



INTERNATIONAL CONFERENCE ON THE
REVISION OF THE ATHENS
CONVENTION RELATING TO THE
CARRIAGE OF PASSENGERS AND THEIR
LUGGAGE BY SEA, 1974
Agenda item 6

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**CONSIDERATION OF A DRAFT PROTOCOL OF 2002 TO AMEND THE ATHENS
CONVENTION RELATING TO THE CARRIAGE OF PASSENGERS AND THEIR
LUGGAGE BY SEA, 1974**

Direct liability of insurers

Submitted by the Comité Maritime International (CMI)

SUMMARY

Executive summary: In this paper the Comité Maritime International seeks to give some background to the issue of direct action against the insurers of shipowners' liability for passenger claims.

Action to be taken: The Conference is invited to consider the information contained in this paper.

Related documents: -

1 In the draft protocol of 2002 to amend the Athens Convention relating to the Carriage of Passengers and their Luggage by Sea, 1974, to be considered at a Diplomatic Conference in October 2002, it is proposed to introduce direct action against the carrier's liability insurer by personal injury claimants. Liability to passengers is, in the case of most passenger ship owners, insured by the Protecting and Indemnity Association ("P and I Club") in which the ship is entered. The International Group of P and I Associations ("International Group") has opposed the introduction of such provisions.

2 It has been suggested that a short paper from the Comité Maritime International (CMI) may assist delegates in understanding the issues involved in the opposition to the proposal for direct action. The CMI is an international association of National Maritime Law Associations which includes in its membership lawyers regularly acting for both claimants and respondents in personal injury cases, as well as for passenger ship owners, P and I Clubs and insurers of all marine risks. The object of the CMI, according to its constitution, is "...to contribute by all appropriate means and activities to the unification of maritime law in all its aspects."

3 In giving its comments, the CMI wishes simply to provide some background to the opposition to the proposed right of direct action for passenger claims. However, the organisation does not wish to take a position for or against such direct action, nor does it seek to comment on the issue of limited liability for such claims, or the amount of any such limit.

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The existing arrangements

4 The P and I Clubs, which cover most passenger ships for liabilities to passengers, are all similar in structure. Each is a mutual insurer which indemnifies its assured (called a “member”) for legal liabilities which it has become liable to pay and has paid, which are within the range of insured risks covered by the Club. The income of the Club consists of payments (called “calls”) which are levied on the members, partly in advance of the policy year (“advance calls”) and partly after the end of the policy year, when the claims falling on the membership of the club for that year become known (“supplementary calls”). Since the nature of claims covered by the Clubs is that they take some time to come forward, and take a significant time to settle, there may be more than one supplementary call for any one policy year, or indeed none at all if the advance calls prove sufficient.

5 Some Clubs have introduced in recent years a “Mutual premium” which includes the advance and anticipated supplementary calls and which is payable in staged payments, but the fundamentals, and the ultimate liability of members to contribute to a major disaster which exceeds the pool and reinsurance cover (see below), remains the same. This simple model demonstrates the fundamental structure of the P and I Club insurance system. In reality it is much more complex.

The International Group of P and I Clubs

6 This is an association of the largest Clubs based in London (plus three in Scandinavia, one in Japan and one in the USA) which pools the excess of any one claim (currently US\$5m) and buys reinsurance in the world market for the excess over the pool limit (currently US\$30m up to US\$1.5bn) - this is the largest reinsurance contract in the world.

7. The International Group also represents the interests of the P and I Clubs (and their shipowner members) at an international level including the International Maritime Organization (IMO).

8 Some substantial Clubs exist in London, and elsewhere, which are not members of the International Group. P and I cover can be purchased from them and other insurers, usually for a fixed premium with fixed, usually much lower, limits than those provided by the mutual Clubs.

9 The International Group Agreement has long been under scrutiny by the Competition Directorate of the European Union (EU) as being in restraint of free competition in insurance matters. A ten-year exemption was granted in about 1987 but its renewal was the subject of intense debate. It was finally accepted that the Group Agreement was not in breach of European Commission (EC) principles after some minor changes were made to the Clubs' accounting principles.

Other reinsurances and reserves

10 In addition to the reinsurance arrangements concluded in and through the International Group, each P and I Club has its own reinsurance arrangements specific to the needs of its membership. Such reinsurances may cover liabilities below the level at which the International Group pooling arrangements become involved, or above the level of the International Group reinsurance cover. In addition to reinsurance arrangements it is usual for P and I Clubs to retain reserves in order to smooth out the overall claims pattern from year to year.

The Impact of Direct Action

11 Since the inception of the P and I Clubs nearly 200 years ago, it has been of the essence of the mutual basis on which they work that the member should have paid any relevant claim before seeking reimbursement from his club. This was recognised in the judgments of the House of Lords in the leading case of the **Fanti and Padre Island** [1990] 2 Lloyd's Rep 191. Most P and I Clubs which are members of the International Group are governed by rules which are subject to English law. That case concerned the alleged right of a claimant who had obtained judgment against a member of a P and I Club which had become insolvent (and thus could not meet the judgment in full) to enforce the judgment directly against the P and I Club by virtue of the Third Parties (Rights against Insurers) Act 1930. The judgments of the members of the House of Lords did not specifically address the general principle of direct action, but were concerned with the interpretation of the Act. Nevertheless they did recognise that the unique status and origins of the P and I Clubs as mutual insurers did put them in a special position in the face of the possibility of direct action. The judgment of Lord Goff contains the following section:

“In a mutual insurance association such as a P and I Club, it is essential that members should be able to assume the financial probity of other members, because all of them are insurers as well as assured. To that end, it is customary to require each member to discharge his own liability before he can be indemnified against it by the club. Each member is, after all, running his own business; it is up to him to make sure that a claim against him is well founded, and the best way of ensuring that is to require him first to pay the claim before seeking indemnity from the club. I must confess that I was much attracted by this submission”.(page 202).

12 It was recognised by the House of Lords (page 201) that in many cases the Clubs do pay direct to the claimant the claims which have been agreed, either because the Club has given a letter of guarantee of the members obligations or because it is agreed, expressly or impliedly, that they should do so. Such arrangements do not change the fundamental obligation of the P and I club to indemnify its member.

13 Arrangements to create a direct right of action in favour of a claimant have been introduced in other cases, notably under the legislation enacting the International Conventions of 1969 and 1992 governing liability for oil pollution. Similar provisions are included in the pending conventions on liability for hazardous and noxious substances (“HNS”) and for pollution by ships bunkers, but these Conventions have not yet entered into force.

14 The 1969 and 1992 Conventions on Civil Liability for Oil Pollution Damage provide for the issue by the Government of the ship's flag State of a Certificate of Financial Responsibility (“COFR”) which certifies that insurance or other financial security is in force, which satisfies the requirements of the convention, and provides details of the name and address of the insurer. Article VII (8) of those Conventions goes on to provide for direct action against the insurer by the victims of oil pollution, and restricts the defences which may be raised by the insurer to such claims.

15 The practical effect of such provisions, which appear at first sight to be no more than a reasonable response to the difficulties of pursuing legitimate claims against the “one ship companies” which are now common in the shipping industry, is that the burden of defending and settling such claims has passed from the ship owner to his insurer, and that the general principle of indemnity which has underpinned the liability insurance provided by the P and I Clubs, has been set aside.

16 These four Conventions expressly provide that the defence of wilful misconduct of the shipowner is still available to the insurer, but any other misconduct, which may well prejudice the cover provided as between insurer and assured, will not be available to the insurer as a defence to a claim made direct against it.

17 The Rules of all the P and I Clubs whose managers are based in London, contain a provision expressly incorporating the English Marine Insurance Act 1906. The provisions of that Act contain a number of clauses which define circumstances in which the insurer is not liable. One of those is section 55(2)(a) which provides:

“The insurer is not liable for any loss attributable to the wilful misconduct of the assured...”

This provision is mirrored by the defence of wilful misconduct of the owner to which an insurer is entitled in defending a direct action for pollution damage, and, in the draft protocol, in defending a passenger claim. The other defences to which the insurer is entitled under the Marine Insurance Act 1906 will not, however, be available to a P and I Club defending a direct action by a passenger.

18 Further, compliance with the ISM Code is now a prerequisite of cover in the rules of all the P and I Clubs in the International Group. Since the ISM Code is now applicable, with effect from July 2002 to all passenger ships and to cargo vessels of over 500 tons, this is an important matter. The ISM Code requires that every ship owner should have in place a Safety Management System, including procedures for reporting and monitoring the safety and pollution prevention aspects of the operation of each vessel and ensuring that adequate resources and shore-based support are applied as required. It also requires that systems should be in place for the reporting and analysis of non-conformities, accidents and hazardous occurrences.

19 It is not difficult to imagine that any accident which gives rise to a claim under the COFR has the potential, on investigation, to reveal a failure of the Safety Management System for the ship in question, which could in turn prejudice the P and I insurance cover. Yet the issue of a COFR at the beginning of the policy year and the relevant provisions of the Convention mean that, in the case of an accident within the terms of the Convention the insurer will be obliged to pay the claim first and to seek recompense afterwards from the ship owner if there has been a breach of the terms of cover. In the case of a vessel owned by a one ship company which has suffered a major casualty and where the vessel's insurers are entitled to policy defences, the recovery prospects look distinctly doubtful.

20 Likewise, it is self evident that members of the International Group will not take kindly to contributing (through the Group Pooling Arrangements) to a claim paid by a member club in respect of an accident resulting from conduct by a member which fell below the standards set by the ISM Code, simply because that Club was obliged to honour the obligations to third parties resulting from a COFR issued under the proposed protocol.

21 One P and I Club, which is a member of the International Group, has already decided, as matter of general policy, not to accept passenger tonnage because it presents the risk of claims of a different nature from those to which a cargo vessel is exposed, and thus that such risks are inconsistent with the mutual nature of P and I insurance. The Chairmen of several Group Clubs have taken the opportunity afforded by their annual report to express grave concern at the potential exposure of the Group Member Clubs, and the Group itself, if a combination of high limits and direct action is imposed by the proposed protocol to the Athens Convention.

22 To a large extent, passengers by sea are now carried either in roll-on roll-off ferries or in passenger cruise ships, some of which are very large. The largest cruise ships in service now carry up to 3500 passengers and 1500 crew, and even larger ships are on the drawing board. The potential liability of a carrier in the event of a major casualty involving such a ship is therefore substantial. If the carrier's liability insurer is to be directly liable to the passengers of such a ship for sums of money substantially greater than those in the 1974 Athens Convention, and with a significant reduction of the policy defences otherwise applicable between the insurer and the insured (as to which see below), this is believed to have an impact on the insurance and reinsurance arrangements currently in place.

23 It is widely recognised that the compensation system created by the 1969 and 1992 Civil Liability Conventions on Oil Pollution Damage, including the right of direct action by claimants, has worked well for 30 years, and has not imperilled the P and I Clubs which insure such risks. The limits of the ship owner's liability under those Conventions (up to 59.7 million SDR or about US\$80 million) are, however, significantly lower than those under consideration for passenger claims under the proposed protocol.

Conclusions

24 Without trying to balance the pros and cons of applying to claims by passengers the principle of direct action against insurers presently applicable in the case of oil pollution, there appear to be well-founded arguments supporting the reluctance of the P and I Clubs which are members of the International Group to accept the principle of direct liability as proposed in the draft Protocol to the 1974 Athens Convention.

25 The issue of certificates of financial responsibility as proposed by the draft protocol will expose the liability insurers of the passenger vessels to which the protocol applies, to significantly greater risks, by reason of reduced defences, than those customarily covered by the P and I Clubs.

26 The complex arrangements for pooling and reinsurance of those risks, which make it possible for the member Clubs of the International Group to offer such extensive cover at present, may be put at risk if direct action such as is proposed by the draft protocol is to become a part of the law of most maritime nations.
