

Tankers weather P&I increases

Although presented by the clubs as a fait accompli, reinsurance rates for the top level P&I cover, so vital to tanker operators, is subject to tough behind the scenes negotiations. The outcome – announced only days before the renewal deadline of all P&I cover – was far from certain. Heinz Gohlish reports.

After a protracted and often difficult round of negotiation with their P&I club, tanker operators then immediately face a further tranche of increases in insurance premiums with the finalisation of the International Group's Excess Loss Reinsurance programme.

What was completed simultaneously in earlier years has now become two distinct events, inevitably with the same outcome. Indeed, for the renewals just completed, there was a likelihood that the excess loss reinsurance rates would bite harder than the primary level increases. In the event, that was indeed the case, albeit only moderately.

Undoubtedly, the first reaction from shipowners, on hearing of the International Group's increases in reinsurance costs was "it could have been worse". The fact that a 37% increase in costs can be absorbed with relative equanimity is due to several factors:

1. **Market perception.** Insurers buyers, in particular those at the high-risk end of the business such as tanker operators, have learned to be pessimistic of late. Underwriters have taken advantage of this and generally talked up a gloomy scenario. The fact that it's not quite as bad as anticipated almost makes it look as though reinsurance underwriters are a reasonable bunch.
2. **Salesmanship.** The P&I Clubs of the International Group have been educating ship owners for the past several years of the "inevitability" of increased reinsurance costs and have extricated themselves from any direct responsibility for this. The Clubs now treat RI as a separate "add-on" largely out of their control and which no longer features in the context of their primary negotiations with the ship owner. This has become "a little administrative matter" after all else is finalised.
3. **The product.** The Group's P&I excess loss reinsurance policy covers the tanker owner for most of the layers between \$30m and \$2.03bn for non-pollution claims and up to \$1bn for pollution claims. The fact is, it is unlikely that any individual tanker operator could replicate this cover elsewhere. And the top end is no longer some theoretical fantasy. Contingency planning and risk management evaluations routinely reach these mega figures. Tanker operators know they need this level of protection and it is not a luxury option.
4. **The future.** The liability environment is becoming more hostile. After a fairly calm post-OPA 90 decade, tanker pollution has once again entered public consciousness. Bulk carriers can sink on the high seas with tragic loss of lives, lost containers can float mid-ocean unobserved and ships can burn to the gunwales out of sight; but it is oil hitting the beach that makes the world headlines. The consequences of oil pollution are only going to get worse and ship operators need all the help they can get.

Yet, despite the seemingly easy acceptance of the increased reinsurance costs, these are not without significance. Last year we reported a 20% increase which was relatively

modest as this programme was still partly protected by a multi-year agreement. This year was the first “back to basics” renewal and there was some concern whether the structure would hold. One alternative was to raise the bottom layer of the excess loss programme from \$30m and likewise increase the Pool layer from \$5m to something between \$6-7.5m. However, the smaller premium clubs would be severely disadvantaged and these long standing (since 1995) break-points remained intact.

The new rates as directly applied to tanker owners and charterers are now as follows:
Excess Loss Reinsurance Costs (Rates: \$ per GT)

Type/year	2003	2002	2001	2000	1999	1994
Dirty Tankers	0.6723	0.4859	0.3953	0.3953	0.4373	1.4367
Clean Tankers	0.3324	0.2364	0.1773	0.1773	0.1970	0.5598
Chartered Tanker	0.1122	0.0749	0.0716	0.0650	0.1290	0.2400

Source: Clubs' 2003 Circulars and previous reports

For a VLCC carrying heavy oils, the excess loss reinsurance programme now accounts for about 30% - 40% of the total premium. Add another 25% for the pool layer and there is not much retained by the club to pay its own retention layer of \$5m. The fact is that both P&I and reinsurance rates dropped very quickly between 1994 and 2000 as a direct result of the improving tanker claims performance. This has now turned around but the reinsurance costs are increasing at a faster rate than the underlying P&I premium.

Despite recent highly publicised incidents, the overall record for tankers remains very good. The reinsurance rates are still far more realistic than 10 years ago and it is unlikely that they will return to that level. The *Prestige* total loss and subsequent coastal pollution might have been the impetus for onerous insurance increases. However, excess loss reinsurance underwriters seem to have recognised, to their credit, that this disaster had less to do with safe tanker operations and more to do with abysmal political interference.

There is another reason why tanker operators may have fared better than anticipated: for the first time in almost 15 years, the heat is temporarily off. P&I underwriters are presently more focused on passenger ships than on tankers. The Athens Protocol 2002 has given cruise liners and ferries their very own “OPA-90” (except the “P” stands for passengers). Reinsurance underwriters have officially recognised that a VLCC offers nowhere near the same high level risk exposure as a cruise liner and have structured their rates accordingly.

For the first time, probably since the inception of this programme, crude oil carriers are no longer the highest rated vessels. Passenger ships now pay \$0.6841/GT, an increase of 81% from the previous year. This may be small consolation for the industry as a whole but it is a welcome respite for tanker operators.

The International Group Reinsurance programme now looks as follows:

IGA Excess Loss Reinsurance 2003-2004

US\$ m	Up to US\$4.03bn (\$4.025m excess of \$5m)		Overspill
2030	Pool, including Overspill Calls, Free Reserves and ad hoc protections		
1530	500m		Top Layer
1030	500m		Third Excess
530	500m	500m (Separate Placing)	Second Excess
30	Excess Loss RI 500m (75%)	Pool Co-insurance (25%)	First Excess
20	Upper Pool		Pool
5	Lower Pool		
0	Club Retention		Club
	Ship Owner's Retention (Deductible)		Ship Owner

Source: Ensign Marine Consulting Ltd.

The main alteration from the previous year is the increased participation of the Pool in the First Excess layer. The individual clubs will all have varying degrees of ad hoc arrangements to protect their exposure within the various levels of pool and retained claims. The Overspill layer is not strictly a straight \$2bn excess but the approximate value of a figure calculated by charging 2.5% of the 1976 London Limitation Convention figure on all entered vessels of a Group Club. Oil pollution remains capped at \$1bn and is not part of this calculation.

USA oil pollution surcharges

Yet tanker operators still face an onerous regime of bureaucracy and costs from the insurance industry. The certification process is not getting easier or lighter; indeed other sectors of the marine industry are also being pushed into that direction. There is no respite in the short term and owners will continue to pay special insurance surcharges specific to certain trades.

The USA oil pollution surcharge, levied by reinsurance underwriters in response to OPA-90, has increased its rates by 40%. This is in line with the main programme. and comes

after a 20% increase last year. The cost is not inconsequential and the current rates are now the following:

USA Oil Pollution Surcharges

	2003/04		2002/03	
	SBT (Marpol)	Non-SBT	SBT (Marpol)	Non-SBT
Tankers > 1000 GT	\$0.126/GT per voyage	\$0.1428/GT per voyage	\$0.09/GT per voyage	\$0.102/GT per voyage
LOOP/Lightening	\$0.063/GT per voyage	\$0.0714/GT per voyage	\$0.045/GT per voyage	\$0.051/GT per voyage
Tanker ≤1000 GT	\$2,520 pa or \$126/voyage	\$2,856 pa or \$143/voyage	\$1,800 pa or \$90/voyage	\$2,040 pa or \$102/voyage
Parcel Tankers (≤5000 t. cargo)	\$7,560pa or \$378/voyage	\$8,560 pa or \$428/voyage	\$5,400 pa or \$270/voyage	\$6120 pa or \$306/voyage
Parcel Tankers (5001-10k t. cargo)	\$18,820 pa or \$941/voyage	\$21,500 pa or \$1,075/voy.	\$13500 pa or \$675/voyage	\$15300 pa or \$765/voyage
Parcel Tankers (≥10,000 t. cargo)	\$0.126/GT per voyage	\$0.1428/GT per voyage	Not specified	Not specified
Voyage Cap	20		20	

Source: Club Circulars 2003 and 2002.

Conclusion

On the positive side, the full P&I reinsurance structure has remained intact and tanker operators still retain a very high level of insurance protection, both for pollution and non-pollution claims. However, on the negative side, costs have increased substantially on all fronts and to the extent that voyage calculations need to be revised.

P&I underwriters, both primary (the clubs) and excess (the international market) have been generally gradualist in approach and have not destabilised the market. This implies that increases will continue into the near future.

However, there is already a view that the rate of increases will slow and indeed that the peak is already in sight. The 2004 round is already perceived to be likely more difficult for insurers.

Much will depend on developments elsewhere – such as CLC limits, the imposition of strict liabilities on operators and direct action against insurers – and the absence of high-profile pollution incidents.

In the meantime, tanker owners seem to have survived this round of P&I increases in reasonable shape.