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Limits to cover could be costly

A decision by P&I clubs to limit cover on passengerships could leave the financial markets picking up the bill.

Jim Mulrenan London

A reduction in insurance cover for cruiseships and ferries may have unexpected consequences for the financing of expensive passengerships.

The risk that the protection-and-indemnity (P&I) clubs' decision to limit cover for passenger death or injury to $2bn could leave the financial markets picking up the bill was highlighted this week by Graham Barnes.

Barnes — a veteran broker whose BankServe Insurance Services is the best-known specialist in mortgagees interest insurance and other products for lenders and investors to the marine market — has written to his clients warning of the increased risk.

The leading cruise operators often finance vessels through securitised bonds rather than traditional ship mortgagees. US pension funds are major investors in these bonds, which are seen as safe houses for their funds because of the favourable ratings of the cruise groups.

But Barnes feels it is pretty unlikely that these funds realise that since the 20 February renewal of P&I cover they have effectively been underwriting part of the risk of a passenger-shipping catastrophe.

The main restriction on P&I cover was previously a $1bn limit for oil spills with $5.5bn available for most other claims including that of a *Titanic* or even larger-scale disaster.

The $2bn limit on passenger cover was brought in as the maximum liability for death or injury is due to rise dramatically under a new protocol to the Athens convention, which also had the effect of stirring up cargoship owners' concerns about the potentially huge claims that could result from a major cruiseship or ferry disaster.

The restriction on passenger cover to $2bn, which rises to a combined limit of $3bn with crew liabilities, means that P&I cover would not be sufficient to meet the full Athens protocol limits for a ship carrying less than 3,500 passengers in an incident where negligence is a factor, or for a ship of 5,329 passengers or greater capacity where there is no fault.

The biggest cruiseships afloat have already passed the 3,500-passenger-capacity mark with newbuildings on order set to have 5,500-passenger-capacity. This leaves aside the risk of an incident subject to US jurisdiction, where the Athens convention limits would not apply. Ferries are also getting bigger, with the largest in service already having 3,000-passenger capacity.

GRAHAM BARNES

Photo: Jim Mulrenan

Barnes proposed solution is to extend mortgagees additional perils insurance — originally introduced to protect banks and financial institutions from loss if oil-spill cover is insufficient — to passenger and crew liabilities.

The bonds are often securitised against a package of assets made up of a number of vessels so a catastrophe involving one puts the entire investment at risk.

Although he has yet to test the market, he thinks premium levels for the additional cruise and ferry risks would probably be comparable with that for oil spills and would be of a tariff nature rather than related to either the indebtedness or maritime risk of the shipowner.

The risk that concerns Barnes is that if there were liabilities unrecoverable from a shipowner or a P&I club, claimants would go after vessels with the scenario rather worse if the corporate veil of a special-purpose shipowning company is pierced and found to be jointly and severally responsible for all liabilities.

The risk of a maritime catastrophe is no doubt remote but the P&I clubs action shows that the organisations with the greatest expertise on such liabilities believe it is not so unlikely a risk that can be ignored.