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# MARITIME SAFETY

The Role of Cargo Owners/Shippers

and

Marine Insurers

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SWEDISH MARITIME  
ADMINISTRATION

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## ANNEX

List of abbreviations used in this report

## 1 Brief summary

The original report, written in Swedish, was prepared at the request of the Swedish Maritime Administration. The background and purpose is presented in the introduction on the following pages.

The main aim is to explore if and how cargo interests and marine insurers can contribute more than hitherto in enhancing maritime safety. The role of ship financiers is also touched upon. The tentative conclusions are as follows.

The concept *cargo owners* covers a wide variety of interests and most of them have no influence at all over the choice of vessels transporting their goods. The difficulties in identifying in legal terms what is an unseaworthy or a substandard vessels further complicate matters. While it is possible to consider applying sanctions to charterers, the private parties concerned must themselves assume the main responsibility for the quality of the ships they use. Wide publicity should be given to unsafe ships which are arrested through port control.

*Marine insurers* already play an important part in safeguarding high quality shipping but they could do more by applying their rules very strictly, by always checking thoroughly ships which are new entrants or transferred from other P&I clubs. A closer co-operation - in both directions - with classification societies would be mutually beneficial as would complete openness in respect of available data. Strict codes of practices should be developed. Uninsured ships must be tracked down and stopped.

*Ships financiers* should take more of a long term view of investments, bearing in mind the traditionally very long depressions in the shipping markets. A serious study in retrospect of the financial outcome of earlier investments in ships might provide useful guidelines for the future, possibly developed into a voluntary code with check-lists to be encouraged for use by all ship financiers. The rules for state controlled mortgage institutes might provide useful guidelines.

## 2. Introduction

Early in 1997 the Swedish government requested the Swedish Maritime Administration to present a study regarding "cargo owners' responsibility when choosing substandard vessels and the role of marine insurance for maritime safety". The task were to be completed before the end of 1997 and the Swedish Maritime Administration asked the former rector of World Maritime University, Erik Nordström, to write such a study. A report was submitted in December 1997 to the Swedish Maritime Administration, which handed it over to the government.

In presenting its request to the Swedish Maritime Administration the Swedish government referred i.a. to the European Commission document "Towards a new maritime strategy", as adopted 13<sup>th</sup> March 1996. The document contains comments and proposals on a vast number of maritime issues. It refers specifically also to the two subjects mentioned in the heading. In the executive summary of the strategy paper those subjects are identified as follows under the heading: "On safety the Commission proposes:

- to consider legislative action on financial sanctions for cargo owners who knowingly or negligently use sub-standard shipping; and
- to examine the question of mandatory third party liability coverage in shipping as a condition for entry into EC ports;"

The two subjects mentioned have also been dealt with briefly by two Swedish commissions investigating marine safety and the competitive position of the Swedish flag merchant fleet respectively.

For obvious reasons the report presented to the Swedish Maritime Administration referred extensively to Swedish rules and regulations and to conditions prevailing in Sweden. The report, containing 55 pages and 4 annexes, was written in Swedish.

The Swedish Maritime Administration did feel, however, that the more general sections of the report might be of some interest also to non-Swedish parties and asked Erik Nordström to prepare a

summary in English. In doing so most of those parts which refer to purely Swedish rules and conditions have been suppressed.

This abbreviated version will accordingly concentrate on the two subjects as such, aiming at presenting the factual and legal framework in which cargo owners/shippers and marine insurers operate. The extent to which these subjects are being dealt with by global or regional bodies like EU, IMO and OECD is also covered. In order to retain the logical sequence of the original report (and to avoid writing what would in essence be a new report) certain references to the Swedish scene have been retained.

In accordance with the mandate the report should also contain recommendations about positions and actions which could form the basis for further Swedish action in respect of the two main subjects. Those recommendations, which are linked to present and future maritime safety policy of Sweden, have been excluded in this abbreviated version of the report.

Although not directly mentioned in the mandate of the Swedish Maritime Administration the subject of a possibly more active contribution to marine safety by ship financiers has been covered in the report and is also briefly referred to here.

This abbreviated version of the report has, as requested, been submitted to the Swedish Maritime Administration, but the responsibility for its contents rests with Erik Nordström.

### **3. The activities of IMO, EU and OECD in relation to the two main issues**

#### **3.1 General**

A large number of very serious marine disasters has focused the attention sharply on maritime safety. Organizations, individual countries and private interests have all increased their efforts to enhance maritime safety as well as to explore new avenues to that effect. Both the public and the maritime press demanded effective and immediate action. All this led to new initiatives and to requests for speedy implementation of measures under discussion.

### 3.2 IMO

The responsibilities of IMO in the field of maritime safety are wide and varied. But the main thrust of this report is to analyze the possibilities of increasing the safety consciousness and activities of cargo owners and marine insurers. For that reason the situation in IMO (as well as in EU and OECD) is relevant to this study only in so far as these two main themes are under consideration (none of those bodies deals directly the potential maritime safety role of ship financing). Cargo owners' responsibilities and their use of standard ships have been referred to more than once in the debates at IMO, but the subject as such is not presently being actively considered as a part of the IMO programme of work. But marine insurance is. The issue of "compulsory insurance" against third party liability risks has been discussed for some time in the IMO Legal Committee and is still on the agenda for its next meeting (April 1998). But this broad subject has given rise to considerable differences of opinion within the IMO family and the present approach (and the tasks of a special correspondence group) has been limited mainly to the third party liability coverage of passengers and crews. Even if this might amount to a simplification you could say that the focus has been transferred and limited from the idea of compulsory insurance as a means of enhancing maritime safety to the "consumer oriented" question of how to guarantee full protection of passengers (and crew members). The Legal Committee will also continue to consider further the creation of a uniform standard of certificates of third party liability to be carried on board ships. The P&I clubs are playing an active part in these discussions and opinions vary as to the usefulness of compulsory requirements in that regard and - even more so - in respect of the extent of information to be provided in such a certificate. It is not unfair to assume that it will take quite some time before IMO will be ready for decisions as regards the general issue of an enhanced role for compulsory third party liability insurance in maritime safety. Many do believe that marine insurance already does what it should in this field and that an IMO intervention would only create increased bureaucracy without any tangible positive effect on safety.

## EU

In 1993 the commission presented its report on "A common policy on safe seas". While accepting in general terms the overriding responsibilities of IMO in this field the Commission felt that it, too, should watch developments closely and a reference was also made to the unique opportunities of the EU "to enforce, with common measures and rigour, respect of the same standards of vessels of all flags when operating in EU waters".

In the so called "Kinnock report" of 1996 safety issues were also highlighted and in respect of the two main subjects of the heading it was proposed to "consider legislative action and financial sanctions for cargo owners who knowingly or negligently use sub-standard shipping" and further that one should "examine the question of mandatory third party liability coverage in shipping as a condition for entry into EU ports". It is of interest to note that, when the Kinnock report was submitted to the EU Council, that body did not even mention the issue of insurance and also softened considerably the reference to the cargo owners by stating that the EU should: "consider, in consultation with the industry, whether to extend the commitment to safe operation in shipping to cargo owners under certain circumstances". The Council did not say THAT, but instead IF, it pointed to the need for consultations with the industry and it felt that measures might be considered under certain circumstances. A discussion paper on the subject of cargo owners' responsibilities is presently being considered within the Commission and might be submitted to member governments and other interested parties early in 1998.

There is no indication that the Commission is presently engaged actively in marine insurance, but that subject might of course be taken up again and no doubt developments in IMO will have a bearing on what the EU might do in future.

## OECD - Maritime Transport Committee

After 1945 the Maritime Transport Committee was for a number of years the co-ordinating maritime policy centre of the OECD member countries. It still played that role when UNCTAD got actively

engaged, from 1964 onwards, in shipping policy issues with the aim of promoting the interests of the developing countries. When shipping started to engage the EU the importance of the MTC was reduced but it is still dealing with a variety of maritime subjects, not least economically oriented ones.

The issue of substandard shipping is approached by the MTC from a different angle than those being at the forefront in the EU and IMO. The point of departure of the MTC is that an owner (or a shipper for that matter) operating or using a substandard vessel gains an unfair competitive advantage over his more conscientious colleagues. Reports from the MTC do show that those advantages can be substantial and that there are a significant number of operators/users thriving on such practices.

While not directly studying the two subjects of this report the work of the MTC deserves attention. But also in this case it is reasonable to assume that quite some time will elapse before any concrete steps influencing the situation will be taken within the OECD.

## **4. Cargo interests**

### **4.1 The concepts cargo owner/shipper**

(The Swedish language report contained a section, preceding this one, about the main actors on the shipping market, but as that section was primarily aimed at persons not having any experience of shipping, and shipping policy, it is omitted here).

The point of departure for this section must obviously be the different texts from the EU which form the basis for the present study. Any contemplated action against cargo interests in respect of choice of vessels for ocean transportation presupposes adequate answers to the following two questions:

- 1. Who is the legal subject against whom sanctions or other legal actions can be directed?**
- 2. Which actions or omissions should be penalized and how can they be legally defined?**

## 4.2 Cargo interests

In the different EU texts cargo interests are called "cargo owners", "shippers" and, sometimes "charterers". The idea of sanctions against such interests is obviously based on a link to the choice of vessels for transporting cargoes. In other words: The company or person who actually selects a vessel which is then or later on proven to be "substandard" should be the target for any remedial action. To what extent is such an identification physically possible and to what extent can it be made *before* the actual shipment of goods (in order to prevent a dangerous sea voyage undertaken by substandard ship)?

Of the three possible subjects identified above the concept *charterer* is fairly easily identified, although it covers the whole range from actually assuming full responsibility of operating a ship (bare boat charter) to the far less tangible act of reserving a limited space on board a ship for transporting own or others cargoes' (slot charter). The charterer *might* be the owner of a cargo transported on board the chartered ship (if for example an industry charters a ship for a single or for consecutive voyages) but in practically all cases he is *not*.

The concept of *cargo owner* is not legally defined, possibly because its meaning is too obvious to require such a definition. But there are two considerable problems when looking at that concept from the point of departure of this report: Firstly, in accordance with maritime law the ownership of cargoes can change quickly and repeatedly - even at mid-ocean - and (that is at least the situation in respect of Swedish law) the transfer of ownership is defined differently in civil law, as compared to taxation regulations. Secondly the cargo owner *might* be the subject responsible for choosing the vessel but as often as not he does not assume that task. In other words: There is by no means a necessary link between cargo ownership and the choice of vessels.

Now, what about the concept of *shipper*? In the Hamburg rules (article 1.3) a shipper is defined in the following manner: "Shipper means a person by whom or in whose name or on whose behalf a contract of carriage of goods by sea has been concluded with a carrier, or any person by whom or on whose behalf goods are

actually delivered to the carrier in relation to the contract or carriage by sea". The "handbook" Use of Maritime Transport (United Nations-ESCAP 1988) has the following to say: "In the context of importing or exporting the 'shipper' is the trader who is responsible for and controls transport". It is obvious that these two definitions do not correspond fully, and, moreover, the second definition goes too far to reflect real life. The shipper is not at all always the person who "is responsible for and controls transport". It is rather the opposite in that roughly 90 per cent of all shippers have no control at all of transport and has no means of deciding on what ship to choose for the transport of goods by sea. The vast majority of the innumerable cargoes which are sent every year by sea are most frequently stowed together with many other units in containers or palletized and sent to sea by liner or other agents, notifying the shipper at what time the goods can be expected to arrive at its destination. Most often the shipper learns only afterwards on what ship his goods were transported and he has, in real life, no possibility whatever of influencing the choice of vessel. The broker or agent might play an important role in that respect, but those parties normally have no link whatever to the ownership of the goods.

As mentioned before it is quite possible to identify *in retrospect* who has been responsible for the choice of a particular vessel but if such a route is followed you cannot prevent the hazardous voyage, as you can identify the culprit only after the completion of the voyage and maybe even after the substandard ship has left the port.

It is true that *the receiver of the goods* is more and more often being made responsible (together with the owner or charterer) for ocean transportation. Such is the case in respect of nuclear and oil transportation as well as for certain hazardous or noxious substances. But in those cases the situation is made simple by the fact that the cargo interests are large, responsible and easily identifiable companies, having a strong interest of their own in choosing high quality ships for the transportation of their dangerous or sensitive and often high-value cargoes.

The trend is clearly to make cargo interests responsible (together with owner or operator) for ocean transportation, but such a co-

responsibility has so far been limited to cargoes which, for one reason or another, are considered particularly sensitive or dangerous.

So, in regard to question 1 at the end of section 4.1, the conclusion must be that there are both legal and practical difficulties, in identifying the subjects against whom legal or other preventive or punitive actions can be taken. And the situation is even worse than that. Because of the proliferation of *terms of trade* (f.o.b., c.i.f. etc.) exporters and importers can easily - should they so wish - "manipulate" those terms and put the responsibility for a shipment where they see fit. If, for example, punitive action is taken in, say, Belgium against importers who choose vessels for their goods and normally buy their goods abroad f.o.b. (free on board). To retain the right of that choice the importer can easily change to buying c.i.f. (cost insurance, freight) and accordingly make the exporter in, for example Argentina, responsible for the selection of the ship. If that ship is substandard you can hardly punish the Belgian importer who will categorically state that he is not responsible for the choice of the vessel. And in Argentina there might be no sanctions in force. And the substandard ship continues to trade as before.

#### **4.3 Unseaworthy and/or substandard ships**

As mentioned towards the end of section 4.1 it is necessary to analyze the kind of acts or omission by cargo interests which could be penalized. Going back again to the initiatives within the EU the suggestion is that sanctions should be applied against cargo interests which have "knowingly or negligently chartered or used unseaworthy or uninsured ships" (excerpts from a speech by commissioner Neil Kinnock in Dunblane 8<sup>th</sup> September 1997). In the Kinnock report from 1996 the reference is instead to "sub-standard shipping".

While the concept of seaworthiness has degree of legal stability since it has been subjected to much litigation after the loadline initiative by Mr Plimsoll in the 1870s, the concept sub-standard ship remains in essence legally undefined. You could possibly say that it resembles a ghost in that - when you see it - you know what it is, while a technical description is difficult. Looking first at *seaworthiness* as used in the international safety at sea framework

of the IMO you find that it is referred to in rather general terms. In SOLAS (6 [c] and 11 [a]) it is stated that a ship should be "fit to proceed to sea without danger to the ship or persons onboard". And in MARPOL (4[4]) the words used are: "fit to proceed to sea without presenting a threat to the marine environment". National maritime codes tend to be more specific and detailed. That is at least the case with the Swedish maritime code which is fairly recent (1994). In that instrument seaworthiness is extended beyond a technical concept, based on hull and machinery, to comprise also all kinds of equipment, adequate manning, sufficient stores etc. The concept of seaworthiness has accordingly been extended in several respects and the Swedish Minister of Justice, when introducing the draft law, stressed that this extension means that seaworthiness is no longer "an absolute or uniform concept", but that it must be linked to the conditions in each individual case and also take into consideration a ship's ability to carry a certain cargo safely and to perform the voyage intended without submitting the ship, the crew, the cargo and any passengers to undue risks.

It is reasonable to assume that cargo interests are in practice facing greater and greater difficulties in assessing the seaworthiness or otherwise of a ship the more extended the interpretation of that concept becomes. In this regard recent developments have created additional difficulties. Is it reasonable to expect cargo interests to investigate to what extent a certain shipping company has satisfactorily implemented the International Safety Management Code to the extent that such implementation affects safety? You might of course say that certification by a maritime authority is adequate proof, but is that proof adequate no matter which maritime authority appears as guarantor? And what about the 1995 amendments to the International Convention on Standards of Training, Certification and Watchkeeping for Seafarers? As safe and adequate manning is an important element of seaworthiness the amendments of that convention requires substantial proof, not only of certificates of crew members, but also of their ability to perform onboard up to the standards indicated in the certificate. It might be natural and reasonable for charterer to make certain that those requirements are met, but you could hardly expect a cargo owner to look into such matters. And if he does not - or cannot - has he then made certain that the ship is seaworthy in every respect?

The role of cargo interests in respect of seaworthiness is legally complex and next to impossible in practice.

Turning now to the concept of *substandard ships* we will find that the slope is even more slippery. In spite of the difficulties just described in relation to seaworthiness that concept has at least been "stabilized" through court decisions and learned treatises. But substandard in the context of shipping remains nebulous and vague. It seems as if only one serious effort has been made at the international level to tackle that concept. In accordance with the IMO resolution 787, paragraph 1.6.9. a ship is categorized as substandard if its "hull, machinery, equipment or operational safety is substantially below the standards required by the relevant conventions or whose crew is not in conformance with the safe manning document". That same resolution also indicates examples of situations when a ship can be considered to be substandard. A common denominator for those examples is that they focus more on the ship itself, its certificates and equipment, than on the operational aspects. You might of course simplify matters by just saying that a ship is substandard if it is arrested by authorities while in port. But although there has been established an amount of uniformity for criteria of arrest in the context of the Memorandum of Understanding (the agreement on port state control, concluded originally between 14 European governments in 1982) this agreement is regional only and is still subject to the degree of uncertainty linked to the assessment of a ship by an individual inspector. And there are of course no guarantees against other criteria for substandard being developed in other regions so that one and the same vessel might be classified as substandard in one region and acceptable in another.

It would appear as if this report paints a rather gloomy picture of the possibility of making cargo interests play an even more active part in marine safety by avoiding unseaworthy and/or substandard ships. But there are other considerations which might strike a more optimistic note. Experiences indicate that low quality ships are primarily found in certain types of shipping. Bulk carriers figure prominently on that list, followed by a number of crude oil carriers and certain general cargo ships. In many other segments of shipping there is simply no room for substandard vessels. The dangerous character of many cargoes and high quality requirements of

customers bar bad ships from many trades. Nuclear cargoes, gas, refined products of oil, dangerous chemicals, cars and lorries, and high value containerized cargoes require - and practically always get - safe ships to cater for their needs. Substandard ships are generally banished to certain trades and to certain cargoes. Coastal shipping is a danger zone, particularly when operating in one and the same nation.

It is a mistake to think that only the developing world is the hunting grounds of substandard shipping. There is, just to mention one example, an influx of river crafts in the Baltic trades, carrying both oil and timber cargoes from the former Soviet area to neighbouring countries. Those shallow crafts are hardly suitable far beyond the river systems and represent a potential hazard to all shipping in that area. In those cases it should be possible for cargo interests to show more restraint. But in this case - as in others - it would seem as if economic considerations outclass caution. But there are examples of cases where cargo owners have succeeded in driving substandard ships from certain trades. It happened in the Japanese bulk trades a few years ago. Through concerted action the Japanese importers of bulk cargoes enhanced their quality requirements in respect of both age and standard and thus succeeded in driving substandard bulk carriers away from those trades. One negative effect of that action was that those ships started to operate instead in other trades - like for example the North Atlantic - where statistics showed a sharp increase in foundering, often with heavy casualties. Effective port state control is another means of preventing substandard ships from trading. But such control is presently exercised in certain limited regions only and, even if extended, it might not be effective in regions where systematic bribery constitute a tolerated element of behaviour.

Under this section a few words should also be said about the activities of the International Transportworkers Federation and actions against certain ships in a handful of countries where the maritime unions are strong. The actions of the ITF are no doubt beneficial in the sense that the kind of vessels they try to stop are frequently substandard. But it must be borne in mind that the overriding interest of the ITF is to protect the crews and their economic and environmental conditions. The mere fact that the ITF issues a "blue

ticket” to a ship once the owner has agreed to sign a collective agreement with the crew is no guarantee whatsoever that a particular ship is up to standards. It might be, but the aim - and the competence for that matter - of the ITF is not to inspect the ship and its equipment. Or rather any such inspection is limited to the quarters and safety equipment of the crew and not, for example, if the bulkheads of that ship are corroded. But the ITF has gathered much information over the years on ships and shipowners and that experience could prove very useful from the point of view of port inspection. An ITF action against a ship is a valuable signal that safety might be in jeopardy.

## **5. Marine insurance**

### **5.1 Introduction**

If a preliminary conclusion, based on the preceding sections, might be that there is a tangible need for a stronger input by cargo interests in enhancing maritime safety, the following section will show, that as far as marine insurance is concerned, the possibilities of mastering those involved in such efforts are clearly there, but the need for such additional efforts are in doubt. (When the report in Swedish was written - during September - December 1997 - the contents of IMO Legal Committee document LEG 76/WP 1, 13 October 1997, was not known. It became known to the author only on 6 February 1998, in connection with a seminar in Gothenburg about the report. The document from IMO contained important data [submitted by Norway] on uninsured vessels. On the basis of that document it can be stated that many part of vessels arrested in the Paris Memorandum of Understanding area January - September 1996 were in fact uninsured. Out of 166 vessels on the list attached to the document, no less than 64% of the number and 45% on the tonnage lacked P&I insurance with any of the clubs, members of the International Group. While that does not exclude that those vessels might have some other kind of insurance, the percentages shown are much higher than what has been estimated before. It would thus seem as if the problem of uninsured ships is much greater than what was believed earlier and this, of course, is quite alarming. If

known at the time the Swedish report would have reflected the seriousness of the problem in a much more marked manner.)

## 5.2 Marine insurance

It seems necessary to state again what has been said before: The aim and purpose of this report is only to highlight those aspects which have been raised within the EU commission as a proposed means of enhancing marine safety by activating - more than hitherto - the cargo owners and the marine insurers. The mandate of the Swedish report is thus limited, and this abbreviated version will obviously have to follow that limitation.

The Swedish version - being aimed at a broader non-maritime readership - contained a fairly extensive section on marine insurance, explaining its background and the different kinds of insurance which are offered in this field. For the purpose of this short English version most of that section has been omitted, as this version is basically supplied for the possible benefit of those who are engaged in maritime affairs, be it as government officials or commercially oriented servants of the trade, all having a certain knowledge of maritime matters.

When comparing marine insurance to land-based activities with a similar purpose (to insure against unexpected losses) you could say that marine insurance is characterized by a number of fairly well defined - and also isolated - segments. A number of companies provide hull insurance, but none of those (except the Swedish Club) also offer P&I insurance. Almost all who offer P&I insurance are mutual, and thus owned by their members, while cargo insurance is provided by other (and often very big) companies. The particular maritime legal concepts, like general average for example, do not simplify the situation.

The EU initiative in respect of marine insurance - and again it is pertinent to point out that this report is based entirely on the EU initiatives - considers the possibility of "examining the question of mandatory third party liability coverage in shipping as a condition for entry into EU ports" (excerpts from the Kinnock report of 1996).

As mentioned before (section 3.2) the Council of the EU has chosen not to comment on the issue of marine insurance, while softening the proposal as regards cargo interests. That omission might have sprung from the knowledge that the IMO handled that issue already, but it has not been possible to establish if that is so or not. It remains a fact, however, that the executive body of the EU has so far not proposed any specific action or even a study in respect of marine insurance as a partner in further enhancing maritime safety. But the EU might, of course, bring the issue up again at any time it chooses.

### **5.3 Protection and indemnity insurance**

Both in the Kinnock report and as matters develop within the IMO (see section 3.3) the marine insurance which it at stake is the protection against third party liability - the P&I insurance. Such insurance is practically always mutual in that the legal entities offering cover are owned by their members. Traditionally the policies are renewed 20 February each year and the members pay a preliminary contribution, which can be subject to increase or decrease, depending on the result of any particular year (such modifications to be decided upon much later, when the result of a certain year has been finally settled- maybe after lengthy litigation in a number of cases).

P&I insurance is provided by a number of mutual clubs (in this report we disregard the few and small companies, which are not mutual). As mentioned before those clubs normally offer only P&I insurance, the Swedish Club being the only exception, also offering hull insurance.

In the EU context, when suggesting a more active role for marine insurance in maritime safety matters, it is argued that "uninsured or underinsured ship" (Kinnock report-speech in Dunblane 8<sup>th</sup> September 1997 by Neil Kinnock) presents a threat to the marine environment. When this issue has been extensively dealt with by the IMO Legal Committee it has been argued (particularly by the International Group - which is a body representing the individual P&I clubs and also acting as reinsurer of some of their risks) that any action in this field would just aim at doors which are already open and create a bureaucracy which is uncalled for. That statement also

refers to the requirement to produce certificates of existing P&I coverage, specifying the conditions of the policy.

Bearing in mind that most ships - at least those trading in the European area - are insured (but see also section 5.1) it has been argued that it is quite unnecessary to require certificates of valid P&I insurance to be presented. At the same time it is somewhat difficult for a bystander to understand why it would be difficult to present a certificate of valid and satisfactory P&I insurance to ports inspectors or whoever asks for it if the insurance cover is there. To the extent that commercially sensitive elements are involved (like for example the degree of deductibles involved (self risk) or other matters influencing the premium) then, surely, there would be other possibilities of arranging that.

It would seem to an outsider as if the P&I interests continue to present their case as one so complex that normal human beings cannot ever grasp its intricacies. If such is the reason for not rocking the present marine insurance boat it seems somewhat erratic. The present P&I coverage is quite extensive and good. But the clubs, (fighting viciously among themselves) are out on a limb if they try to say no serious improvements can be made in a maritime insurance market, which has enjoyed the protection of exclusivity for years. Because of the fierce competition between the clubs premiums are now at their lowest for many years and those premiums form an important part of the running costs of a ship. To give an example the annual cost for P&I cover for a fairly large crude oil carrier can amount to about 400,000 USD.

As mentioned under section 3.2 the IMO Legal Committee is presently engaged in studying both the general issue of "compulsory insurance" as a means of enhancing further marine safety and those elements of P&I insurance which aim at protecting the interests of passengers and crew members. Some time will no doubt elapse before any concrete decisions are taken at the international level. This of course does not exclude the possibility that the P&I clubs themselves can make progress by, for example, agreeing on a uniform certificate for P&I insurance and thus preclude intervention by governments. The EU might also take up the issue of "compulsory insurance" again and it is of course also possible (but hardly de-

sirable) that individual governments might take action. The United States does already operate a system requiring certificates of financial responsibility (COFRs). The intensive vessel traffic in UK waters has made that government indicate a firm line in respect of "compulsory insurance" as shown in the IMO Legal Committee document LEG 74/6/1 (13 September 1996), paragraph 8: "The UK is (therefore) considering primary national legislation to require some or all ships calling in UK ports or operating in UK waters to have compulsory insurance or other financial securities to meet third party liabilities".

In connection with the question of whether there is a real need for "compulsory insurance" or not it might be of some interest to note that a requirement has been introduced since 1 January 1997 that all owners of Swedish flag vessels wanting to enjoy the present government support must provide evidence of satisfactory marine insurance, including P&I cover. In about 220 cases submitted so far there is only one where the P&I cover was considered to be unsatisfactory. The problem was remedied by the owner getting proper P&I coverage.

#### 5.4 Deductibles and direct action

In connection with marine insurance two additional aspects deserve to be mentioned briefly. *Deductibles* (in the Nordic countries called "self-risk") constitute the amount which the insured will have to cover himself before any claim can be laid to compensation by the club. Obviously the degree of deductibles has a direct impact on the premium which the owner is requested to pay to the club. The mutuality concept of P&I insurance and the system under which it operates also means that an owner can be compensated by the club only for the amount which has actually been paid to a claimant (once the owner has first paid his deductibles). Even so there is no guarantee that the owner will get his compensation. The club might decide that the owner was not under any legal obligation to settle the claim or he might have settled it at too high a level. The owner can then be denied compensation or the amount can be reduced. In practice such problems are of limited relevance as the owner will in all likelihood consult the club well before any action is considered in respect of a claim.

As indicated briefly before *direct action* is normally excluded in P&I insurance, viz. a claimant cannot bypass the owner and request compensation directly from the owner's club. This restriction can of course prove fatal for a claimant (for example a stranded crew) as an owner might not be found, or, if found, might be unable to pay a claim. This limitation has been extensively discussed within the IMO Legal Committee and it remains to be seen to what extent the clubs - through their International Group - might be willing to try to find some voluntary solution to the problem.

### 5.5 The time element as a vehicle for quality

This report does not deal with the classification societies and will touch only briefly on the role of ship financiers for improving further safety of shipping. The clubs - being mutual - should take a stronger interest in the quality of the ships they insure, as a sub-standard ship presents an increased risk for all members that premiums will have to be increased (if the competitive situation so permits). As policies are normally renewed once a year (on 20<sup>th</sup> February) the clubs should be able to keep a constant or at least frequent vigil on the quality of the ships they insure. The quality consciousness of the classification societies has improved considerably over the last few years. The normal intervals between inspections (unless a ship encounters unexpected events) are five years, which would seem to leave a certain room for the condition of a ship to deteriorate considerably before any action is taken by the class representatives. And the ship financiers can exercise full and effective quality control only during the negotiations preceding a decision to make the investment. These three parties - the clubs, the classification societies and the ship financiers - can all play important roles in the efforts to enhance marine safety. Recent complaints indicate that one of them does not always feel that the others do what they should. An example is the criticism from one classification society that certain bulk carriers which were expelled from one society and transferred to the Polish register enjoyed the same premiums in spite of the fact that they were expelled because of unsatisfactory safety standards. It would seem as if the marine insurers concerned have declined to comment on that serious allegation.

## **6. Ship financiers - their contribution to marine safety**

In the introduction to this report it was mentioned in passing that the EU initiatives in respect of maritime safety did not explicitly mention ship financing. A brief reference to that aspect was included in the Swedish version of this report and should also be referred to in the abbreviated English version.

The preceding section refers to the importance of engaging more than hitherto the insurers, the classification societies and the ship financiers in the task of further enhancing marine safety. At a time when ship financing has to rely almost entirely on external sources for the supply of capital to investments in shipping it is no doubt interesting to analyze to what extent banks and other institutions could be tapped as an additional source of enhancing maritime safety.

You might say that there is no need for such initiatives as banks and other sources of finance have always been very selective in their approach and are very competent in assessing their risks. That might be so, but in shipping there are many examples of less judicious investments, not least the happy influx of capital during the short periods of freight rate booms, leading invariably to a large number of newbuildings entering the market simultaneously when the market has already collapsed.

As mentioned before the only - but very important - occasion when ship financiers could have their say is during the negotiations preceding a suggested investment in ships. As is the case in respect of land based industries the caution exercised in that connection is very much influenced by the experiences of the two parties in their previous relationship. If there have been contacts over many years - maybe a mutually remunerative one - a favourable decision might be reached quickly and few questions are asked. If, on the other hand, the relationship is newly established discussions might continue for long, and might eventually terminate in a refusal to provide the necessary funding. But the ship financiers clearly have a say - and an important one. The issue is to what extent they exercise it in practice and how thorough they are in their analyses.

Looking at the contracts which are signed you get truly impressed. Innumerable paragraphs specify the conditions which have to be met by the lender. It all looks very reassuring. But contracts with both lenders and providers of capital seem to indicate that the volume of the contract does not correspond to realities. At least not when the parties have a long standing relationship. And the degree of actual control varies rather much, it seems, from bank to bank, from mortgage institute to mortgage institute. Some are very thorough, other rather lax. But the paragraphs of the contract are as many, and practically identical.

It is interesting to note, also, that the financial institutions maintain a degree of scepticism towards ship financing, in that they generally request the owner to pay the premium of a special insurance, safeguarding the bank against the non-fulfilment of certain financial obligations of the owner in accordance with the contract (in the rather cumbersome terminology of Sweden such an insurance is called [free translation] a capitalinterestinsurance).

The same applies in all likelihood in other countries. Banks and other providers of capital obviously have differing experiences of ship financing, some being experts of long standing, others having shipping as a sideline of financial activities.

But if those who provide capital for ship investments did apply seriously all the contract clauses about classification and safety requirement, evidence of satisfactory insurance, adequate operational manning procedures etc., they could indeed contribute more than hitherto to a safer environment at sea.

## **7. Some conclusions**

### **7.1 General**

A reference was made in the introduction to the specific mandate which stated the areas which should be covered in the report. It was also mentioned that certain parts of the Swedish version were not covered in this abbreviated paper. Specific references to Swedish law and Swedish conditions have been minimized and the con-

cluding recommendations have been omitted as they were intended for further consideration by the Swedish Maritime Administration and the Swedish government. The present section of the version in English will accordingly mention in general terms only and briefly some conclusions which could be drawn from the contents of the previous chapters.

## **7.2 Cargo interests**

Considering the large variety of cargo interests as well as the many uncertainties linked to the two concepts unseaworthiness and sub-standard shipping it is hardly realistic to consider a general system of sanctions against "cargo owners who knowingly or negligently use sub-standard shipping" (quotation from the EU Commission paper: "Towards a new maritime strategy".) The flexibility of the terms of trade and the possibility of changing them to avoid unwanted consequences increases the practical difficulties further.

A combination of approaches might go some way towards the desired end. Firstly to encourage the private parties to agree on a "quality code" with a number a criteria or check points aiming at limiting the use of substandard shipping. Secondly some kind of sanctions against charterers of substandard bulk, crude oil and general cargo carriers and/or, thirdly, targeting the receivers of cargoes and sanctioning them in connection with ships being detained following port state control. To that one should add wide publicity of flagrant cases of detention, mentioning also the charterer/cargo owner/receiver.

## **7.3 Marine insurers**

As mentioned under section 5.1 it would now appear as if the number and tonnage of uninsured ships is far greater than has been thought previously. As there are considerably uncertainties linked to available data in this respect the IMO should consider, as a matter of priority, to develop, in co-operation with the insurers, a reliable system of identifying uninsured vessels and to agree on an internationally accepted certificate for both hull and P&I insurance. Lack of insurance should also be identified as an additional reason for detention in port until this shortcoming has been rectified.

In parallel a system of compulsory P&I insurance should be developed for both passengers and crews (or alternatively an accident insurance) with a corresponding certificate to be provided whenever requested. At least in countries with a lively seasonal passenger/tourist traffic it appears desirable to make sure, on the national level, that such crafts have sufficient third party liability insurance. It might also be motivated to consider to what extent - if any - it is justified today to exclude marine insurance from compulsory elements in national insurance regulations.

#### **7.4 Ship financiers**

On the one hand ship financiers are very experienced in assessing risks and on the other experience over the years show that banks tend to contribute actively to long shipping market depressions by supplying credits to shipowners during brief market peaks. A more long term approach might be advisable, but the decisions are of course influenced by many different considerations, among those the amount of available funds and the length of the relationship of the parties. Again the financiers themselves should seek to establish some kind of quality code with a check list, but the competition between the suppliers of capital does not make such a co-operation an easy task. It would be interesting if some recognized institution (like the World Bank or the OECD) could make an assessment in retrospect of ship investments over a number of years.

## List of abbreviations used in this report

<b>ESCAP</b>	<b>The Economic and Social Commission for Asia and the Pacific (Bangkok).</b> <b>The European Union (Brussels).</b>
<b>F.o.b - c.i.f</b>	<b>See explanation in relevant text: cargo interests.</b>
<b>IG</b>	<b>The International Group of P&amp;I clubs (London).</b> <b>The International Maritime Organization (London).</b> <b>The International Ship Management Code (IMU 1993).</b> <b>The International Transport Workers Organization (London).</b>
<b>MARPOL</b>	<b>The IMO Marine Pollution Convention (1973 and 1978).</b>
<b>MOU</b>	<b>The Memorandum of Understanding between originally 14 European states about port state control etc., since enlarged both in contents and membership (Paris).</b> <b>The Maritime Transport Committee of the OECD (Paris).</b>
<b>OECD</b>	<b>The Organization for Economic Co-operation and Development (Paris).</b>
<b>P&amp;I</b>	<b>Protection &amp; Indemnity - a third party liability insurance offered by some 15 mutual clubs, co-operating in the IG.</b>
<b>SOLAS</b>	<b>The 1974 Convention on Safety of Life at Sea.</b>
<b>STCW</b>	<b>The International Convention on Standards of Training, Certification and Watchkeeping, including the important 1995 additions.</b>
<b>UNCTAD</b>	<b>The United Nations Conference of Trade and Developments (Geneva).</b>
<b>WMU</b>	<b>The World Maritime University (an IMO institution, located in Malmoe, Sweden).</b>