

Passenger Liabilities

As cruise ships get larger the potential for catastrophe becomes all the more alarming. This is especially so with all the security scares that will be with us for the foreseeable future, apart from the ever-present possibility of accidents. The liabilities in such an event for a cruiseship carrying over 3,000 passengers would be vast. Providing insurance cover for this type of event is a major challenge and the premium costs to cruise lines are substantial.

The Athens Protocol sets out new statutory liabilities for passenger claims increasing the amounts that would have to be paid in compensation. This is causing concern among those institutions providing insurance cover for cruiseships as well as the lines themselves.

The Athens Protocol was adopted by an IMO Diplomatic Conference in November 2002. Following achievement of the necessary number of ratifications it will come into force one year later. The current expectation is that the EU will ratify on behalf of all EU states by the middle of this year, meaning that the Athens Protocol will come into force during 2005.

Higher limit

The Athens Protocol increases the minimum guaranteed liability limit to SDR250,000 (\$330,000) per passenger. This compares with SDR46,666 (\$61,000) under the existing 1974 Athens Convention. The IMO has recommended a maximum limit of SDR400,000 (\$525,000) while individual states can impose a higher minimum. In 1999 the UK government set a SDR300,000 minimum limit for passenger ships operating out of the UK.

As an example of its impact, for the 1994 *Estonia* ferry disaster in which 728 passengers were lost, under the present Athens Convention the liability was \$44.6m. Under the proposed new minimum liability limit, this figure would have jumped to about \$240m, and under the maximum limit to \$382m. For a cruiseship carrying 3,500 passengers this would mean providing cover for \$1.2bn under the minimum limit (see graph). Additional cover would be needed for crew and other claims.

Institutions financing cruiseships will need to ensure that these liabilities are fully covered as any problems or gaps in

cover could result in serious financial problems for the operator and potential default on loans. This change could therefore cause some re-assessment of lending risks to cruise operators and a need for operators to consider additional mortgage protection or other insurance.

Clubs decide

P&I clubs will have to decide if and how they will cover this increased liability and what the cost will be to passenger operators and passengers. According to Graham Barnes, director of BankServe Insurance Services in London "The cost all depends on the P&I clubs." The key question is whether the P&I clubs will provide passenger vessels operators the cover required under Protocol either:

- to the minimum level to allow cruiseships and ferries to trade in countries that ratify the convention. This would be to a level of SDR250,000 per passenger and guaranteed, or
- to the maximum level of SDR400,000 (\$525,000) per passenger, or higher, and guarantee the first SDR 250,000, or
- Abandon cover for passenger liabilities.

Mr Barnes suggests that the first option is most likely. This is the minimum necessary to allow passenger vessels to continue trading. "This means P&I club managers must get the support of their members, 95% of which do not operate passenger vessels and categorically reject taking the Overspill risk (mutual liability for claims in excess of pool reinsurance)," said Mr Barnes

The current pool re-insurance limit appears, at first sight, to be sufficient to cover a 3,500 passenger cruiseship, but it does not take into account other liabilities covered by the clubs, such as crew, pollution, removal of wreck and collision.

In order to get members approval, club managers will have to ring-fence passenger liabilities so that members not operating passenger vessels carry no risk of an Overspill claim from the Athens Protocol. This can only be done by having a separate re-insurance programme for passenger liabilities, paid for by those members which require passenger liability cover. Such a pool re-insurance programme for passenger liabilities up to \$2bn would cost an estimated \$300m plus per annum.

Mr Barnes told LSE that P&I club managers are in the advanced stages of setting up an International Group Captive, code named Hydra, to handle all pool claims, including the pool re-insurance programme. Hydra could arrange to give the requisite guarantees meeting the requirements under the Athens Protocol as well as the Certificates of Financial Responsibility under OPA '90 in the US. These guarantee costs might be \$100m per annum.

This makes a crude total of \$400m per annum to be paid for by members requiring cover for passenger liabilities. Such costs would be passed onto passengers through ticket prices. Costs would be divided between cruiseships and ferries. Loss statistics show that ferries are by far the greater risk.

Statistics for 2000 show that about 12m cruise tickets were sold and 417m ferry tickets sold on what can be described as insurable ferries. Based on these numbers, an extra \$1 on a ferry ticket would raise over \$417m. Assuming the average cruise duration is five days, \$1 per day on a cruise ticket would raise \$60m. This total of \$477m should meet the cost of cover.

Single pool cover

The UK P&I Club, a leading cruise-ship supporter which includes Carnival Group among its members, appears to want to maintain passenger liability cover within the single pool re-insurance programme and stand down the objections of many leading shipowner members. It takes the view that "the value of the International Group system is to provide as much cover as possible for the needs of all types of owner and ship. Any attempt to reduce the exposure in respect of individual risks is ultimately detrimental ... The real impact is pretty limited." But the impact of a major overspill claim would be significant.

If P&I clubs maintain unity and stick to their traditional approach of not singling out any individual risks for passenger ships or any other type, there should not be a major impact on costs to cruise lines or passengers. A problem would arise if some owner members with other types of ships balked at providing this level of cover.