier, typically >200,000 DWT

Use of Dispersants

A more tangible impact of DWH on shipowners (and especially tanker owners) has been the contractual hangover on OSROs[8] caused by the spraying of chemical dispersants in that spill.

Some plaintiff personal injury lawyers have sought to target all and sundry in their actions for alleged sickness and injury of clean-up workers and others arising out of the use of dispersants. Although the OSROs were following the US Coast Guard's order to spray they find themselves as one of the defendants and face expending sizable legal costs to try and extract themselves from the litigation. OPA '90 does not confer responder immunity for personal injury claims and the OSROs are also lobbying to be able to claim such immunity to protect themselves from these types of claims.

In the interim, they have sought contractual sanctuary as a means of insulating themselves against a similar liability where dispersant use is ordered in future spills. Both major US OSROs have drafted a new term in their contract under which the shipowner assumes liability for all claims arising out of the use of dispersants. These addendums also currently require the shipowner to contract directly with the dispersant manufacturer for supply of the dispersant at the time of use but those contracts similarly contain one-sided indemnities such that the shipowner effectively becomes the product liability insurer for the dispersant manufacturer.

[8] Oil Spill Response Organisations

On behalf of shipowners the Clubs have been in negotiation with the OSROs in an effort to temper the effects of these new provisions and to seek a more balanced liability regime, not least because some of liabilities contemplated by the revised wordings would fall outside of normal P&I cover. Those discussions continue.

Towards greater NRDA cooperation

Away from the DWH, the IG has recently entered into a Memorandum of Understanding ("MOU") with the US Department of the Interior ("DOI"). One unique aspect of OPA`90 is the concept of a natural resource damage assessment or NRDA in the event of an oil spill, whereby various Trustees (depending on the resources impacted) are charged with determining the extent of any injury to the natural environment caused by the spill and calculating compensatory damages payable by the Responsible Party[9] to restore those resources.

Shipowners and their Clubs are keen to be involved in this process from the very beginning and to have the opportunity of working with the Trustees in their assessment – a so-called cooperative NRDA. To this end there is already a MOU in place with NOAA, the National Oceanic and Atmospheric Administration, and this additional MOU with the DOI is intended to compliment that to help ensure that the NRDA process can be a collaborative rather than combative effort for all concerned.

[9] The party designated by the US Coast Guard to be responsible for meeting the OPA`90 liabilities created by a spill, usually the shipowner in the case of a ship-borne spill

THE CASE FOR RAISING LLMC LIMITS

Unlike CLC, the Bunkers Convention has no integral limitation mechanism. Instead a shipowner's liability is limited according to the local law of the state in which the spill occurred. In many cases this is LLMC – the Convention on Limitation of Liability for Maritime Claims, either in its original 1976 form or the 1996 Protocol under which limits are significantly higher.

This international convention has been around for many years and is a mainstay of maritime legislation in a wide variety of states. It governs limitation not only under the Bunkers Convention but for many other maritime claims as well.

But once again a major casualty has thrown the spotlight on the convention system and may herald a very significant increase in an owner's liability.

The "PACIFIC ADVENTURER" lost containers overboard in a storm off the eastern seaboard of Australia in 2009. Some of those containers pierced one of the ship's bunker tanks and heavy fuel oil became stranded along a wide stretch of some of Australia's premier beaches. The clean-up response was substantial and the cost ultimately came to considerably more than the ship's limitation fund under LLMC.

When the shipowner sought to rely on limitation a public outcry ensued. The State Premier campaigned for the shipowner to meet its obligations in full and without recourse to limitation, though a compromise was eventually reached.

A grouping of States (including Australia) have since tabled a request to the IMO that consideration be given to increasing the limits under LLMC in order to increase the amount of compensation available to claimants under the Bunkers Convention and for other maritime claims. An existing amendment procedure under LLMC permits increases of up to 6% per annum compounded for every year since the Convention was established in 1976 if the States who are party to the Convention agree. The very considerable impact that this would have on shipowners and their Clubs is graphically demonstrated in the tables below, which highlight the 1996 Protocol limits (Oct -96) on a gross tonnage basis and the limits if they had been increased by the maximum 6% per annum compounded for every year until October 2010:

Loss of Life/Personal Injury	**Oct-96**		**Oct-10**	
	SDR	US$	SDR	US$
Vessel GT				
2, 000	2,000,000.00	$3,120,000.00	4,521,807.91	$6,854,378.26
5, 000	4,400,000.00	$6,864,000.00	9,947,967.91	$15,518,829.94
10, 000	8,400,000.00	$13,104,000.00	18,991,567.91	$29,626,845.94
50, 000	36,400,000.00	$56,784,000.00	82,296,767.91	$128,382,957.94
100, 000	60,400,000.00	$94,224,000.00	136,559,167.91	$213,032,301.94
175, 000	90,400,000.00	$141,024,000.00	204,385,717.60	$318,841,719.46
Any Other Claims	**Oct-96**		**Oct-10**	
	SDR	US$	SDR	US$
Vessel GT				
2, 000	1,000,000.00	$1,560,000.00	2,260,903.96	$3,527,010.17
5, 000	2,200,000.00	$3,432,000.00	4,973,983.96	$7,759,414.97
10, 000	4,200,000.00	$6,552,000.00	9,495,783.96	$14,813,422.97
50, 000	18,200,000.00	$28,392,000.00	41,148,383.96	$64,191,478.97
100, 000	30,200,000.00	$47,112,000.00	68,279,583.96	$106,516,150.97
175, 000	45,200,000.00	$70,512,000.00	102,192,858.80	$159,420,859.73

The Clubs have argued that the existing limits are perfectly adequate and that the issue should be looked at in the round rather than in isolation against the backdrop of a very small number of major incidents. The limits should form a framework of certainty and reasonable risk for the shipowner in order to continue to encourage international carriage rather than being overtly penal and thus dissuasive.

The IMO Legal Committee asked the Clubs for help in giving the debate some context by providing data on cases where claims exceeded the limitation available under LLMC. The data provided showed that:

- Between 2000 and August 2009, the total cost of pollution damage claims from a spill, or the threat of a spill, exceeded the limits of liability contained in the 1996 LLMC Protocol in only 10 incidents, whether or not the Protocol was in force in the State in whose waters the incident occurred, and

- Since the entry into force of the 1996 LLMC Protocol on 13 May 2004, the total cost of claims that were subject to limitation exceeded the limits, save for incidents involving pollution damage arising from bunker oil spills, in only 7 cases.

The debate is still to be had at the IMO. But recent events may play a part; following the grounding of the containership “RENA” in New Zealand’s Bay of Plenty in October 2011 and with an expensive pollution clean-up and salvage operation in the offing, there are already calls within the New Zealand press both for the owners

of the “RENA” to bear the full burden of the costs without resorting to limitation and for New Zealand to support the raising of the LLMC limits.