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## Establishing a new protection and indemnity (P&I) insurance institution in Turkey

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**World Maritime University**  
Malmö, Sweden

**ESTABLISH A NEW PROTECTION AND  
INDEMNITY (P&I) INSURANCE INSTITUTION  
IN TURKEY**

By

**Muhammet Alper KECELI**  
**TURKEY**

A dissertation submitted to the World Maritime University in partial  
fulfilment of the requirements for the award of the degree of

**MASTER OF SCIENCE**

**in**

**MARITIME AFFAIRS**

**(MARITIME LAW AND POLICY)**

**2012**

## DECLARATION

I certify that all the material in this dissertation that is not my own work has been identified, and that no material is included for which a degree has been previously been conferred on me.

The contents of this dissertation reflect my own personal views, and are not necessarily endorsed by the University.



22.10.2012

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## **ABSTRACT**

Title of Dissertation: **Establishing a New Protection and Indemnity (P&I) Insurance Institution in Turkey**

Degree: **MSC**

Insurance draws attention as a sector that is understood much better in terms of its importance especially in recent years globally and in Turkey as well and this sector is developing each day. In direct proportion to the development of insurance, the importance of marine insurance forming a special part of insurance has also come to the surface.

Marine insurance, as a field has unique characteristics that can dominant from general insurance principles from certain angles, and stands before us as a dynamic field necessary to be reviewed and handled over and over again with the developments in the world.

In Turkey, there have been various studies related to some of the fields of marine insurance. In this dissertation, components of Protection and Indemnity Insurance will be dealt with comprehensively. Furthermore, problems and solution methods associated with club insurance practices are addressed.

**KEYWORDS:** Protection and Indemnity, P&I insurance, National P&I Clubs, IGPANDI, Liability, Third Party

(According to the English Law protection and indemnity insurance is called club insurance. This writer prefers to use it as Club insurance in the first two chapters and will continue with P&I insurance.)

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## **LIST OF ABBREVIATIONS**

<b>B.C.</b>	Before Christ
<b>CLC</b>	International Convention on Civil Liability for Oil Pollution Damage
<b>CPI</b>	China Protection and Indemnity Club
<b>D.W.T</b>	Dead Weight Tonnage
<b>EU</b>	European Union
<b>F.D&amp;D</b>	Freight, Demurrage and Defense
<b>GRT</b>	Gross Tonnage
<b>HM</b>	Hull and Machinery Insurance
<b>IDO</b>	Istanbul Sea Buses
<b>IG</b>	International Group Clubs
<b>IGPANDI</b>	International Group of Protection and Indemnity Clubs
<b>ILU</b>	The Institute of London Underwriters
<b>IOPC</b>	International Oil Pollution Compensation Convention Funds
<b>IUA</b>	The International Underwriting Association of London
<b>Korea P&amp;I</b>	Korea Protection and Indemnity Club
<b>MIA</b>	Marine Insurance Act 1906
<b>P&amp;I</b>	Protection and Indemnity
<b>TTK</b>	Turkish Commercial Code
<b>TUGS</b>	Turkish International Ship Registry

**UK**            The United Kingdom of Britain

**USA**            United States of America

## INTRODUCTION

Since the ancient times of history, both commercial carriage and passenger carriage have been realized mainly over seas. In other words, maritime transportation of people and goods, has historically fulfilled the communication function. Due to this characteristic, it is considered as being one of the fields that has significantly contributed to the development of world civilization. Similarly, the emergence of the insurance concept has also evolved in connection with maritime adventures. For that reason, the first insurance policy known from history was a marine insurance policy.

In the early part of the twentieth century, as the cargo carriage increased widely together with the development of ship building techniques and development of industrialization and mass production, the importance of marine insurance, which had been already practiced since the prehistoric period increased in direct proportion. Within the same period, petroleum started to be used as an energy source, which also brought environmental damages around the middle of the century and added a new dimension to marine liability insurances.

A marine adventure of a ship is a fact that is able to pose many risks. This may be the reason why it is called a 'marine adventure' in English and 'deniz sergüzeşti' in Turkish, due to its highly risky structure.

It really depends on the existence of the insurance that maritime voyages, which carry the characteristic of a full adventure, do not become adventures full of fears for the ship owners. While risks of marine adventure can destroy the ship owner commercially if the ship, which is a big asset on its own, is lost, damages to the cargoes on the ship and the losses likely to emerge from the liabilities against third parties can bring out bigger effects for the parties that are responsible for the damages than the ship. On the one hand, that is what the financial dimension is and it is another dimension to take into account that shipping can cause damages to all stakeholders. There is no doubt that all living creatures will be affected from the

consequences of the damages caused by ships likely to result especially from environmental disasters. As a result of all these, it can be concluded that the damages caused by ship accidents are important in terms of states, people and even all living creatures.

The above-mentioned features of the marine adventure make marine insurance simply obligatory for the parties whose interests are under risk. In addition, marine insurance is obligatory in terms of the contract parties in some international agreements and state regulations. Especially, it is seen that Protection and Indemnity (P&I) insurance is obligatory in various fields as it is liability insurance.

In Turkey, there is such an obligatory insurance application in obtaining the CLC-92 certificate regarding the 1992 Convention about the International Convention on Civil Liability for Oil Pollution Damage. Again, there are similar regulations for having an obligatory insurance application; however, case and contents of codes are different from the oil pollution responsibilities, in the relevant legislations for ships imported from abroad and the Turkish Environmental Act.

It is seen that the maritime sector in Turkey is in a development process in recent years. In previous years, some tax exemptions facilitating the transfer of ships to flying Turkish flag and clearing the way for construction of many ships by supporting the ship construction sector caused the Turkish merchant marine fleet to develop and grow in tonnage. However, it cannot be said that these developments have significant reflections on the field of marine insurance in Turkey.

Although there are some studies to ensure knowledge about Turkish marine insurance, it can never be said that a limited number of previous studies is enough for a sea country like Turkey. Especially, the lack of a study that examines the insurance by putting primary marine insurance together and comparing it with each other is really important.

In this dissertation, P&I insurance, which forms an important part of marine insurance, will be addressed comprehensively and there will be information regarding P&I insurance applications in Turkey. The Turkish Commercial Code will be frequently referred to as it has the characteristic of being the exclusive regulation in Turkey in terms of marine insurance. On the other hand, English law, the dominant application will be reviewed. While reviewing English law, the Marine Insurance Act will be the centre of attention, but club rules or P&I institution rules as well as institute clauses and club insurance determining the contract rules in cargo and hull insurances will also be analyzed. Expectations of the maritime sector actors related to the problems and recommendations will be explained while giving information about P&I insurance applications. The dissertation will be formed by five chapters.

In the first chapter, there will be information related to the historical development of marine insurance and the Marine Insurance Act 1906. Under the topic of Marine Insurance Act, a general overview, sources, factors, types of marine insurance and characteristics of marine insurance contracts will be explained.

The second chapter will be the chapter where P&I insurance will be analyzed. After the historical background and legal features of club insurances are reviewed, parties in the club insurance, club structure, scope of guarantee coverage, International Group (IG) and debts of the parties towards each other will be addressed.

The third chapter is about advocating the establishment of a national P&I institution. This chapter puts forward the following premise in support of the establishment of a national P&I institution; P&I insurance is one of the most important services to national shipping, and therefore, such services should be provided within the nation. It will establish data records about marine incidents, and collect information from investigations, which is helpful for making risk analyzes. On the other hand, most of the countries have enough capability to service hull and

machinery insurance. If both insurances were supported or served from the same sources, claims would be handled proficiently and assessments of compensations could be performed very quickly.

The fourth chapter will analyze the benefits and criticisms of the national P&I applications. Being a participant of a club membership is creating some extra cost for the shipowners, such as having to share some huge risks coming from the other memberships' property. Not only small risks have to be taken, but also the responsibility for all the other members' risks because of being part of a mutual insurance system. In a national P&I model, if reinsurance arrangements are made on a package basis of one national fleet, rate levels will be quite competitive. A national insurer will find greater ease in obtaining a better spread of risks and more reasonable terms and conditions of insurance, particularly in respect of premium and terms of payments. On the minus side, for an ideal spread of risks a stable management, the size and number of vessels are among the most important factors. National portfolios are not large or diverse enough to provide a proper spread to enable P&I to operate effectively. Eventually, the cost of localised P&I cover may go up. There are some necessities for managing all claims, like access to an international network of correspondents and lawyers. There is a good example for understanding how they arrange to find success in Korea and other countries. The Korean P&I institution is one unique example of how it is possible to manage a national P&I insurance.

In the last chapter, club insurance applications in Turkey will be reviewed. How club insurance is regulated in the country, where it is obligatory, problems related to the insurance and how the sector sees the insurance will be discussed.

In the conclusion section, besides the general assessments related to the dissertation, there will be solution suggestions and measures regarding the problems identified in the dissertation.



## CHAPTER 1

### 1 Historical Development of Marine Insurance and Marine Insurance General Overview

#### 1.1 Historical Development of Marine Insurance

##### 1.1.1 Marine Insurance in Europe

When considering the historical development of insurance, the earliest applications similar to insurance in the world are seen to have come up in Babel in B.C. 2000. This primitive insurance in which capital owners undertook a risk of their caravans getting robbed for a certain fee were legislated later by the king of that era, Hammurabi. With the help of the act, it was made obligatory to share the losses of the caravans which encountered attacks, between all caravan owners. This is accepted to be a first in land based insurance.<sup>1</sup>

When considering the beginning of marine insurance, it is seen that<sup>2</sup> the Rhodes Rules<sup>3</sup> are accepted to be the foundation of modern general average<sup>4</sup> as applied in Roman Law in the ninth century before Christ. Again, it is known that Phoenician Maritime Law regulating general average and marine insurance in general emerged in the seventh century before Christ. There is information that maritime loans had begun to be applied in Roman Law in the third century before Christ.<sup>5</sup> A maritime loan contract was a contract where the payment of the debt and the interest determining the loan amount of the borrower, called bottomry, depended on the condition that the ship arrived safely to the port of destination.

The first applications similar to today's insurance were marine insurance. The

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<sup>1</sup> Soyer, B., (2001), *Warranties In Marine Insurance*, London: Cavendish Publish Ltd., p. 8, 9

<sup>2</sup> Zimmermann R., (1990), *The Law of Obligations, Roman Foundations of the Civilian Tradition*, , Oxford Pub., p.11

<sup>3</sup> Lex Rhodia de iactu

<sup>4</sup> Damage to the ship or load in maritime trade

<sup>5</sup> Koschaker, P., (1977), *Introduction to Roman Private Law*, Ankara University Publications, p. 30

reason for this is seen to emerge from its natural characteristic, as the maritime trade carries a high risk. A marine insurance contract aiming to cover possible damages in return for a certain premium is encountered in the beginning of 13th century in Italy.<sup>6</sup>

At the beginning, insurance contracts were certified through notaries. However, this method was normally not suitable for the commercial life and gave place to the method of issuing a policy.

The word policy was used for the first time during that era as "polizza" in Italian meaning promising, entering into obligation.<sup>7</sup> In parallel with this information, researchers show that the first known insurance policy was issued for a ship named "Santa Carla" sailing from Genoa, Italy to Mallorca on October 23, 1347.<sup>8</sup> In 1370, reinsurance of a marine insurance policy was issued for the first time for a ship going from Genoa to Brugges.<sup>9</sup> However, issuing and delivering of the marine insurance policies commonly started as of the 15th century. In this sense, the first insurance company was founded in Genoa in 1424. Marine insurance spread to Spain, France, Portugal, the Netherlands, England and North Germany after that era.

Apart from these, various legislations were enacted, which set down determined rules regarding marine insurance in Europe in the 14th and 15th centuries. These can be listed as ;

Barcelona Charter (1434-5), Philippe De Bourgogne Charter (1458), Genoa Charter (1498), Florence Charter (1522), Burgos Charter (1537), Seville Charter (1553), Bilbao Charter (1560), Amsterdam Charter (1598), Flandres Charter (1537).<sup>10</sup>

Within the same periods, malicious behaviors of the insured led the insurers to come together and form associations. In this regard, the first insurance association

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<sup>6</sup> Soyer. Supra. P.9

<sup>7</sup> Soyer. Supra. p.9

<sup>8</sup> Bennet, H.,( 2006),*The Law of Marine Insurance*, second edition, Oxford University Press, p. 1.02

<sup>9</sup> Soyer, B., Supra. P.9

<sup>10</sup> Ibid. p. 9

fulfilling functions such as determining the conditions and premiums of the insurance policies, rescuing ships which had grounded or in danger was founded in Florence in 1552.<sup>11</sup>

Marine Insurance had been conducted by private individuals until the 17th century and as these private individuals from time to time, had difficulty in paying the claims liabilities from time to time, insurance companies began to be founded and spread as of the 17th century. In this context, lots of insurance companies have been founded through charters of the kings in many countries in Europe and these insurance companies were granted the privilege to enter into a contract.<sup>12</sup>

### 1.1.2 Marine Insurance in England

Insurance was brought to England by Lombardian (Italy) merchants banished by the German King Freidrich II in the 14th century and then settled in London. It can be said that the first insurance applications in England were carried out by Italians.<sup>13</sup> The Lombards possessed the marine insurance market during the period they resided in London. At the beginning of the 16th century, when they left London, it can be said that marine insurance applications had already become established in London.<sup>14</sup>

After the Lombards, the foundations of Lloyd's market, one of the most important exchange markets of the world's insurance sector, were laid in the 17th century by a person named Edward Lloyd through his coffeehouse located in Tower Street in London gaining reputation in terms of marine insurance.

This coffeehouse was known as a place where ship owners, seafarers and merchants engaged in overseas trade came together. Customers used to come to this coffeehouse to execute their work related to insurance. This coffeehouse, where insurance conditions and tenders were passing around, was the most suitable place in

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<sup>11</sup> *ibid* p. 10

<sup>12</sup> *ibid*. p. 11

<sup>13</sup> *ibid*. P.12

<sup>14</sup> Tetley, W., (2002), *International Maritime and Admiralty Law*, Canada: Covansville,

London to underwrite an insurance for any kind of marine risk.<sup>15</sup>

In 1691, Edward Lloyd transferred his coffeehouse to Lombard Street and thus extended his business. He was reaching lots of information through his connections in different ports and sharing this information with the relevant persons coming to the coffeehouse. He began to publish 'Lloyd's News' three times a week in 1692 in order to announce this useful information to a broader audience. This newspaper was later forbidden due to its political content. However, the tradition of sharing information via newspaper continued with the newspaper named 'Lloyd's List and Steamship Newspaper' after Lloyd's death.<sup>16</sup>

Although, two insurance companies were granted the privilege to enter into an insurance contract through the charter of the King of England in 1720, this case did not affect the Lloyd's market significantly. Insurers and brokers conducting insurance activities at Lloyd's coffeehouse established a community named Lloyd's after the death of Edward Lloyd (1769). After five years, this community was transferred to the Royal Exchange and in 1871 it became an association by an act legislated by English Parliament. In 1779, the first standard marine insurance policy, the "Ship & Goods Form" was issued. This policy was in use until the Lloyds Marine Policy Form took its place in 1982.<sup>17</sup>

An insurance association known as the 'Institute of London Underwriters' was founded by marine insurance companies in 1884. The primary role of the association was to prepare insurance conditions applied by marine insurers. Another association founded in England was the 'Salvage Association' which was established in 1856.<sup>18</sup> The International Underwriting Association of London (IUA) is the world's largest representative organisation for international and wholesale insurance and reinsurance companies. The IUA was formed on 31 December 1998, through the merger of the

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<sup>15</sup> ICS, (2012), Marine Insurance, ICS Press, p.3

<sup>16</sup> Ibid. P.4

<sup>17</sup> Tetley, Supra.

<sup>18</sup> ICS. Supra. p.11

Institute of London Underwriters (ILU) and the London International Insurance and Reinsurance Market Association (LIRMA).

In England, in the beginning, certain provisions of *Lex Mercatoria* originating from Roman Law applied by all European merchants related to marine insurance, were applied. In 1601, the first written law was brought into force in England to regulate marine insurances. Important provisions of *Lex Mercatoria* were included in English Common Law. In 1906, the Marine Insurance Act was enacted to regulate marine insurance completely and is still in place today.<sup>19</sup>

Legislation related to Lloyd's was made through an act in 1911. Today, Lloyd's is not an insurance company but actually a leading 'insurance market' holding insurers and intermediates within its structure.

### 1.1.3 Marine Insurance in Turkey

The first time insurance emerged in Turkey was, much later compared to the western Europe due social, economical, regional and political reasons. Especially in the Ottoman period, they stayed out of insurance for many years and insurance was only able to develop after the Imperial Edict of Reorganization in 1839.<sup>20</sup>

In 1870, after the big fire in Beyoğlu, three English insurance companies began to work in Turkey. After this development, foreign insurance companies began to establish their agencies in the country. However, there was not any legislation to regulate the practices of these insurance companies for a long time. The first domestic insurance company was established in 1925. This company is Anadolu Anonim Türk Sigorta Şirketi (Anatolian Anonymous Turkish Insurance Company) founded jointly by Türkiye Cumhuriyeti Ziraat Bank and Türkiye İş Bank.<sup>21</sup> This was followed by the establishment of Milli Reasürans T.A.Ş. the first domestic reinsurance company in 1929.

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<sup>19</sup> Tetley, Supra. p.

<sup>20</sup> Nomer C.,&Yunak H.,( 2000) *Sigortacılığın Genel Prensipleri*, İstanbul, p.5

<sup>21</sup> Helmis J., (1963). *Deniz Sigortaları*, Ülkü Basımevi, İstanbul, p.6

In Turkey, surrounded by sea on three sides, although development of maritime business is adopted as a government policy, unfortunately it has not been able to reach the desired levels. Likewise, the insurance sector is a newly developing sector having an increasing share in financial markets recently. As a result of these components, it cannot be said that marine insurance is developing as it is in the west. Still, Turkey provides most parts of marine insurance from overseas insurance markets.

## 1.2 Marine Insurance General Overview

### 1.2.1 Definition

Insurance contracts are divided into two main areas, land and marine insurances, depending on the risk. The insurances taken against the marine risks will be examined in this dissertation. Marine insurance is defined as "One who has a benefit measurable with a price in salvage of the ship or the keep safe of cargo from marine risks can have insurance on this benefit " in article 1339 of the Turkish Commercial Code. The English Marine Insurance Act 1906 (MIA 1906) on the other hand, defined marine insurance as "A contract of marine insurance is a contract whereby the insurer undertakes to indemnify the assured, in manner and to the extent thereby agreed, against marine losses, that is to say, the losses incident to marine adventure "in section 1 entitled 'description of marine insurance". It is understood from the definitions that two main factors are necessary to sign a marine insurance contract. These factors are benefit and risk factors.<sup>22</sup>

### 1.2.2 Sources of Turkish Marine Insurance Law

The body of rules being in the forefront in terms of marine insurance law in Turkey is the fourth chapter of V. Book of the Turkish Commercial Code (TTK). The chapter entitled "Insurances Against Marine Risks" is covered from article 1339 to 1459 of the Turkish Commercial Code.

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<sup>22</sup> Kender, R., &Çetingil, E., (2003) Deniz Ticaret Hukuku, Arıkan Yay. İstanbul, p. 129

In the Insurance Act no. 5684, special provisions related to marine insurance have not been included. The rules valid for land insurances are also valid for marine insurance.

Another important source for the marine insurance is general conditions. Conditions prepared by the Undersecretariat of Treasury in order to be utilized in the contract having the characteristics of 'general transaction terms' regulating the subject of the insurance, insurance coverage, cases out of the coverage and rights and obligations of the parties are named general conditions of the insurance. In the field of marine insurance, there are two general conditions, namely 'Cargo Transportation Insurance General Conditions' and 'Ship Policy General Conditions', which are still in effect.

The last paragraph of article 1266 of the Commercial Code states; “Apart from the issues written in the first paragraph, insurance policy contains insurance extended conditions confirmed by the Ministry of Economics and Trade and printed in a way to be read easily; on the other hand a provisional policy contains a reference to aforesaid extended conditions. In case the conditions contained in the confirmation and edition in that paragraph are not fulfilled, the ones that are to the policy owner's disadvantage among the extended contract conditions, act of law are applied.”

Again in article 1264 of the Turkish Commercial Code, it is stated that the above mentioned provision cannot be amended as it would be disadvantageous for the policy owner and in case the provision is amended, acts of law will be applied *ex officio*.

The fact that the insurance contracts should be signed in compliance with the general conditions is expressed more clearly in article 11 of the Insurance Act no. 5684, effectuated on 14 June 2007 and entitled 'Insurance Contracts' as "The main content of the insurance contracts is regulated in accordance with the general conditions to be applied by insurance companies and approved by the Undersecretariat. However, special conditions can be utilized according to the characteristics of the work in the

insurance contract. These issues are stated explicitly in a way not to lead to any mistake in the insurance contract and under special conditions title”, and the contracts signed in contradiction with this provision will be penalized by an administrative fine as stated in clause (f) of article 34 of the same Act entitled 'Administrative Penalty', that is "In case the regulation of general conditions is violated in contradiction to the first paragraph of article 11, then one thousand Turkish liras...".

It is understood from this provision of the Act that signing an insurance contract in contradiction with the general conditions will be penalized with an administrative fine. However, it is also accepted in the doctrine that regulating the insurance contract in contradiction to the general conditions has no effect on the validity of the contract.<sup>23</sup> In other words, contrary to any general condition provision, it is possible to conclude an agreement and such contract is valid. Yet, the limits of freedom of contracts in terms of insurance contract are determined by mandatory general provisions or Turkish Commercial Code provisions, which are mandatory in favor of the policy owner.<sup>24</sup>

As explained above, both cargo insurance contracts and hull insurance contracts are to be signed in accordance with the relevant general conditions. However, it should be stated that the validity of the contract will not be affected by violating the general conditions. The responsibilities of the insurer issuing a policy contrary to the general conditions for adapting the Turkish Commercial Code and Insurance Act are covered.

In today's marine insurance market, as a country marketing insurance to many countries in the world, marine insurance legislation of the UK has a wider field of application. It is not different in Turkey that meets the majority of the needs for marine insurance from England. In this sense, another source for the contract of cargo and hull insurance application is the clauses prepared by IUA in compliance with the Marine

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<sup>23</sup> Kender, R.,( 2008), Türkiye'de Hususi Sigorta Hukuku, Arıkan, p.43

<sup>24</sup> Ibid. P.43



Insurance Act 1906. These clauses are included in the insurance policy and constitute the context of the insurance contract.<sup>25</sup>

### 1.2.3 Types of Marine Insurance

Insurance contracts are differentiated according to the criterion of meeting the needs in the doctrine. In this analysis, insurance contracts are classified as loss insurance and amount insurance. Loss insurance is mentioned when the risks that insurance holders encounter are realized and the damage they suffer are covered concretely. If loss insurance is related with disappearance of the possibility of decreasing or increasing of the active asset, 'active loss insurance' is mentioned and if it is related with emerging or increasing of the liabilities in assets, 'passive loss insurance' is mentioned.<sup>26</sup>

It is possible to consider marine insurance within the scope of loss insurance. Marine insurance is grouped in various ways in the doctrine. According to an opinion, marine insurance is divided into three, namely hull insurance, freight insurance and liability insurance.<sup>27</sup> In this group, they are divided as follows;

Hull insurance; Freight and Loss of Hire Insurance, Ship Construction Insurance, Hull insurance and Yacht Insurance,

Cargo insurance; goods and value insurance,

Liability insurance; contractual liability insurance and third party liability insurance.<sup>28</sup>

In another classification made in terms of marine insurance, it is possible to divide marine insurance into two groups, namely property insurance and public liability insurance.

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<sup>25</sup> Kender, R., &Çetingil, E., Supra. p.130

<sup>26</sup> Algantürk, D., (2006), Protection and Indemnity Insurance , 2<sup>nd</sup> edition, Arıkan, p.85

<sup>27</sup> Turner, H., The Principles of Marine Insurance, 1986, 7th edition, Stone&Cox Limited, p.65

<sup>28</sup> ICS, Supra, p.67

### 1.2.3.1 Property Insurance

Insurance is taken out against reduction in assets of the insured as a result of damage to the insured goods of an insurable interest. The insurable interest owners in these insurances are mostly property owners.

Insurance types considered among the property insurance within marine insurance are:

- 1- Freight Insurance
- 2- Hull and Machinery Insurance
- 3- Profit Insurance
- 4- Cargo Insurance

### 1.2.3.2 Liability Insurance

This insurance type is defined in the MIA as ‘Any liability to a third party may be incurred by the owner of, or other person interested in or responsible for, insurable property, by reason of maritime perils.’. It protects against the possible losses to both properties and health of the third parties that are damaged because of the incident caused.<sup>29</sup>

Insurance types to be accepted as public liability insurance in marine insurance can be listed as:

- 1- Collision Liability Insurance
- 2- Protection and Indemnity Insurance
- 3- Other Liability Insurances.

The subject of this study will be Protection and Indemnity Insurances known as Club Insurance.

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<sup>29</sup> Algantürk D., Supra. p. 23

## CHAPTER 2

### 2 P&I Insurance

#### 2.1 General

This marine liability insurance type, also known as “Protection and Indemnity Insurance” or “Club Insurance” will be referred to as P&I Insurance in the following parts of the study as commonly used in the discipline. P&I insurance was among liability insurance in the part of Chapter 1 related to marine insurance.

Liability insurance is an insurance type that protects against financial losses of the policy owner due to the damages to both property and health of the third parties that are damaged because of the incident caused by the insured.<sup>30</sup>

When considering marine insurance, the first thing that comes to mind is warranty, yet P&I insurance was addressed in the previous chapter as it is involved in liability insurance and emerged later than other types of marine insurance. As a key element for the study, P&I insurance will be discussed in this part.

##### 2.1.1 Definition

As there is not any P&I insurance practice in Turkey yet, a definition can not be found in its legislation. However, it is known that P&I insurance can be concluded as a liability insurance as per Article 1339 of the Turkish Commercial Code, “Any person who has an interest measurable by money in experiencing maritime risks of the ship or cargo safely may insure this interest.”

On the other hand, there are not any definitions for P&I insurance in the MIA. Indeed, when the wider scope of guarantee is considered, it can be clearly understood how difficult it is to define P&I insurance.

In doctrine, Algantürk (2006) defines P&I insurance as; An exceptional

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<sup>30</sup> Algantürk, D., Supra. p.23

insurance type that member ship owner insures expenses and liabilities against third parties are not involved in hull insurance coverage in accordance with mutual insurance principles. Further, Acar (2008) defines P&I insurance as, An insurance related to liabilities against third parties due to being the owner of the ship or operating the ship and some expenses necessary to be obliged to make.

### 2.1.2 Historical Development

It is seen that the first P&I clubs emerged in England when protection indemnity clubs are viewed. After all, the most developed country in the world in this field is England.

After the "Bubble Act" dated 1720 known as cartel law in which authority to conduct insurance activities was given to two companies. The insurance sector was not somehow balanced, ship owners were bound to two companies having authority to conclude insurance. The insurance was expensive for the ship owners to purchase and, furthermore, not providing sufficient protection. This led ship owners to search for new initiatives. As a result of these searches, hull clubs were established as a solution. This structure, not seeking for any profits, was a good alternative for the cartels of this era. The Cartel Law did not affect the Lloyds sector, in which private persons concluded insurance.

When the Bubble Act in question was abolished in 1824, big companies started to enter into the insurance sector and the competition with Lloyd's insurers heated up .

Economic challenges in England in the 19th century led people to emigrate to the United States and Australia. This emigration, which increased significantly in the last quarter of the 19th century was particularly realized by lots of people travelling with poor vessels. Naturally, the number of ships and seafarers increased in that period. Within the same period (1846), the Fatal Accidents Act also known as the

Lord Campbell Act came into force.<sup>31</sup> With this act, compensation rights were granted for physical damages, including the ones who were destitute for dead. After this act came into force when passenger transportation was dense, many passengers and crew experiencing physical damages put the shipowners in a tight spot as they claimed. Another issue challenging ship owners was that all of the collision damages were not paid by hull insurance coverage.<sup>32</sup>

The aforementioned necessities formed a basis to put a structure similar to hull clubs, which had emerged before, into practice and the "Ship owners' Mutual Protection Society", the first protection P&I was established in 1854 as a sequence to the Britannia Club, which was a hull club before.<sup>33</sup> This P&I was operating under the name of "The Britannia Steamship Insurance Association".<sup>34</sup>

Towards the end of the 19th century, increasing compensation claims regarding cargo resulted in adding indemnity assurances among the protection P&I assurances at this time. With this development, clubs started to turn to P&I clubs and began to provide both protection and indemnity assurance for the ship owners.<sup>35</sup>

As the Hague Rules were accepted in 1924, P&I took 'defense coverage' into the scope of P&I insurance.<sup>36</sup>

Increasing liability risks and growing demands led P&I clubs to face capacity problems. P&I clubs desiring to overcome these capacity problems through reinsurance signed the first pool contract aiming to share indemnity payments over

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<sup>31</sup> Dover, V., (1975) *A Handbook to Marine Insurance*, London: Witherby, p.509

<sup>32</sup> Hazelwood, J.S., (2010). *P&I Clubs Law and Practice*, 4<sup>th</sup> edition, London: Lloyd's List, p. 7

<sup>33</sup> Ibid. P.6

<sup>34</sup> Algantürk, D., Supra. p.7

<sup>35</sup> Arnould, T., (1981). *Law of Marine Insurance and Average*, 16<sup>th</sup> ed., London: Stevens&Sons, p.128

<sup>36</sup> Algantürk, D., Supra. p.9

a certain amount between six clubs in 1899.<sup>37</sup>

P&I insurance in other countries developed very much later than it did in England. There is currently not any P&I club in Turkey. The P&I insurance need in Turkey is met from abroad, especially from England.

## 2.2 Legal Quality of P&I Insurance

### 2.2.1 Mutual Insurance

Mutual insurance is an insurance type in which the insured come together and secure themselves against certain risks. According to Article 1263 of the Turkish Commercial Code; "Mutual insurance is a contract under which the insurer undertakes to give indemnity against a premium in case of occurrence of a danger (risk) prejudicing a person's benefit which may be measured by money or to pay money or perform other actions due to life period of one or more persons or certain events occurred in their life". According to the first paragraph of Article 3 entitled "Establishment of insurance companies and reinsurance companies" of Insurance Law no. 5684; "Insurance companies and reinsurance companies which are going to operate in Turkey have to be established as a joint stock or a cooperative. Insurance companies and reinsurance companies shall not be engaged in other businesses except insurance transactions and business which are directly related to insurance operations."

Ship owners come together to secure their interest within the scope of club insurance in P&I insurance. This way, each one of the ship owners composing the Club obtains a member title and deposits a certain amount of 'premium' to indemnify potential damages. Premiums collected at the beginning of the policy year are directed to investment. On the other hand, at the end of the policy year, all loss cases are closed with the collected fund. If the money collected in the P&I fund is not

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<sup>37</sup> Anderson P., et al., (2010). Marine Insurance: Module Three- P&I Clubs and Mutual Insurance, Lloyds Maritime Academy, p.19

enough for paying the losses, then the members are asked for additional premium. As the P&I club does not seek profit, additional premium is only collected for such a case. Again, according to the case, if the premium is not exhausted despite paying for all losses, the P&I club can take it as reserves or distribute among the members.<sup>38</sup>

There are also fixed premium insurers providing assurance given within the scope of P&I insurance. However, primarily mutual P&I clubs will be addressed in the study and fixed premium insurers will be explained briefly.

### 2.2.2 Financial Liability Insurance

A member ship owner secures decrease likely to occur in his/her passive assets due to the claims given to third parties. For that reason, a P&I insurance is a type of a financial liability insurance.

In order for the P&I club to make payment to the member, the member should have made payment to the damaged first.<sup>39</sup> This rule is called the "pay to be paid rule". As a result of this rule, the payment liability of the P&I club to the member is equal to the money that has gone out of the pocket of the member.

### 2.2.3 Damage Insurance

When the risks of the insured are realized and the damage is indemnified concretely, damage insurance is mentioned. If damage insurance is related to diminishing of the asset or disappearance of increasing opportunity, 'active damage insurance' is mentioned; if it is related to emerging or increasing of passive assets, 'passive damage insurance' is mentioned.<sup>40</sup>

In P&I insurance, P&I secures legal debts to emerge in the assets of the ship owner. This damage to emerge in the assets occurs when a third party is damaged.

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<sup>38</sup> Acar, S., (2008), Protection and Indemnity, Vedat Kitap, p.235

<sup>39</sup> Ibid. p.248

<sup>40</sup> Ibid.338-342

Expenses that the P&I club undertake through this insurance are the amount the assets of the insured shipowners lose in value due to the damages of the third party.

#### 2.2.4 Passive Insurance

From the definition above, it is a passive insurance as it secures damages related to the emergence of passive assets in P&I insurance, which is a damage insurance or increasing of passive assets.

As a result, P&I insurance is passive insurance, like all passive insurances, the 'insurance price' is not determined, because the damage for the third parties is unknown in advance and it is not possible to detect it beforehand.<sup>41</sup>

#### 2.2.5 Voluntary Insurance

It is determined whether an insurance is voluntary or obligatory according to whether there is an obligation to conclude that insurance or not.<sup>42</sup>

P&I insurance is an insurance in which the member is not obliged to sign a contract as per a provision of law. In principle, it is an insurance that the member concludes to protect his/her own assets and thus it is a voluntary insurance.<sup>43</sup>

Besides, it can be necessary to have P&I insurance for the ship passing through certain regions as per the legislation of that region. However, this case does not eliminate the voluntary quality of the P&I insurance.

### 2.3 Structure of the P&I Club

#### 2.3.1 The P&I Insurer

The structure where the ship owners come together with the purpose of securing the part of maritime risks that is not indemnified with other marine

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<sup>41</sup> Hazelwood, J., *supra*. p.104

<sup>42</sup> Algantürk, D., *Supra*. p.86

<sup>43</sup> *Ibid.* p.86



insurances and which is based on mutual insurance understanding is called 'P&I club'.

As the P&I members are not company shareholders, they do not have rights or roles to make capital commitment or participate in profits. The relationship among the P&I members and the rights and obligations of the members are determined in Articles of Association and the Rule Book. P&I members deposit a certain amount of premium to the P&I club as per the Articles of Association and participates in the damages that other members encounter.<sup>44</sup>

#### 2.3.1.1 General Assembly

The superior body of a P&I club is the general assembly. All of the P&I members are authorized to attend a general assembly meeting and each member has a right to vote. A general assembly meets in two ways, as ordinary or an extraordinary assembly as in company law. The general assembly is conducted once a year. For the issues that must be handled immediately, general assembly can be called for an extraordinary meeting.<sup>45</sup>

Powers of a general assembly include:

- annual report and deciding on accepting the accounts,
- election of board of directors,
- election of inspectors,
- amendment in P&I rules,
- deciding on dividing the P&I club or merging it with another P&I club,
- amendment in the articles of association,

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<sup>44</sup> Hazelwood, J., Supra. p.64

<sup>45</sup> Acar, S., 2008, Supra. p.48

- determining wages the members of the board of directors.<sup>46</sup>

#### 2.3.1.2 Board of Directors

The Board of Directors is responsible for conducting the ordinary operations of the P&I club and developing them in every respect. The Board of Directors is authorized to incur every kind of expense when conducting the operations in question.<sup>47</sup>

The number of members of the board directors cannot be below 10 and over 35.<sup>48</sup> A person to be assigned to the board of directors should be younger than 70 years old.<sup>49</sup>

Members of the board of directors are elected for three years by the general assembly and have the opportunity to be re-elected. The board of directors meets regularly, yet they can meet for extraordinary sessions if necessary.

The principal tasks of the board of directors are;

- Accepting indemnity claims in to amounts approval to be within lower amounts left for the authority of board of directors,
- settling disputes between a member and the P&I club,
- determining the premium amount and collection time,
- organizing the processes regarding reinsurance,
- managing the assets of the P&I club,
- conducting the administrative affairs within the P&I club,

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<sup>46</sup> Hazelwood, J.S., Supra. P.10

<sup>47</sup> UK P&I Rules, No:15 A

<sup>48</sup> UK P&I Rules, No:13

<sup>49</sup> UK P&I Rules, No:14 A

- deciding on opening and closing the policy year
- preparing the amendments in the P&I rules.<sup>50</sup>

#### 2.3.1.3 Managers

Due to the need for professionalism in management of the clubs, managers have been assigned to these roles from outside with the service procurement method. Management needs of the P&I clubs are met by associations. A P&I club can appoint a company, an association or administrative staff as P&I manager.<sup>51</sup>

The primary duty of the managers is to take executive actions in line with the policies of the board of directors. In this sense, the managers are responsible for:

- carrying out the decisions of the board of directors,
- collecting the premiums,
- appointing correspondents,
- fulfilling indemnity claims,
- preparing a report to submit to the board of directors and
- ensuring the continuation of the investments.<sup>52</sup>

#### 2.3.1.4 Correspondents

It is very important for the P&I clubs to be at the side of its members anywhere required. In this sense, P&I clubs perform their activities for a fast and efficient service all around the world through their correspondents. The task of the correspondents is a kind of counseling. Correspondents are neither agents nor

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<sup>50</sup> Hazelwood, J.S., Supra. P.11

<sup>51</sup> Ibid. p.21

<sup>52</sup> Ibid. p.26

representatives of the member or the P&I club.<sup>53</sup>

P&I correspondents make efforts to take necessary actions immediately when a damage occurs or to shed light on the cause causing the damage.<sup>54</sup> Apart from that, another task of the correspondents is to inform the P&I club about the developments in the country they live.

There are about 1000 correspondents working for P&I clubs all around the world today.<sup>55</sup>

### 2.3.2 Members

In the P&I insurance contract, the shipowners secure their liabilities and expenses against third parties, which are unusual by the hull insurance policy of their ships, in return for the premium paid is called member.<sup>56</sup> Membership is a concept related to mutual P&I clubs and in fixed premium P&I insurances the insured and insurer are mentioned.

Although the member is defined to be the ship owner here, it is necessary to understand the concept of ship owner broadly as insurable interest. The definition of insurable interest is made in MIA as: Subject to the provisions of this Act, every person has an insurable interest who is interested in a marine adventure. In particular a person is interested in a marine adventure where he stands in any legal or equitable relation to the adventure or to any insurable property at risk therein, in consequence of which he may benefit by the safety or due arrival of insurable property, or may be prejudiced by its loss, or by damage thereto, or by the detention thereof, or may incur liability in respect thereof.

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<sup>53</sup> Ibid. p.15

<sup>54</sup> Ibid. p.16

<sup>55</sup> Acar, S.,supra. p.54

<sup>56</sup> Algantürk, D.,Supra. p.34

In other words, it is accepted that ship owners in case of association, ship share holder, charterer, ship operator or manager, mortgage holder are included in the concept of having an insurable interest shipowner.<sup>57</sup>

Joint owners (association of ship owners);

In case there is more than one consecutive or joint owners of the ship in the application for membership in the P&I clubs, this is called joint owners or association of ship owners.<sup>58</sup> In this case, P&I membership is issued for names or titles for more than one person. However, tasks and rights in terms of the P&I clubs are considered to be one. Some of these persons will be explained below briefly.

Ship shareholder;

In English law, the ship is considered to comprise 64 shares. Ship owners have property rights in proportion to their shares in the ship. For that reason, each ship share holder has the right to insure the ship.<sup>59</sup>

Loss Payee;

According to Article 14/I of MIA: Where the subject-matter insured is mortgaged, the mortgagor has an insurable interest in the full value thereof, and the mortgagee has an insurable interest in respect of any sum due or to become due under the mortgage.” In this sense, a loss payee holder can insure his/her ship as insurable interest owner.<sup>60</sup>

Charterer;

In a bareboat/demise charter, as the management of the ship belongs to the charterer, the charterer is not much different from the ship owner in terms of

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<sup>57</sup> Hazelwood S.J., *Supra* p. 65

<sup>58</sup> UK P&I Rules, No:10

<sup>59</sup> Alganturk, D., *supra*. P. 36

<sup>60</sup> Hazelwood, J.S., *supra* p.74

financial liability. In parallel, a charterer is not different from the ship owner in terms of insurable interest and entering the P&I club.<sup>61</sup>

## 2.4 P&I Insurance Coverage

### 2.4.1 General

When P&I insurance is mentioned, a comprehensive coverage comes to mind. P&I clubs are divided into classes providing insurance coverage with different characteristics. The primary coverages provided by the P&Is are collected under the classes of:

- protection
- indemnity
- freight, Demurrage and Defence
- strike
- war.<sup>62</sup>

A member is not obliged to participate in all classes. The number of effective classes determines the premium payable.

### 2.4.2 Guarantee Period

P&I insurance cover starts at noon on February 20 under normal circumstances and ends at noon on February 20 the next year. The reason why the insurance starts on February 20 is that the ice in the Baltic Sea is thawed on that day and in the past ship owners, began to renew their commands on that date.<sup>63</sup>

Together with this rule, ships registered in a P&I club can be insured for more

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<sup>61</sup> Williams, R., (2008) *Gard Guidance to the Statutes and Rules*, Gard AS, p. 467

<sup>62</sup> *Ibid.* p.70-77

<sup>63</sup> Merkin, R., et al., (2008). *'Marine Insurance' in Southampton on Shipping Law*, Informa, p. 341

than one insurance year. Again, it can also be agreed that the insurance should continue for a certain period of time.<sup>64</sup>

Notifications regarding the continuation or the termination of the membership and insurance conditions of the P&I club should be done before January 20. If there is a notification related to increasing the premium by the P&I, this should be done before December 20, otherwise the policy should be renewed at the rates of the previous year.<sup>65</sup>

### 2.4.3 Risks within the Coverage

#### 2.4.3.1 Protection and Indemnity Cover

##### 2.4.3.1.1 Protection Cover

a) Liability to indemnify damages or compensation for personal injury, illness or death of seamen or any other person, and hospital, medical or funeral expenses incurred in relation to such injury, illness or death.

Losses and expenses emerging from injury, illness or death of the crew, passengers or other persons due to the faulty shipping or management of the ship registered under the P&I club, or negligence in, taking the necessary measures on the ship are within the P&I insurance coverage.<sup>66</sup> Within the scope of this insurance, the persons mentioned as other persons are any persons related to the ship or cargo other than the crew. These are dock workers, guides, substitute crew, surveyors, salvors at sea, refugees and stowaways. Liability regarding these people is based on fault in general. Treatment of the injured persons, funeral expenses and carriage charges are within the scope of the insurance. Liability of the ship owner against the crew resulting from the contract or law is not regulated within this article but within the article below.

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<sup>64</sup> UK P&I Rules, No: 16/B

<sup>65</sup> UK P&I Rules, No: 17

<sup>66</sup> UK P&I Rules, No:2/1,2,3,4, Skuld Rules No:7/1

b) Liability arising under certain indemnities and contracts due to injury, illness or death of the crew, passengers or other persons.

In addition to the cover above, the kind of losses or expenses arising under law or contract are within the scope of the guarantee.<sup>67</sup>

c) Repatriation expenses of crew of the registered ship,

Covering the repatriation expenses of the crew depends on realizing this with a legal justification. In this sense, when there is no reason for the insurance to be involved, as in the case of a number of crew whose labor contract is terminated is returned to his/her country, these expenses should not be covered.<sup>68</sup> However, it cannot be said that all of these cases are excluded from the coverage. For example, repatriation expenses of a seafarer who has left the ship to go to the funeral of a relative can be covered.<sup>69</sup>

In particular, repatriation expenses incurred because of the following reasons are within the scope of P&I insurance coverage:

If the repatriation of the seafarer is necessary due to an injury, illness or death,

If the repatriation of the seafarer is necessary due to the fact that the ship is involved in a serious accident.<sup>70</sup>

d) Substitute expenses of the crew of the registered ship,

When a new seafarer replaces another member of crew leaving the ship in cases of injury, illness and death as mentioned above, these expenses are paid within the

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<sup>67</sup> UK P&I Rules. No: 2.14

<sup>68</sup> Acar, s., Supra. p. 97

<sup>69</sup> Skuld Rules, No: 7.1.6

<sup>70</sup> Skuld rules, No:7, UK P&I Rules, No:2/4



scope of P&I insurance coverage.<sup>71</sup> Particularly substitute expenses due to the following reasons are within the P&I insurance coverage:

- If a substitution is necessary due to the injury, illness or death of a seafarer,

- If a substitution is necessary for the seafarer repatriated to his/her country or landed for a reason arising from the law.<sup>72</sup>

e) Diversion expenses.

As a rule, liability and expenses resulting or arising from deviation are considered to be outside of P&I coverage. However, for treatment in cases of injury, illness of ship men, losses or damages resulting from a deviation occurring due to reasons such as presence of stowaways or refugees on the ship and salvage are covered within the scope of P&I insurance. Again, port charges and other extra expenses for landing of the persons aforementioned are included in the insurance.<sup>73</sup>

f) Life salvage

If life salvage is realized within a salvage process, this is indeed related to hull and cargo insurances and considered to be a moral duty. Thus, this activity is accepted as not to be entitled to any indemnification. However, charges and expenses, which are legally necessary to pay to the persons rescuing or trying to rescue the ones on the ship are paid within the scope of P&I insurance. However, if some of these expenses are covered by hull insurance or cargo insurance, P&I insurance does not cover these.<sup>74</sup>

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<sup>71</sup> UK P&I Rules, No:2/4, Skuld Rules, No:7.1.10

<sup>72</sup> UK P&I Rules, No:2/4, Skuld Rules, No:7.1.10

<sup>73</sup> Skuld Rules, No: 11, UK P&I Rules, No:2/7

<sup>74</sup> Williams, R., *Supra*. p. 192

g) Collision with other ships

Hull insurance secures the liability arising from the collision and excludes a certain percentage of the liability in general. This proportion is 1/4 of the liability. Here, this 1/4 proportion not secured by the hull insurance policy but by P&I insurance.<sup>75</sup> Similarly, P&I will cover any liability which exceeds the amount covered by the hull insurance.

P&I can provide other guarantees regarding the collision in addition to the 1/4 collision liability in return for extra premium.<sup>76</sup>

Collision losses with 1/4 assurance by the P&I insurance are as below:

- Damages to the things on the other ship (collided),
- Delay of the cargo on the other ship (collided),
- General average debt shares and salvage expenses of the cargo on the other ship,
- Sue and labour expenses.

If two ships collide with each other, everybody will participate in the damage with the proportion of their faults. If the damage occurred due to a force majeure without anyone's fault, in this case each one bears his/her own damage.

h) Loss or damage to property (fixed or floating objects)

Damages caused to ports, docks or similar fixed or floating objects by the ships registered under the P&I club striking them and the damages to the cargo due to such events are within the scope of the P&I insurance coverage.<sup>77</sup>

As the definition of a collision is two ships colliding with each other, ships

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<sup>75</sup> Ibid. p.219

<sup>76</sup> Hazelwood, J.S., Supra. P. 127

<sup>77</sup> UK P&I Rules, No:2/11

colliding into fixed or floating objects are not considered collisions.

i) Liability arising out of towage of or by an entered ship

Towage of the ship can be divided into two routine or not routine. Routine towages are towing activities with the purpose of entering into a port, leaving the port or making a movement in the port.<sup>78</sup> On the contrary, non routine towages express rather open sea towages.<sup>79</sup>

Damages caused to others during the routine towage of the ship to the port and within the member's liability are also included in the P&I insurance coverage. However, to benefit from the coverage, it is necessary that this damage should not be a damage included in the hull policy.

j) Removal of wreck (Wreck Liabilities)

A wreck occurs when the ship becomes unserviceable and loses its ship feature in one sense. In case the ship registered under the P&I club becomes a wreck, and per the legislation is required to perform removal of wreck, it is within the P&I cover provided that the operations are approved by the P&I club and the rights over the wreck are not disclaimed and subjected to conveyance. The value of the wreck is deducted from the indemnity to be paid by the P&I club. Expenses involved in the wreck removal of coverage are as follows:

Expenses related to removal of wreck of the insured ship or the things on the ship,

Expenses related to removal of wreck of the things on the ships collided with in case of collision,

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<sup>78</sup> UK P&I, Rule No:2.13, Skuld Rule No:23

<sup>79</sup> Standard, Guide to P&I

- Liability arising during the removal of wreck.<sup>80</sup>

#### k) Quarantine expenses

For ships having epidemical dangers, measures like disinfection of the ship, quarantine of the ship, or not being allowed to enter the port are applied. Among these measures, the quarantine obligation causes additional expenses for the ship owners. If the ship registered under the P&I does not know that it will be subjected to a quarantine obligation at the destination port when it goes on a voyage, quarantine expenses due to an epidemical disease are covered within the scope of P&I insurance with the following conditions.<sup>81</sup>

- An epidemic should occur on the ship,
- Net losses of the quarantine and disinfection expenses encountered by the member are within this coverage,
- If it is known or knowable that the ship will be quarantined at a port and yet the ship goes to that port, the expenses are not indemnified.<sup>82</sup>

#### 2.4.3.1.2 Indemnity Cover

Risks involved in the indemnity cover are the liabilities arising due to the income-generating function of the ship.

#### a) Cargo liabilities

The liability of the ship owner due to the deficiency of the cargo or subject of the transportation and damages or losses are secured by the P&I insurance. Various reasons can cause damage to the cargo.<sup>83</sup> In addition, in case some other conditions occur, P&I insurance can be valid in terms of this liability. These conditions are

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<sup>80</sup> UK P&I Rules, No:2.15, Skuld Rules No:20, Britannia Rules No: 19

<sup>81</sup> UK P&I Rules, No:2.16

<sup>82</sup> Skuld Rules, No:21

<sup>83</sup> UK P&I Rules, No:2.17

briefly mentioned below.

Bill of lading<sup>84</sup> should be issued in accordance with the provisions of the 1924 Brussels Convention. However, with the consent of the P&I club, another bill of lading can be used.

If a value over 2500 USD dollars is declared per piece for the cargo in the bill of lading, the value exceeding this value is not indemnified.

It is necessary to take required actions and to follow the recommendations if a cargo, which is likely to be broken is carried.

If the damage to the cargo on the ship occurred as a result of detouring of the ship without the consent of the P&I club, this damage is not covered by the P&I club. If there is a deviation without the knowledge of the ship owner, the ship owner should inform the P&I club about this situation immediately.

In many cases of faulty bills of lading, damage to the cargo is not within the scope of the P&I insurance.

Discharging cargo, which does not comply with the contract of carriage is also out of the coverage.<sup>85</sup>

b) Liability arising from the damage to the cargo in case of collision (General average contributions)

If the ship owner is responsible for the damages to the cargo on the other ship as a result of a collision, this responsibility can be claimed from the P&I club.<sup>86</sup> The liability here is 1/4 coverage in parallel with collision liability of the P&I.

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<sup>84</sup> Carriage of Cargo Contract

<sup>85</sup> UK P&I Rules, No:2.17

<sup>86</sup> UK P&I Rules, No:2/19, Skuld Rules, No: 17

c) General average contribution or salvage expenses of the cargo (General average contributions)

If the general average share or salvage expenses of the cargo are not met by the responsible cargo or another party due to the carriers breach of the contract, these expenses are indemnified by the P&I insurance. The conditions related to bills of lading mentioned in the indemnity of the damage regarding carrying of the cargo should also exist here.<sup>87</sup>

d) Ship's proportion of general average

P&I secures the ship's proportion of general average and salvage under the following conditions:

P&I insurance provides cover for the part exceeding the part secured by the hull insurance,

The reason for the coverage being left out of the hull policy should be that the value calculated for the participation in ship's proportion of general average or salvage expenses should exceed the value written in the hull policy.

The value of the ship on the hull policy should be up to date.

e) Pollution (Guarantee) Risks

Oil pollution experienced on March 18, 1967 in the Torrey Canyon disaster in the English and French seas can be seen as the reason for the emergence of environment liability law. This big pollution incident showed that the polluted environment can reach unrecoverable dimensions.

After the Torrey Canyon disaster world states sought to constitute an indemnity regime against the damages to the environment. Within this scope, the

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<sup>87</sup> UK P&I Rules, No:2

1969 Civil Liability Convention has included 'strict liability' and 'compulsory insurance' concepts into maritime law. With this convention entering into force in 1975, the owner of the ship causing the pollution was held strictly responsible and was allowed to limit his/her liability under certain circumstances for the damages arising from pollution environment of the oil.<sup>88</sup> On the one hand, strict liability of the ship owner was issued, with the same convention, and indemnity of the ship owner was guaranteed within the pollution liability by imposing an obligation to conclude insurance.

The CLC 1969 Convention was a start in terms of regulations about the environmental liability of ships and after that date, various conventions and regulations emerged regarding the same issue. These regulations, also known as IMO Conventions, are listed below:

- International Oil Pollution Compensation Funds regarding Establishment of a Fund for Compensation of Oil Pollution Damages dated 1971 (IOPC Fund)

- With this convention, an international fund was established to cover environmental pollution damages. The oil industry was obliged to make contribution to this fund.

- International Convention for the Prevention of Pollution from Ships (MARPOL 73/78)

- 1992 Civil Liability Convention Protocol (CLC 92) and 1992 Fund Convention Protocol (Fund 92)

CLC 1992 was accepted to correct the deficiencies in the Fund Convention dated 1971.

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<sup>88</sup> Anderson, P., Supra. P. 133

All of these regulations are important for the P&I insurance, because the liability regarding the damages arising from the pollution is on the ship owner, and shipowner obliged to be insured. Insurance regarding the pollution in question is provided by the P& clubs.

The scope of the coverage provided by the clubs regarding oil pollution is defined in the club rules as: "The liabilities, losses, damages, costs and expenses that the member will encounter as a result of the discharge or escape from an entered ship of oil or any other substance, or the threat of such discharge or escape are within the club insurance coverage."<sup>89</sup>

When the club rules are examined in details, it is seen that the scope of the coverage is as below:

- Losses or expenses arising from the pollution, which occurred during the discharge of oil or other harmful substance from an entered ship,
- The costs of any measures reasonably taken for the purpose of avoiding or minimizing pollution or any resulting loss or damage together with any liability for loss of or damage to property caused by measures so taken,
- Liabilities arising from carrying oil at the sea as per any contract in which the member or the club is involved,
- The costs or liabilities incurred as a result of compliance with any order or direction given by any government or authority, for the purpose of preventing or reducing pollution or the risk of pollution,
- Damages to the cargo on the ship or to the property of the member due to the discharge or escape of oil from the ship, (These damages are within the coverage

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<sup>89</sup> UK Club Rule No:2/12, Britannia Rules No: 19, Skuld Rules No:19



as considered to be for the third parties. So, the pollution is not only considered to occur outside of the ship.)

Damages arising from the oil discharged or escaped from the other ship because of a collision.<sup>90</sup>

#### f) Fines

Fines imposed by competent courts or administrative authorities for the members are within the scope of club insurance coverage. In order for a fine to be considered within the club insurance coverage, the fine should originate from the member or crew of the entered ship or third parties for whom the member is responsible in terms of activities and behaviors as per law or contract terms.

Fines within the scope of club coverage are listed as below:

- 1- Fines related to the notification or recording of the load on the ship,
- 2- Customs fines (fines regarding smuggling),
- 3- Immigrant fines,
- 4- Contamination fines,

The club insurance coverage is valid in terms of fines provided that:

- The fine should be declared clearly in the club rules,
- The member should make necessary efforts not to incur any fines,
- Fines incurred by the crew are within club insurance coverage from the member by the imposing authority. Fines that are obliged to be paid by the crew not requiring the liability on the member are not within the scope.<sup>91</sup>

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<sup>90</sup> Williams, R., Supra p. 233

<sup>91</sup> UK Club Rules No:2.22, Skuld Rules No: 20, Gard Rule No:49, Shipowners Rules No: 2.19

g) Confiscation costs

Losses and expenses following confiscation of the ship by any legally empowered court or authority can be paid within the discretionary power of the club.<sup>92</sup>

h) Sue and Labour and Legal costs

After a risk involved in club insurance coverage occurs, legal costs of the member are also within the scope of the guarantee. However, the costs should be acceptable and preventive and reduce the total costs of the club.<sup>93</sup>

i) Omnibus Guarantee

It is called omnibus rule when the club makes payment for a claim by using its discretionary power, although it is not obliged to pay. This is an accommodation payment. The club already has a very comprehensive discretionary power in terms of various damages. It can be possible to pay a risk, which remains outside of the coverage.<sup>94</sup>

#### 2.4.3.2 Other Guarantees

a) Freight, Demurrage, and Defence (F.D.&D.)

This guarantee secures legal interests. When the member encounters a legal problem, the club steps in and pays the legal costs. Almost every club has rules regarding this guarantee.

However, there are clubs named 'defence clubs' established to exclusively provide this cover.

The freight and/or demurrage in themselves are not covered here. F.D.&D.

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<sup>92</sup> UK Club Rules No:2.22

<sup>93</sup> UK Club Rules No:2.25

<sup>94</sup> UK Club Rules No:2.22, Skuld Rules No: 20

guarantee covers defence costs related to freight and demurrage. Thus, this guarantee covers all legal costs.

b) Strike

Strike insurance covers the losses arising from the strikes of crew. Retention of the ship by the crew and operational expenditures during this period are secured. Club demands a separate premium for this guarantee.

c) War

War insurance left out of the scope of coverage in almost all insurance types are within the club insurance guarantee. Clubs have special rules for war risks. Furthermore, there are clubs established only to provide this cover.

#### 2.4.4 Risks Excluded From Coverage

a) Insurable interests within hull insurance coverage are outside of the coverage. In other words, losses or damages that an entered ship or its equipment will encounter are not within the coverage, if they are covered under the hull policy. However, the club rules can otherwise be stated.

b) Liabilities arising from carrying nuclear, explosive substances on the ship registered in the club are out of coverage.

c) Using the ship registered in the club for illegitimate operations are out of the scope of the club coverage.

d) In case of double insurance, only one indemnity payment is made. For that reason, in the exclusions title under club rules, double insurance is mentioned.

e) Costs regarding the repair or cleaning of the ship are out of the coverage.<sup>95</sup>

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<sup>95</sup> Britannia Rules No:20, UK Club Rules No: 5, Skuld Rules No:30, North of England Rules No: 27, Standard Rules No:19

## 2.5 Reinsurance

Reinsurance provider of the club insurance is an International Group which is an association consisting of the clubs providing club insurance assurance (International Group of P&I Clubs). The International Group has 13 members in total with eight from England, two from Norway, one from the United States, one from Sweden and one from Japan.

With the International Group, the relationship between the clubs are regulated through a contract. The International Group has a secretariat established in London. The basic purpose is to share the risk that each of the clubs poses among the group members. Conditions related to this are regulated under the contract named pool contract. For a club to be a candidate member of a member of the International Group, it has to be established since five years at least and its financial status should be stable and creditable in its own country.<sup>96</sup>

The International Group provides reinsurance for their members within the conditions below:

According to that

- Each group is liable for risks up to 8 million dollars.
- Risks between 8 million dollars and 30 million dollars are shared between themselves in certain proportions as per 'pool' contract.
- The part between 30 million and 50 million dollars are within the coverage scope with reinsurance system called as Hydra.
- The International Group provides assurance with 'excess of loss reinsurance' from Lloyd's sector for the losses between 30 million dollars and 2,050 billion dollars.

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<sup>96</sup> Hazelwood, J.S., *Supra*. P. 368

□ Losses above 2,050 billion dollars are treated as per a contract attachment of co-sharing agreement named overspill agreement. These claims are collected from a fund named the Catastrophic Reserve Fund.<sup>97</sup>

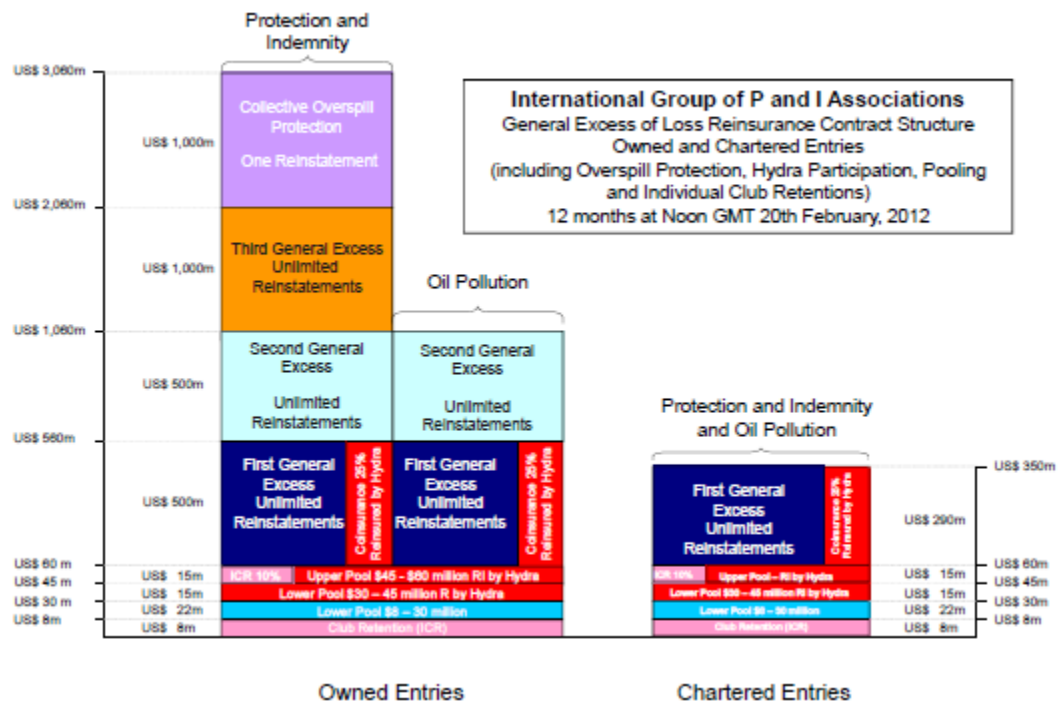


Figure 1: Reinsurance Chart of International Group<sup>98</sup>

There are three functions that the International Group fulfils.

The primary and the most important one is reinsurance function. With club insurance, risks above 8 million dollars are within the scope of the coverage. Not only the clubs involved in the International Group but all clubs can benefit from the reinsurance coverage (time to time including the clubs with fixed premium).

The second function is 'representation' function. This function is fulfilled in order to protect the interests of the clubs. Particularly, the International Group represents the clubs in international organizations and operates as a pressure group during preparation of a legislation.

<sup>97</sup> <http://www.igpandi.org/Group+Agreements/The+Pooling+Agreement>, Last Visit: 15.08.2012

<sup>98</sup> <http://www.igpandi.org/Group+Agreements/Pool+reinsurance+programme>, Last Visit: 15.08.2012

The third function is to provide information exchange between the clubs. Subcommittees working within the International Group inform the clubs who in turn inform the members. This information exchange can be related to general issues like oil pollution, physical damages and can also be related to instant information like maritime security.<sup>99</sup>

## 2.6 Debts of the Parties in Club Insurance

### 2.6.1 Debts of the Member

#### 2.6.1.1 Premium Payment Debt

In club insurance, the basic debt of the member is to pay premium. The price called premium or fee can differentiate in terms of fixed premium and mutual clubs. In mutual clubs, premium, as stated before, is the amount arising as a result of sharing the loss claim between the members paid by the club for the previous year. Here the fundamental principle of equality of incomes and expenditures of the club works.

Premium is fixed in the clubs with fixed premiums and as will be stated later, additional contribution, release contribution or extraordinary contribution fees are not collected from the members as in mutual clubs. As a result of this, a certain insurance amount is determined for each coverage type in these clubs and indemnity payment is made as limited to this amount.

In mutual clubs, when incomes of the club are discussed, it is referred to contributions and investment incomes. Indemnities and operational expenditures compose the expenditures of the club. Premium can be collected with different names at different times. These premiums will be addressed below briefly.

**Advance Calls:** The premium is paid in cash once the member enters the club. This premium is determined according to the tonnages of the ship registered under the club. It is a premium characterized with basic contribution given for both

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<sup>99</sup> <http://www.igpandi.org/About>, Last Visit : 15.08.2012

operational expenditures and damages.

**Supplementary Calls:** The members can be asked for additional premium for the expenses of the club after the policy year ends. Particularly, it can lead to additional premium demand whose amount of damage is realized over the expectations and claim payments following the judgment decrees.

**Release Calls:** As per the club rules, the member leaving the club makes release payment with the purpose of being exempted from additional premium in the next policy year.<sup>100</sup>

**Catastrophic Premium (Overspill Calls) :** During the policy year, in case the members demand indemnity claims with very large amounts, clubs demand catastrophic premium from the members. In order to demand this premium, indemnity claims should exceed the source of catastrophic reserve fund created within the International Group.<sup>101</sup>

#### 2.6.1.2 Obligation of Notification

The member should always share the information related to the quality of the risk as per 'utmost good faith' rule having an important place in English law which is also defined in MIA. In this sense, this obligation can emerge for the member before the contract, during the contract and after the contract. The first point where this obligation emerged first is the application form constituting a basis for the contract between the member and club in club insurance. A Member is responsible for declaring the issues determining the risks in membership application form. A Member fulfills notification liability before signing the contract in one sense by filling in this application form. A Member should also inform the changes declared in the application form having important influences.

If a member insured the same risk with another club, he/she should inform the

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<sup>100</sup> Skuld Rules No:4/5, North of England Rules No: 16

<sup>101</sup> Skuld Rules No:4/4, North of England Rules No: 13

club about this double insurance. A Member should also inform the club about the address change. Otherwise, the notifications made to previous address is considered to be valid. In addition to these, if any risks involved in the coverage are realized, this should be reported to the club by the member immediately.

In case the member doesn't fulfill his/her obligation of notification on time and properly, it is possible to encounter consequences like not paying or partly paying the indemnities.<sup>102</sup>

Although it is stated above that it is necessary to share the information regarding the quality of risks with the club, due to the widely and flexible application of utmost good faith rule, it is necessary to consider the liability in question as every kind of information to take into consideration in the premium account of the member and entered ship. Regarding this issue MIA brought an arrangement, namely "Every circumstance is material which would influence the judgment of a prudent insurer in fixing the premium, or determining whether he will take the risk."

Circumstances not required to be reported unless wanted by the insurer are listed in the same article of MIA. These circumstances are:

- Any circumstance which diminishes the risk,
- Any circumstance which is known or presumed to be known to the insurer. The insurer is presumed to know matters of common notoriety or knowledge, and matters which an insurer in the ordinary course of his business, as such, ought to know,
- Any circumstance as to which information is waived by the insurer,
- Any circumstance which it is superfluous to disclose by reason of any

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<sup>102</sup> UK Club Rules No: 5/N



express or implied warranty.

#### 2.6.1.3 Obligation to Take Protective Measure

One of the duties of the member to the club, is taking necessary measures to prevent incurring of the damage and growing of the damage after it incurred. This issue is defined in Article 78/4 of MIA as; “It is the duty of the assured and his agents, in all cases, to take such measures as may be reasonable for the purpose of averting or minimizing a loss.” Due to these measures taken and efforts to diminish the damages, expenses are secured by sue and labour clause. Measures like surveying the ship and performing necessary maintenance accurately are among the measures required to be taken.

In the club rules, it should be stated that the member is obliged to have his/her ship surveyed in a determined period of time by the surveyor assigned by the club.<sup>103</sup>

It is necessary to fulfill repairment requirements detected during these surveys.<sup>104</sup>

#### 2.6.1.4 Pay To Be Paid Rule

The damage occurred for the third party should be paid by the member besides the debts and obligations mentioned above so that the club can make payment to the member.<sup>105</sup>

This rule named as “Pay to be paid” is among the liabilities of the member.

#### 2.6.2 Liabilities of the Club

As the member has various liabilities against the club, club has also some liabilities against the member. Primary liability is to provide insurance coverage against the liability of the member to pay premium.

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<sup>103</sup> North of England Rules No: 30, UK Club Rules No: 5/Q

<sup>104</sup> North of England Rules No: 29/5, UK Club Rules No: 5/K

<sup>105</sup> Hazelwood, J.S., Supra. P. 335

Within the scope of the insurance coverage provided by the club, first of all fulfilling the demands of the member should be mentioned. Within this frame, activities such as performing necessary determinations, suing necessary law suits and taking necessary steps are met by the club.

Another liability of the club is indemnity payment. In order for the club to make indemnity payment, a risk within the coverage of the club insurance should be incurred. In order for the member to have right for indemnity, he/she should fulfill his/her liabilities. Another condition for the club to make indemnity payment is to be behaved in accordance with the payment rule first.

Besides these liabilities of the club, there is a liability to provide financial guarantee. This liability particularly emerges as to procure club guarantees and bank guarantees rapidly to ensure that the ship with seizure or under seizure danger starts to move as soon as possible.<sup>106</sup> In case of detention of the ship at any port, this liability should be fulfilled immediately.

## 2.7 Fixed Premium Insurers

An important recent development has been the proliferation of fixed premium P & I insurers. The common perception is that such underwriters, although the mutual P & I clubs usually have a good product for large operators, they can provide coverage and service that is tailored to the requirements of a small owner operating in a less complex environment. In other words, not everyone needs a five star product, including unlimited liability, a strong legal support, detailed representation worldwide and practical assistance claims. Some owners will be very happy with a more limited coverage and less sophisticated service demands. These owners are almost invariably small craft operators in a niche market that does not stray far from home and may not be able to share additional future calls. Fixed premiums insurers believe that 10-15% of the total activity is to have a ship of their natural market and

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<sup>106</sup> Algantürk D., Supra. p. 116

the owners should not be entered with a mutual club. As a consequence, several alternatives have emerged, therefore, some of which are now well established.<sup>107</sup>

Some insurers are reinsured fixed premiums to Lloyd. Underwriters favor small vessels engaged in local trade and prefer to stay away from transoceanic voyages. These cover small tankers where the limits of the CLC<sup>108</sup> within their coverage limit and they will issue blue cards (confirmation of P & I cover to CLC authorities).<sup>109</sup>

The distinction between protection and indemnity risks today is largely theoretical but originally covered passive protection to personnel and damage to property, while compensation liability under the cargo owners under a contract of carriage. Today, most owners still get their coverage of liability insurance from P & I clubs although it is possible to achieve with other underwriters, usually for a fixed premium and the limits of generally low coverage than those offered by the clubs.<sup>110</sup> Two characteristics that distinguish the P & I clubs from other insurers are that they are controlled and governed by their member shipowners, who provide the members with a degree of flexibility, and they are run on a nonprofit or mutual, basis making them economically attractive.<sup>111</sup>

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<sup>107</sup> Drewry Briefing Report., 1998, Marine Insurance Issues, Practice and Costs, Drewry Shipping Consultants Ltd., p. 42

<sup>108</sup> Civil Liability Convention 1992, shipowners have strict liability because of effecting oil spill for carrying permanent spill hydrocarbons or another words; crude oil.

<sup>109</sup> Drewry Brief Report, Supra, p. 42

<sup>110</sup> Merkin, R., et al., Supra, P. 337

<sup>111</sup> Ibid. P. 337

## CHAPTER 3

### 3 National P&I Institution

#### 3.1 Introduction

The main objective of having a national P&I institution is to ensure that domestic shipowners/operators will be able to meet their financial responsibility for any legal liability arising out of any maritime related incidents.

A second objective is to ensure that there is adequate marine insurance coverage, secure legal liabilities and expenses for damage, or compensation of risks as they are not covered under existing local regulations.

This explains the interest of some of the local authorities why they see a need to set up their own P&I institutions. Generally, domestic legal rules are the starting point of their focal demand; cabotage trade is second in the queue because some international conventions have mandatory international insurance covers, which are really hard to find for shipowners due to insurance providers' higher risk assessment processes. Typically, the age of cabotage vessels is high, and they are sailing in high collision risk areas like short sea shipping. Further, they have financially low trade capability; therefore, they have many sub-standard features for risk assessment criteria' for the International Group of P&I members. However, local legislations are ordering shipowners to have protection and indemnity insurance certificates. In other words, it is not easy for the cabotage ships and weak operators to find a relevant P&I insurance from five star clubs. Those ships have some legal liabilities, which come from the national legislation but they are totally out of the IGPANDI risk assessment scope.

There are many aspects that would need to be looked at to establish a purely domestic P&I institution, not least the competition (law) aspect, if such a P&I provider would have to abide by EU and domestic competition law. Capital requirements would also need to be closely considered, particularly the future

Solvency II<sup>112</sup> requirements if such a domestic insurer has to abide by those rules too. Without a reputation to speak of, since it would be a start up facility, it would have to obtain the confidence of a sizable percentage of the national fleet as well, if it were to insure only nationally registered vessels. Since most of the oceangoing nationally registered vessels are insured through the IG Clubs, and with some non-IG providers, it would be necessary to question whether such owners in adequate numbers would be prepared to leave the relative comfort of their existing P&I provider (if the word “comfort” can be used) to join a start up facility that would not only have no experience in the P&I world, but would be competing against the existing P&I market, which can be quite cut throat!<sup>113</sup>

There are many critical questions before setting up a national P&I institution. The following key questions have to be well answered before taking financial decision to set up a national P&I institution. What sort of levels of cover would be provided? For what risks? At what price? With what level of Club retention and what level of reinsurance? Where would that reinsurance be placed? With what level of security/rating requirements? How would the membership be serviced? Where would the Club be registered? What would the Club’s policy be on its investments? How would the premium calls be structured? Would it be a mutual or a fixed premium insurer?

In this dissertation, the author will try to find answers to all the questions especially in conclusion.

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<sup>112</sup> The **Solvency II Directive 2009/138/EC** is an [EU Directive](#) that codifies and harmonises the EU insurance regulation. Primarily this concerns the amount of capital that [EU insurance](#) companies must hold to reduce the risk of [insolvency](#).

<sup>113</sup> Interview with secretary of IGPANDI David BAKER date on 25.06.2012

## 3.2 Proficiency of Countries for serving Cargo and Hull & Machinery insurance

### 3.2.1 Historical engagement

Most countries have enough capability to service hull and machinery (HM) and cargo insurance. This experience always gives an advantage to them to follow to resolve new challenges. As already mentioned in the first chapter, the mentality of mutuality appeared in the area of H&M Clubs. National H&M insurance providers could try to join together to share control of claims. This practice will support development of a mutuality culture in the local market. Countries which plan to set up a national P&I institution could start by this step and they might find success at the end.

Historically, the concept of mutuality existed in the HM market. This reality shows that it is the right beginning area for national insurers to train themselves for the next step. Therefore, the next step will be establishing a national P&I Club.

### 3.2.2 Technical Engagement

When the provider of the HM insurance and P&I cover are coming from the same origin as the shipowner, there will not be any conflict to resolve in finding a responsible party for claims, or disputes regarding which insurer should compensate a loss. A shipowner might prefer to get the insurance certificates from the same provider who issued HM and P&I at the same time. In this case, the shipowner's intention is to try to protect himself from double insurance risk possibilities. The source of this problem comes from the covering of the same risks with two different insurance policies; all possible future claims negotiations can be resolved by having a different insurance from same provider. This method will be helpful to easily find the responsible party. All possible claims will be carried out with one provider, and they will be compensated on behalf of the shipowner; in fact all claims will be handled with safely compensated.

In other words, if both insurers are supporting or serving from the same sources, claims are handled with very simple settlements, and assessments of compensations will need only short time periods. This is an absolute comfort for the shipowner to have the perfect insurance service. Additionally, there might be an operational convenience for the insurer in the claims handling process.

### 3.3 Reaching National Statistics

P&I insurance is one of the most important services to national shipping and therefore such services should be provided within the nation. It will be easy to establish data records about marine incidents, and collecting information for casualty investigation is carried out in a safe manner, and these data are helpful for making risk analyzes.

#### 3.3.1 Preparing Initial Plans for Setting Up

Preparing the initial plan is important, and it is easy to reach the national statistics to create national policies by the recognized authorities who wish to be pioneering in order to form an association of owners of small and medium sized ships, which are operating on the coast. For example, this P&I institution, which will provide insurance cover to these ships by collecting a fixed premium, will go for 100 per cent reinsurance. The structure of the institution will be worked out after taking into account taxation and regulatory issues. All the outputs can be found from national statistics to choose the structure of the P&I, which could be mutual or a fixed premium.

There might be some alternative reasons for choosing the structure of the new P&I facility, like in the case of small and medium sized vessels, claims will be lower as compared to large ocean going vessels. So the recognized participants have proposed to start with coastal ships in the initial plan.

### 3.3.2 Mother Tongue Advantages

Not only to analyze the statistics, but also during the operations, communications between insurance provider and member or customer of the insurer dialogs, using the mother tongue has an absolute advantage to find solutions for the all possible situations like analyzing the data or asset to claims.

Using the geographical advantage, a new provider needs to register in its own country. In the first decades, it will serve local and regional potentials. Because of this, tax advantages are secondary unlike for most IGPANDI members.<sup>114</sup>

### 3.4 Coverage

Like the majority of Clubs, national P&I institutions cover their members or customers for similar third party liabilities in respect of loss of and damage to cargo, injury, illness or loss of life of crew or passengers, pollution damage, collision liability, fines, and wreck removals.

#### 3.4.1 Relations in IGPANDI and the World Market

As in market conditions, a national P&I institution should have a good cooperation with the international P&I society. Although it may still not be a member of IG Clubs, the coverage provided by itself is, in principle, identical to that provided by a IG Club in respect of both scope of cover and possible service limits. In other words, nothing has to be served different from IG Clubs by national P&I institution. It might maintain very close links with some major clubs in the pool through a co-insurance arrangement.

Initially, national clubs might need some support from one of the IGPANDI members. This support is like an umbrella for sharing its market experience and

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<sup>114</sup> Some of the IGPANDI members has shifted their head Office to offshore countries instead of their natural origins, because of benefit from tax advantages.



management knowledge. Finding a helping hand in the setting up period is getting a unique advantage for the establishment of a new national P&I institution.

### 3.4.2 Fixed Premium versus Mutual

Both systems have their own advantages, and they will need to be compared very clearly before starting the new institution.

A mutual insurance company, which is called a club, provides cooperative self-insurance to its members. The membership is composed of a common interest group wishing to pool their risks as well as for "at cost" insurance coverage. The club as a "non-profit" mutual is therefore owned by the insured. As it has no shares to be issued, it does not need to make profits or give dividends.<sup>115</sup>

Moreover, at fixed premium insurers, they generally tailor their policy and costs according to each shipowner's individual situation, and consensual agreed premium for the policy year is fixed and final, so shipowner will never be asked to pay any supplementary calls.<sup>116</sup>

IG clubs just expect to provide having high standard ships and operators. It is quite normal for a ship to be inspected with a condition survey, as it has almost certainly happened before being a new member. If ships do not reach the international safety or security standards, then they will not be accepted until / unless the deficiencies are corrected. There may also be a review of the office of the ship's operator and the management team. Again, if the club is not convinced that the acceptable standard is in operation, it is likely that coverage will be denied.<sup>117</sup> Those mentioned ships, which are seen as sub-standard by the IG, will need to carry insurance certificates on board for continuing their commercial trade. In this case,

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<sup>115</sup> Find more: [http://www.epandi.com/ukpandi/infopool.nsf/html/About\\_Home](http://www.epandi.com/ukpandi/infopool.nsf/html/About_Home) last visit: 18.07.2012

<sup>116</sup> Find more: <http://www.raetsmarine.com/products/ShipownersLiabilityPandi/fixed-versus-mutual> last visit: 18.07.2012

<sup>117</sup> Anderson, P., (2011). Postgraduate Diploma in Marine Insurance 2010/2011 Module Three – P&I Clubs and Mutual Insurance, LLOYDS Maritime Academy, p. 22

those small ships or their operators ask to have P&I from fixed premium insurers. Actually, they are not really sub-standard, but their current standard is below the IG risk assessment level. In reality, the ships under IG insurance are continued to be detained during port state controls<sup>118</sup> because of their sub-standard technical conditions. It does not mean that a ship by being entered in any Club membership after a Club's condition survey, will have port state control standards.

It appears, however, that these vessels or ship operators may find insurers willing to provide liability insurance or they can navigate the ship without insurance coverage.<sup>119</sup>

The historical background of the protection and indemnity insurance has traditionally and originally been based on the mutuality concept. Some of the fixed premium providers have withdrawn after limited service in the P&I market. Generally, reinsurers prefer to use their underwriting capacity in the most profitable areas instead of the limited income markets of third party liability insurance. So it is not easy for the fixed premium insurance providers to find acceptable rates of the reinsurance offers.

Third party liability itself is really a huge responsibility for the ship owner and his insurer is carrying out this responsibility on behalf of him. However, if you are the insurer and assured at the same time, you may have control yourself, and it may be practically feasible to compensate possible claims. In fact, the commercial insurance market process is different from this situation and it has to find profit at the end of the day. That is why countries prefer to set up their national P&I institutions in the mutual concept instead of fixed premium. There are many examples where countries have set-up mutual systems like Japan P&I, Korea P&I, China P&I and Filipino P&I. The first three, P&I Clubs are considered to have capability to accomplish the

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<sup>118</sup> **Port State Control (PSC)** is the inspection of foreign ships in national ports to verify that the condition of the ship and its equipment comply with the requirements of international regulations and that the ship is manned and operated in compliance with these rules. Read more: [http://www.imo.org/blast/mainframe.asp?topic\\_id=159](http://www.imo.org/blast/mainframe.asp?topic_id=159) last visit: 30.08.2012

<sup>119</sup> Anderson, P., *Supra*. p.22

reinsurance requirement from their own reserves or local capabilities. It means it is not necessary for them to contact western reinsurers for obtaining reinsurance.

In national P&I institution concept, providers choose mutuality instead of fixed premium. The Indian maritime administration and competent authorities have started to negotiate to set up a national P&I institution for their cabotage ships based on mutuality. Fixed premium itself is totally commercial, and local authorities or national structures take care of strong protection against possible risks, first rather than trying to have profit.

On the other hand, a smaller tonnage vessel shipowner has to be part of a huge risks pool<sup>120</sup>, due to the memberships of the bigger tonnage shipowners in the same pool. His marine peril risks are maybe lower, but automatically he has to share huge potential risks of big pool contributors with their properties and trade capacities because of being party of the mutuality system. Additionally, he has gigantic risk cover limits, which maybe never need to be used. Maybe it is not necessary for his trade to have those guarantee limits, and live together with five star standards. As already mentioned, IG has upper insurance limits, and some shipowners never need to ask for the compensation limits and it is not cost efficient to have these limits because of their lower trade capacity.

### 3.5 Reinsurance

The balance of any P&I premium formula main outgoing expense will be reinsurance premiums. Reinsurance premiums are fixed with the financial and technical capability of the insurers, and there are differences depending on the market conditions. Most of the time, insurers pay reinsurance premiums with their levy premiums at a ratio of 30-40 percent of their premium income. Market players who are party of the low market have to pay high premiums for reinsurance. In that

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<sup>120</sup> Although the Group clubs compete with each other for business, it is to the benefit of all shipowners insured by Group clubs for the clubs to pool their larger risks. Pooling is regulated by the Pooling Agreement which defines the risks that can be pooled and how losses are to be shared between the participating clubs. The Pool provides a mechanism for sharing all claims in excess of US\$ 8 million up to, currently, approximately US\$ 6.9 billion. Read more: <http://www.igpandi.org/Group+Agreements/The+Pooling+Agreement> last visit: 30.08.2012

case, the insurance service costs more because of the financial and historical background, and reinsurance premiums are higher. Initially, a new institution is not a good competitor in the market due to the need to pay huge reinsurance premiums.

The International Group clubs organize an excess of loss reinsurance for the club's individual members. It is the largest of most existing maritime liability policy and is headed by the Janson Green Syndicate at Lloyd. Participating underwriters, each with a relatively low line are distributed around the world and this is probably the most complex political and international maritime market. (A notable absentee in the policy is Munich Re, which became a P & I reinsurer to the "alternative" (non-group) P & I market.) The excess loss reinsurance suits the international market in that it has a share of U.S. \$ 2 bn P & I industry without the need to develop the expertise necessary to manage the intricacies of P & I claims.<sup>121</sup>

It is generally accepted that a large P & I account is necessary to provide sufficient diffusion of risks and to avoid excessively volatile exposure to claims. The question is how dire is the need of a portfolio for P&I to be self-sufficient and stable? Indeed, is there an optimal size of a P & I Club? The issue is further complicated by the pooling agreement, which absorbs all claims in excess of U.S. \$ 8 million and the shield of the IGA<sup>122</sup>. In the 1980s two P & I Clubs have ceased their activities. The main victims were the non-IG Oceanus Group, which collapsed when its reinsurance underwriters withdrew, and the member of the group, Sunderland Club, which was easily absorbed by the IGA colleague, the UK Club. This shows that the IGA looked after its own and the owners could count on the greater security of the International Group.<sup>123</sup>

Both examples show that reinsurance is one of the most important issues of P&I management.

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<sup>121</sup> Drewry Report., Supra., P.67

<sup>122</sup> International Group of Agreement

<sup>123</sup> Supra.,Drewry, p.71

### 3.6 Tax Exception

Today, most shipowners procure their P&I insurance directly from foreign insurers. State treasuries do not have any income coming from the P&I insurance market because the service providers are already located outside of their jurisdiction. In that case, a new establishment of a national P&I facility may have some tax exception in the domestic market. There will not be any changes for the state treasuries' incomes, never having had this benefit from abroad, nor in local potentials. However, using this kind of tax practice technique may help the new national P&I provider to stand on its own capabilities.

### 3.7 Insurance Sanctions

This concept is very new in the global market. Provision of P&I insurance is used as a political argument as part of economical sanctions for blocking trade from a target country. India has decided to create its own P&I insurer because of sanctions from the Iran conflict. They have dealt with Iran for a long period of time carrying cargo, but currently they do not have P&I cover because of sanctions against Iranian trade.

EU and the USA have taken a decision to make sanctions against Iran, especially its oil trade. Most of the carriers have confirmed they will not ship oil from Iran. It is clear that the EU sanction to ban insurance has imposed a new stranglehold on shipping. The banning of insurance specially for tankers creates a relatively special position, as almost 95% of tankers are insured by a P&I club, which is a member of the IG, and which in turn dominates the market.

Shipping lines have to have liability insurance on board according to relevant international conventions in order to trade with Iran or attempt to find cover elsewhere. The insurance sanctions have a deep impact on the tanker industry, not just for the EU controlled fleet, which is being subject to a total trade and insurance prohibition, but also on the great majority of tanker owners around the world who are

contracted to lift Iranian oil regardless of destination. According to Liz McMahon's article in Lloyd's List, the IG has recently updated itself to follow EU sanctions against Iran with information to the members concerned. Non-EU regulated clubs are not directly affected by those sanction decisions, but their reinsurance arrangements are EU regulated. Consequently, non-EU regulated clubs are necessarily being part of the sanctions as well, because of their reinsurer relations (Lloyd's List, 2012).

For shipowners, P&I insurance is looking like a ticket for their trade. Asian players have long term contracts to carry crude oil from Iran. For trying to keep their trade potentials, Asian insurers have increased their own reinsurance for continuous trade from Iran.

After all those developments, the Iranian government will now provide insurance cover for any foreign ships entering its territorial waters. Therefore, the government took a decision to provide a sovereign guarantee but said insurers must limit cover to \$50 million.<sup>124</sup>

Unfortunately, the Indian Shipowners Association moved to set up its own mutual P&I Club after the sanctions against Iran because of the need to cover their current trade with Iran. "The move to set up an Indian P&I association assumes significance in the context of the recent decision of the Europe-based P&I Clubs to refuse cover to ships carrying Iranian cargo from July 1."<sup>125</sup>

Countries need to protect their trade and their fleets against all possible sanctions. P&I insurance is starting to be used as a political argument. However, oil spills can occur even in innocent countries which originally are not part of the current conflicts. For example, Iranian crude oil may be carried from Iran to China. During this voyage, an incident may happen and spilled oil may affect the Sri Lanka coasts. How is it possible to say that there are sanctions against Iran and this damage

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<sup>124</sup> McMahon, L., Iran Offers Insurance Covers to Oil Shipment Moving, Lloyds list no.60722, 20.07.2012

<sup>125</sup> <http://www.thehindubusinessline.com/industry-and-economy/logistics/article3533123.ece> last visit: 01.09.2012

is without any guarantee. Therefore, countries should to set up their own P&I facilities because of these possibilities.

## CHAPTER 4

### 4 Examples of National P&I Institutions

#### 4.1 Introduction

The International Group of P&I Clubs covers 90% of the world's P&I insurance market while the remaining 10% is covered by others, basically called as small contributors of the market. It is clearly apparent that many of the others (most of them are fixed premium institutions) can compete with the IG Clubs in terms of pricing, security and services provided. This chapter will mainly focus on some of these alternatives. They are really solid, viable businesses. Some are worth being mentioned for their potential (much as China P&I Club or Korea P&I Club) or for the alternative they offer in particular areas.<sup>126</sup>

On the other hand, the Japan P&I Club is part of the IG and an atypical P&I Club. However, it is closer to a "national" club, despite being a member of the International Group of P & I Clubs. In fact, even if it makes efforts to add tonnage of Taiwanese, Singaporean or Korean ships, the majority of vessels entered in its control are still Japanese. The club has its own "coastal" membership (payment of fixed premiums) for members who are not international traders.

#### 4.2 China P&I Club

##### 4.2.1 Overall Status

China Shipowners Mutual Association, commonly known as the China P & I Club or CPI, was established in 1984. Since then it has seen a spectacular development and improvement in aspects such as tonnage entered, membership, management and service levels in such a short time. With the full support of government agencies and maritime communities, the CPI has already become a major P & I Club in the Asia Pacific, offering suitable P & I cover and

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<sup>126</sup> Omni sectoral report 2011



comprehensive professional services. Nowadays, the members of this association are very diverse, not only limited to mainland China, but also include eminent owners in Hong Kong, Singapore and other parts of Far East Asia.<sup>127</sup>

CPI has adopted a policy of prudence and consolidation in underwriting. Its main concern is the benefits of mutuality: providing excellent service in a non-profit organization. The tendency to increase the reserve Fund shows that the financial situation of the club has been growing stronger over the years.

CPI reported that for February 20<sup>th</sup> of 2011, the Association had 135 members with a total of 1043 registered vessels totalling 27.8 million GT. The total tonnage registered increased by 3.79 million GT, an increase of 15.79% over the previous policy year. In the 2010 policy year, 207 ships, totalling 7.02 million GT, were newly joined in the Association, among which 95 ships, totalling 4.27 million GT, were newbuildings, accounting for 61% of the newly entered tonnage.<sup>128</sup>

The legal and management infrastructure of CPI is very similar to the IG P & I Clubs located in Britain and Scandinavia. According to its statutes (by-laws) and rules, the general membership and Board of Directors are the governing bodies of the Institution.<sup>129</sup>

#### 4.2.2 Coverage and Relations

##### 4.2.2.1 Coverage

As the majority of clubs, CPI covers its members for similar liabilities towards third parties for loss and damage of goods (cargo), injury, illness or the loss of life of

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<sup>127</sup> Read more <http://www.cpiweb.org/> last visit: 04.09.2012

<sup>128</sup> CPI Annual Report 2010

<sup>129</sup> Bye-law rule:34

the crew or passengers, oil pollution damages, collision liability, fines, and wreck removals.<sup>130</sup>

#### 4.2.2.2 Relation with IG

The CPI has a co-operation with the international P & I society as a co-insurance provider association for their members. Although the CPI is not a member of the pooling agreement, coverage by the CPI is, in principle, identical to that provided by a pool club regarding both scope and limits. CPI maintains close relations with some dominant clubs of the pool through an agreement of co-insurance.

#### 4.2.2.3 Relation with Hull Insurance

Mutual Hull cover is also offered to its members for reducing costs and to fully protect their interests, and the scope of coverage is similar to the related international insurance clauses.<sup>131</sup> As already mentioned in chapter three, providing members both HM (Hull and Machinery) and P&I insurance together is giving unique advantage to the shipowner for resolving all possible claim challenges. In this respect, CPI has mutual hull cover as well.

Additionally, FD&D coverage and Time Charterers Liability cover are being offered to members as well.

#### 4.2.3 Correspondent Network

CPI reported that it has built up a global network of correspondents reaching a number of about 200, covering all major ports in the world in 2011. Having understood the important role of correspondents, CPI has established a strong network of correspondents from the beginning of its foundation.

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<sup>130</sup> CPI Rule Book. Rule:3

<sup>131</sup> <http://www.cpiweb.org/> last visit: 05.09.2012

## 4.2.4 Claims Handling

### 4.2.4.1 Service

The claims services are centralized at the headquarters in Beijing with managers, executives and support staff, divided into three divisions. Corresponding to the management union is the headquarters. There are two representative offices and a designated service company with claims processing teams based in Dalian, Shanghai and Hong Kong taking care of local members there.

### 4.2.4.2 Additional Services

CPI has served to assist its members with FD & D services, drafting of contract terms, and advisory services. Other loss prevention services are required by individual members for financial safety. One of the most important services for members is to ensure continuous financial safety during arrest of ships or detention in the port in any condition. Shipowners hope to expect continuous trade with minimum cost conditions from their insurers.

### 4.2.4.3 Letters of Guarantee

According to a CPI declaration, currently, a letter of guarantee from the CPI is not only one of the three officially accepted forms of security by the Supreme Court of China, but it is also accepted by many government agencies and different applicants around the world. In case of difficulty of CPI, co-insurance Clubs are also ready to help by providing a pool member letter of guarantee. In addition, the CPI has an agreement with the financial guarantee from the Bank of China, Bank National de Paris (BNP) in France and other facilities with bond insurers, reputable local or other financial institutions in Hong Kong, the Philippines and Singapore. All of these security measures have proven effective and fast when needed.<sup>132</sup>

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<sup>132</sup> <http://www.cpiweb.org/> last visit: 05.09.2012

Having effective letters of guarantee is of vital importance for the P&I institution members or clients for protecting their trade. Every P&I institution has to have effective letters of guarantee to cover safe trading lines for their members/clients.

#### 4.2.5 Advantages of Being a Local Institution

It has to be easy to resolve problems for CPI, because it is the only local P & I Club in mainland China. The CPI can make use of its benefits and privileges as the location advantages to its members for offering lower cost services, such as a lawyer in the internal courts, who is legally approved to release arrested ships immediately. All those related advantages are not only existing for the CPI, but are also real for all substantial national P&I institutions.

#### 4.2.6 Management Team

As mentioned before, realizing that only a good management team can guarantee an acceptable service quality, the P&I institutions have always focused on training staff for keeping them dynamic. When the CPI management board members' background was checked, it was discovered that it is now being managed by a team of managers and staff who have expertise in law, insurance, accounting and seamanship. Some of them have acquired qualification as claims proficient and / or proficiency in maritime law in British universities, and many of them have undergone training in the P & I Clubs and London-based international law firms abroad.

They all have well educated backgrounds and impressive market experiences. Qualification of management team is very important for members because of cost efficiency. This criteria has to be the minimum level for a national P&I institution setting up business.

#### 4.2.7 Current Situation of CPI

CPI stated that underwriting work has made significant progress since the 2010 policy year. The volume of tonnage entered has maintained a high growth rate.

Due to a flat shipping market, competition in the insurance market has become more severe. In such circumstances, the Institution still maintains an increase in entered tonnage, due to the high quality of service, solid financial position and the competitive price the institution has offered for the past 10 years. These factors have gained wide recognition among the majority of Chinese shipowners.<sup>133</sup>

It is clearly understandable from the annual report of CPI that in aspects of underwriting and marketing, the CPI has done extensive work in research, screening, promotion and evaluation. To ensure the quality of members, the Institution demanded from each new applicant to observe their operations, and explain the rules to themselves.

It is interesting to note that despite a tonnage of only 28 million GT in 2011 (slightly smaller than the Swedish Club had at the same time), free reserves of the club were at a record of 686.2 million dollars. Only seven clubs in the International Group of P & I Clubs have free reserves greater than this figure. The total assets were \$ 723 million in 2011.<sup>134</sup>

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<sup>133</sup> [http://www.cpiweb.org/en\\_gongzuohuibao/annalsindex.jsp](http://www.cpiweb.org/en_gongzuohuibao/annalsindex.jsp) read more from annual report 2012 last visit 01.09.2012

<sup>134</sup> Read more: [http://www.cpiweb.org/cpien\\_index.jsp](http://www.cpiweb.org/cpien_index.jsp) last visit: 01.09.2012

## 4.3 Korea P&I Club

### 4.3.1 Overall Status

The Korea P & I Club was established on January 26, 2000 in order to provide reliable P & I insurance to support the Korean shipowners in accordance with the Shipowners' Mutual Insurance Associations Act of 1999.

Principal owners, such as Hanjin, began to enter in the club in 2005, and co-insurance with the IG clubs started. Entered tonnages passed 1 million GT in that year. Only three years later, in 2008, tonnage had reached more than 5 million GT.<sup>135</sup>

Since 2011, the Korea P & I Club has an independent club offering P & I coverage limits up to \$ 300 million. Members of the Korea P & I Club are Hanjin, Hyundai Merchant Marine, STX PanOcean, SK Shipping, Chang Myung, Korea Line, Korea Shipping, Sinokor, Pan Korea Line and Boyang.<sup>136</sup>

### 4.3.2 Coverage and Relations

#### 4.3.2.1 Coverage

The KP&I has the same principles of coverage as found in international P&I insurance law and practice.

#### 4.3.2.2 Relations with IG

The Korea P & I Club also has aimed to attract larger vessels through a new experience by sharing coinsurance agreements with a common IG body. It already has a co-insurance with IG, but this is based on the Korea P & I Club taking the first part of each loss, with higher cost incidents being covered by its partners. But this

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<sup>135</sup> <http://www.kpiclub.or.kr/eng/About/history.htm> last visit: 03.09.2012

<sup>136</sup> OMNI 2011 annual P&I report, page 47???

quasi-free structure could be supported by a system between the Korean Club and IG each taking a specific percentage of risk.<sup>137</sup>

#### 4.3.2.3 Relations with Hull Insurance

As reported by Trade Winds (2011), the Korea P & I Club, founded ten years ago, aims to become a much larger, more international club as part of a "Vision 2020" strategy. However, KP & I did not yet intend to enter the market of the hull insurance according to its strategic planning.

#### 4.3.3 Correspondent Network

The Korea P & I Club has an extensive network in the world ports and Korea P & I Club is suggesting to its members and captains to seek advice and assistance from the Club's correspondents on the list published by the Club, when they are in trouble or facing unexpected difficulties.

The KP&I Club maintains a worldwide network of surveyors and correspondents who have different experiences in claims management. When the vessels of the club members are arrested in any country because of cargo claims, collisions, and oil pollution, correspondents may still be available to assist members, as in the case with IG rules. Currently, the KP&I club has about 590 correspondents in all major ports around the world and can provide corresponding services from neighbouring ports if there are no designated contact points in any specific port. Principally, the Club prefers to work with a local correspondent who always tries to provide faster and better service with full knowledge of local laws and excellent experience.<sup>138</sup>

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<sup>137</sup> Trade winds, 28.10.10, Korea P&I Club aims to double tonnage by 2020

<sup>138</sup> <http://www.kpiclub.or.kr/eng/Services/claim.htm> last visit: 04.09.2012

#### 4.3.4 Claims Handling

##### 4.3.4.1 Service

According to the Club policies, when accidents happen, a claim team provides a fast interest in order to protect the interests of club members, including the appointment of experienced surveyors to determine the cause and extent of damages. In addition, if necessary, the claims team appoints a competent lawyer who has experience in the initial phase. To provide timely legal services, KP&I Club has a legal consultant contract with three law firms named Choi&Kim, Yoon&Yang and Kim&Chang. In addition, the club has potential to appoint other firms depending on the nature of claims or incidents. In cases abroad, the Club has contacts to appoint surveyors and lawyers through its local correspondents to protect the interests of club members. KP&I is known for its claims team providing faster action and better services to protect the interests of members in the market.

##### 4.3.4.2 Additional Services

Korea P & I Club has intended to expand into areas such as freight, demurrage and defence, and time charterers responsibility. It aims to move from being a fixed premium provider to a mutual insurer, but as already mentioned, it did not intend to enter the market of the hull insurance.<sup>139</sup>

##### 4.3.4.3 Letters of Guarantee

The previous information lead to one strong reality about KP&I that it really has a strong financial structure and growth capacity. KP&I's renewal results for 2012 with the expansion of the limits of cover up to 10 billion dollars and strengthening its ability to issue a letter of guarantee to attract larger vessels in overseas trades shows the entry of large shipping companies and overseas fleets is on the right track. The

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<sup>139</sup> Trade winds 01.11.2010 Korea P&I Club hoping to land new quote-share deal



renewal result will be a driving force for the development and continuous motivation of the Korea P & I Club to expert growth for years to come.<sup>140</sup>

#### 4.3.5 Advantages of Being a Local Institution

Korea P&I club managing director BS Park says the message from owners is that they want a local, Korean language P&I because of easy communication, but they also want to see the same limits in KP&I like the group clubs offer.<sup>141</sup>

The advantages of using local language have been mentioned previously in this dissertation.

#### 4.3.6 Management Team

The staff are employed by the Club. However, the CEO, responsible for the overall management and operation of the Club (executive management director) is elected through open competition.<sup>142</sup>

All of the managers and experts are well educated and have strong market experience in maritime law and/or claims assessment.

#### 4.3.7 Current Situation of Korea P&I

The Club is independent and is owned and operated by the ship-owners (members) and Ship-owners' Association. Principally based on non-profit making and non-corporate tax paying, it is operated as a special organization, to some extent sovereign guaranteed and underwritten by the Republic of Korea. The Club has to report certain important matters to the Ministry of Transport and is also subject to regular auditing by the National Financial Agency Service. Like other insurance

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<sup>140</sup> Trade winds 28.10.10 Korea P&I Club aims to double tonnage by 2020

<sup>141</sup> Trade winds, 01.11.2010 Korea P&I Club hoping to land new quote-share deal

<sup>142</sup> Email interview between Korea P&I management CEO Mr. B.S.PARK 11.09.2012

companies and banks in which the Government put some amounts of funding as key start-up capital (without possession of any share or shareholder rights by the Government), the Korean government gave some start-up capital for KP&I. The major part of KP&I's reinsurance is placed at Lloyd <sup>143</sup>

Korea P & I lists among its main benefits the lack of language barrier and time difference. As a non-profit organization focused on Korea, KP & I is not directed by commercial managers; therefore, the Club says it can offer more competitive call rates than other clubs. <sup>144</sup>

The Club's approximate total levy of premium is around \$ 30 million in 2012, which is \$4 million more than the previous year. The Club' free reserves rose more than expected to \$ 18 million, about \$ 6 million more than at the year of 2010. Currently, Korea P & I Club covers about 870 ships with around 10 million GT (one million GT more than in the previous year). Plans for the future are even more aggressive, with tonnage objectives for 2020 being 20 million GT and around \$ 100 million for premium. <sup>145</sup>

#### 4.4 Japan P&I Club

The Japan P&I Club has long been the only Asian representative within the IG. <sup>146</sup> The Japan P & I Club is the only organization in Japan underwriting P & I insurance for oceangoing vessels and Japanese coastal vessels. It was founded on October 2, 1950 in accordance with the Shipowners' Mutual Insurance Association Law. The Japan P&I Club became a member of the International Group of P & I Clubs in 1976 and joined the other clubs in the pooling agreement of the

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<sup>143</sup> Ibid, interview

<sup>144</sup> Asian maritime march april 2011 KOREA P&I BOOST ASIAN PROTECTION MUSCLE

<sup>145</sup> Trade winds, 09.03.2011, Korea P&I Club expands by 20% in a year

<sup>146</sup> Asian maritime, march april 2011, KOREA P&I BOOST ASIAN PROTECTION MUSCLE

International Group of P & I Clubs in 1989. The Japan P & I Club celebrated its 60th anniversary in October 2010.<sup>147</sup>

This club is already part of the IG, which is why it will not be discussed in details in this study.

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<sup>147</sup> Read more: [http://www.piclub.or.jp/E\\_rep/gaiyo/gaiyo.html](http://www.piclub.or.jp/E_rep/gaiyo/gaiyo.html) last visit: 14.09.2012

## CHAPTER 5

### 5 Club Insurance Applications in Turkey

#### 5.1 General

Today, many countries of the world have current clubs which have been established and operating in the market. Turkish shipowners, the state or foreign owners have not had an established P & I insurance club so far in Turkey. Therefore, the Turkish owners obtain their needs for liability insurance from clubs established overseas.

In this context, the Turkish shipowners generally prefer to procure club insurance from the British P&I clubs. The British clubs market is inflexible for Turkish shipowners in terms of small tonnage vessels which are under 10000 GT. The Turkish merchant fleet does not only have large vessels, but also small-tonnage vessels and those ships are not at all suited to the IG. The IG market has provided the same amounts of protection limits for all types of vessels without regard to particulars of the ship. However, some types of ships have different risk potentials, and never need the existing limits, which are provided by the IG Clubs. Having those limits is a part of the fixing of the premiums in Clubs' insurance policies. A ship may carry less risk than a floating platform, which has a high risk potential for environmental pollution, however, this related ship is insured to the upper limit at almost equal risk premiums. In short, some ships have high-risk and others have low-risk, but they pay nearly same premiums to purchase the same pool of P & I protection, which lead to injustice for small and medium sized vessels of Turkish shipowners.

Selection of the club for a Turkish shipowner is sometimes complicated and it is changed depending on various conditions. Sometimes there is not even any alternative choice for the shipowners. During the acceptance process of the club membership, the club will evaluate to ask for the premium with the possible potential

burden of risks, and when the club thinks that the candidate shipowner will bring a serious charge for club is financial body, in this case the club does not accept the application.

In fact, over the time, clubs have two different structures. The first group gathers lower limit risks and others collect high potential risks. Due to the structure of the non-profit clubs, competition between clubs may never be considered as existing, but they do compete with each other. However, a combination of competitiveness shows its face when low potential risks are collected in good volumes; they have fluctuating movements depending on the size of the damage. In this case, large and financially strong clubs can provide a wide range of covers and limits with lower premiums.

While shipowners in Turkey, with large tonnage and ships carrying less risk, prefer their ships to enter the British P&I clubs or other more powerful clubs; nevertheless due to the above-mentioned reasons, owners of small tonnage or having old ships are turning to some different alternatives. Consequently, they may select a fixed premium P&I insurer or have to enter clubs which are asking high premiums with limited covers.

Some of those fixed premium insurers are notorious institutions working with inadequate capability to handle damage claims. These companies are not preferred by the owners, especially due to their bad reputation of compensation payments.

Particular club insurance, which is asked from the maritime authorities of certain countries to have club insurance on board, has to be provided by accepted P&I club list. Authorities in some countries have accepted the insurance certificates with a "reputable club list" due to the sheer fact like Singapore and Turkey.

## 5.2 Turkish Merchant Marine Fleet

### 5.2.1 The position of Turkish merchant fleet within the world fleet

In 2011 the Turkish merchant marine fleet tonnage under foreign flags amounted to around 12 million DWT. As of 1 January 2011, vessels of 1000 GRT and above, the total tonnage of Turkish shipowners, both under Turkish flag and foreign flags, reached 19.6 million DWT. (Table 1)

As of the beginning of 2011, regarding the Turkish shipowners' ships of 1000 GRT and above, around 40% percent of these ships were registered under the Turkish flag and 60% were registered under foreign flags (Table 1).<sup>148</sup>

At the end of 2011, Turkish registered ships alone reached a number of 1245 ships and a total tonnage of 9,7 million DWT with an average age of 21.<sup>149</sup> The tonnage area of 0-1000 DWT of the Turkish fleet registered mostly fishing vessels, fishing boats and pleasure yachts.

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<sup>148</sup> <http://www.denizticaretodasi.org/DetoPortallng/Default.aspx?tabid=567> last visit: 18.09.2012

<sup>149</sup> Source: statistics of General Directorate of Merchant Marine  
<http://www.denizcilik.gov.tr/dm/istatistikler/Resmilstatistikler/> last visit: 19.09.2012

Table 1:

**Turkish Ships Under the National Flag and Foreign Flags**

Years	(1000 GRT and Over)						Total Fleet Controlled	
	National Flag			Foreign Flag			No	1000 DWT
	No	1000 DWT	%	No	1000 DWT	%		
1998	427	8,349	95,82	35	364	4,18	462	8,713
1999	448	8,697	90,48	69	915	9,52	517	9,612
2000	456	8,269	90,63	96	855	9,37	552	9,124
2001	445	7,321	82	107	1,607	18	552	8,928
2002	451	7,815	83,77	117	1,514	16,23	568	9,329
2003	432	7,045	79,9	147	1,772	20,1	579	8,817
2004	408	6,556	75,23	163	2,159	24,77	571	8,715
2005	420	6,427	70,23	237	2,725	29,77	657	9,152
2006	432	6,844	65,47	353	3,609	34,53	785	10,453
2007	446	6,464	58,16	424	4650	41,84	870	11,114
2008	490	6,592	50	513	6,591	50	1003	13,183
2009	520	6,736	43,9	636	8,592	56,2	1,156	15,328
2010	560	7,246	42,1	665	9,954	57,9	1,225	17,201
2011	547	7.797	39.7	672	11.863	60.3	1.219	19.660

*Source : ISL January-February 2011*

5.2.2 The position of the Turkish merchant fleet compared to the fleets of the neighbouring countries (Table 2 (National Registry data))

The capacity of the Turkish merchant fleets and the neighbouring countries is shown in Table 2. Greece is in the first place being among the three largest merchant fleets of the world, and Turkey is in the third place in this region.

Table 2:

**Turkish Merchant Fleet and the Neighboring Countries (01.01 2011)**  
*(300 grt and over)*

World dwt rank	Country	No	1000 DWT	World Share %	Change Rate %
5	Greece	1.106	71.268	5,30%	5,10%
11	S.Cyprus	843	32.200	2,40%	2,30%
24	Turkey	928	8.646	0,80%	0,70%
30	Russia	1.326	6.225	0,50%	3,30%
49	Egypt	99	1.452	0,10%	5,10%
59	Iran	245	1.178	0,10%	-14,50%
72	Ukrania	178	676	0,10%	-9,00%
75	Bulgaria	45	618	0,00%	-10,00%
88	Syria	35	268	0,00%	-26,40%
96	Romania	29	159	0,00%	0,00%
119	Iraq	2	27	0,00%	-77,80%

*Source : ISL January-February 2011*

The number and tonnage of the ships in Turkey are adequate for implementing a national P & I institution when comparing this potential with the countries in the region. This club may be not only national, it may also provide the potential for the regional demands. This situation can be acceptable as a substantial size in terms of club insurance. However, the quality of members as much as quantity of members, is also important for club insurance. The majority of the Turkish merchant marine vessels are small and old. According to data, the average age of the Turkish merchant fleet was 21 years in 2011.<sup>150</sup> In 1999, this figure was

<sup>150</sup> Ibid, last visit: 24.09.2012



considered to be 17. Merchant marine fleet renewals and reconstructions have become a necessity.

Due to, the above-mentioned reasons, having P & I insurance is becoming problematic for the Turkish shipowners. However, it is worse because shipowners are prevented from gathering intelligence to verify the existing problems in the maritime sector. There is another reality why some shipowners have insurance which is only because it is mandatory and because of the legislation.

Therefore, to know whether they purchase sufficient protection for a paid premium is also not possible.

### 5.3 Mutual and P&I Club Insurance Regulations in Turkey

In Turkey, due to the absence of a P & I club, current legislation does not cover to explain specifically the club insurance. Insurance risks, which are covered by a club, are all referred to the in Turkish Commercial Code (TTK) as marine risks in general. However, in this code, the club insurance terms, and limits, are not specifically determined. These insurance coverage areas are already mentioned as extremely large insurance covers.

Insurance Law No. 5684 permits procurement of "vessels liability insurance" from abroad. This indication is understood to be a provision related to P&I insurance. However, at the moment there are not any available arrangements in legislation about defining P&I insurance, explaining insurance limits and determining solutions to problems that may arise due to carrying out insurance business outside the country.

Although P&I insurance is not regulated specifically in national law, in recent years, it has been entered into legislation as a necessity due to the impact of international agreements. The following arrangements are examples in this regard:

□ In Penal regulation of Article 21 of the Environment Code, it is expressed that, after any pollution incidents in Turkish waters, vessels are responsible to pay

administrative fines. A letter of guarantee given by a P&I insurer is acceptable for previous payments for releasing the detained ship.

□ Regulation on The law of Development of Maritime Trade Fleet and Promotion of the Ship Building Facilities has an Article, namely "Obligations of Insurance and Class". Ships are imported under this regulation, and have to have a P&I insurance certificate on board. This P&I insurer should be an acceptable P&I insurer for the Turkish Maritime Administration.

□ There is a regulation on the requirement to obtain insurance cover for vessels against maritime claims and supervision thereof since July, 2011. The purpose of this regulation is to set out the obligations and requirements of vessels flying the Turkish flag. Vessels, regardless of the flag state, arriving in or sailing out of ports, terminals, anchorages and other port facilities in Turkish territorial waters, must obtain insurance cover against maritime claims and to establish policies and procedures for their supervision.

□ Turkey is part of the Civil Liability Convention 1992 (CLC 92). In the Regulation of Issuing CLC 92 Certificates, identified ships are obliged to undertake, in accordance with arrange CLC-92 certificate from IG clubs, or the club has to be on the Turkish Maritime Administration determined clubs list.

□ The Turkish Straits Maritime Traffic Regulations Application Instructions include another application for P&I. In Article 12 of this Directive, the ship cannot pass through the Turkish straits without having P&I club insurance corresponding to the requirements laid down.

As can be seen, an insurance type is undefined in the legislation of Turkey; however, the same legislation requires it under certain circumstances.

#### 5.4 Problems about Club Insurance in Turkey

It has already been mentioned about the problems of the shipowners not finding appropriate insurance from the market and paying higher premiums for P&I insurance applications in Turkey. P&I Insurance awareness has started to develop in the Turkish maritime industry in short time period. The clubs having a very wide discretion to indemnify claims is known in the market. Claims traffic is not the main factor for processing how to use the discretion of the clubs, it is the members' condition.

Therefore, to be strong in the eyes of the club, owners have to defend their rights against the club. It is essential for an efficient utilization of insurance. This can be performed by Turkish shipowners by working existing together and being involved in management of the certain clubs.

Perhaps recognition of the right in the Turkish courts to directly sue based on possible unfair behaviour of the clubs may be a solution. However, the recognition of the right to directly sue may also have a negative impact. It has led to increased premium rates for Turkish owners at the same time. This situation may cause them to exit from the Turkish registry to foreign flag quickly.<sup>151</sup>

However, there may be no legislation about pleading right against clubs in the Turkish courts now. This is definitely recognized, especially with regard to third parties damage, but not in terms of shipowner. Otherwise, the sense of justice is incompatible with waiting and following of the injured third party pleading against the club where the club is located.

#### 5.5 Inquiry Study

Regarding the determination of the maritime sector's attention for the establishment of a local P&I insurance club by the Turkish maritime administration,

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<sup>151</sup> Acar, Supra 2009

an inquiry was carried out with maritime and insurance industry representatives to measure the club expectations in the two sectors.

In the related inquiry, 26 Turkish flag shipowners participated. Questions were asked about shipowners' insurance problems in the survey area of their current clubs and dimensions about a local club. The shipowners which answered the questionnaire/inquiry were a large proportion of having a say in the maritime sector.

- Are you satisfied to run with your current P&I insurer club?

The question was addressed to shipowners to observe if they were satisfied to run with their current P & I insurance clubs. Three of the 26 owners expressed they were very satisfied, 14 of them stated they were satisfied, six of them revealed some problems, and three of them were dissatisfied with their current P&I clubs. Here, 35% of participant shipowners were dissatisfied with their current clubs. Even such a rate a strong representation of ship owners group means that there is actually quite a high rate of dissatisfaction with their current clubs in the maritime sector.

- How do you communicate with your current club?

When shipowners were addressed the question of communication capability with their clubs, 20 participants replied; "I'm communicating through correspondents", 6 participants said; "I'm having a direct connection to my club". The means of shipowners' communications with P&I insurers are largely being provided by the correspondents in Turkey. It was also asked how club communications were in terms of the activities of correspondents. In this respect the response was largely positive. Only one shipowner could not communicate at all, and two of them said 'communication is bad'. It is clearly understandable that correspondents' activities are strong enough to be greatly enhanced in Turkey. Yet another result is, Turkey has qualified human sources for P&I insurance to satisfy operation of P&I institution.

- What is the most important factor affecting the choice of your club?

17 shipowners responded to this question that the most important factor was attention to the club's financial position, and five members stated that the club's prestige was important. As can be seen, prestige in the sector and financial structure of the club are important for a large proportion of shipowners. The club must have sufficient financial strength to compensate the claims for compensation. The prestige of the club is related to the nature of providing financial security of the club. There is special importance of these points where it is necessary to provide a letter of guarantee. In fact, here the shipowners are seen to expect a financially strong and reputable structure in the event of the establishment of the Turkish club. Even if the financial situation criteria can be achieved quickly, the prestige gain of the club is a phenomenon that takes a period of time. Therefore, it can be expected that the Turkish shipowners would stay out of the local club for a long time.

- When the Turkish club is established, would you join this club?

In this context, the shipowners were asked for their attitudes about what they intend to do when a local P&I club is established. The majority of shipowners (20 shipowners) stated that if the conditions were appropriate, they may regard a local club positively. Only three participants expressed unconditionally that they would be included. However, three other shipowners stated that they would adopt a course of action corresponding to the attitude of the rest of the industry.

It is understandable that shipowners engaged in maritime trade are thinking of their short-term commercial interests, so the fact that there is a suspicious approach to a new club can be acceptable. The shipowners were stating as a main concern for not participating in a local club that it will take time to acquire market prestige for the new club, and they may think that they could find themselves in difficult situations in this process.

- Is the government support needed for the establishment of the Turkish club?

As for governmental support for establishment of the club is necessary or not, 17 shipowners answered that state funding must be found, at least in the setting up of

the organization. Nine members stated that a club can be established with the maritime sector's own efforts and at all stages without state support.

Shipowners largely believe that the Turkish P&I club cannot be established without support of the State. Structured as a mutual shipowners' club, such an institution takes decisions on premiums to be paid as well as which damage claims to be paid together.

## 5.6 Case Study

### 5.6.1. What is the logic of P&I Clubs? How do they operate?

5.6.1.1. P&I insurance is an indemnity insurance, to indemnify owners for the liabilities. It provides a very comprehensive coverage for loss claims of third parties related to the operation of the ship. Claims include cargo damages, crew demands, collision, wreck removal and pollution.

5.6.1.2. It is traditionally executed by cooperative type organizations named as 'clubs' as mutual insurance.

Each insuree is the member of the provider club and has voting rights depending on the tonnage and can be selected for the executive board of the club. Clubs do not provide insurance to make profit. On the contrary, in order not to pay higher premiums to the insurance companies seeking profit, they work to provide insurance coverage that they would obtain from them at cost. Claims ruled to the members as a result of the lawsuits of the third parties are paid from the club safe deposit box; then these monies are shared among the members as 'contribution margin'. Contribution margin is something like premium, but the amount is not known in advance; it changes according to the accounts of that year.

5.6.1.3. The 13 largest P&I clubs of the world are based in London under the name of the International Group of P&I Clubs. The majority of these clubs, which have been operating for 100-150 years, are English.

The most important duty of the IG is to provide reinsurance from the Llyod's market and big reinsurance companies for all of the clubs with a single contract. Thus, it significantly decreases reinsurance costs of the clubs. This decreases the contributions collected from the club members. The 13 clubs have collected premium amounting to 2 billion USD per year by the end of 2007.

5.6.1.4. There are some insurance companies that provide the same coverage for fixed premium and with known methods in the P&I market. There are big insurance companies behind some of those but the financial power of some is not clear. These companies generally insure ships that are not in demand by big clubs; furthermore they make use of dissatisfaction against big clubs. The coverage is generally more restricted, due to the amount limit. As it does not bring profit, none of those companies have a long history in P&I market.

5.6.2. What advantages does a Turkish P&I Club bring to whom?

For the Insurance Sector

5.6.2.1. It is hard to gain advantage directly because of the following:

i. If the club will be a mutual pool, it will aim to decrease the insurance cost of the providers, not to gain profit. It will provide insurance at cost but not profit.

ii. If the club is a fixed premium insurer, it will either not profit or have a little profit. Otherwise, it cannot compete with the big clubs. However, it can gain profit in the sector of other fixed premium insurers (ships with smaller tonnages and/or standards).

For the Shipping Sector

5.6.2.2. There is no direct advantage at first sight of the club being Turkish, because ship owners prioritize their expectations, instead of being nationalistic in selecting the club. (See Par. 5.6.3.1).

If a foreign club meets these expectations, they do not hesitate to prefer that club.

5.6.2.3. On the other hand, explaining to a Turkish club and achieving the demands can be easier for Turkish ship owners. Because, the clubs have such discretionary powers to fulfill these demands that can not be seen in other types of insurance.

It is a very important issue to search how satisfied Turkish ship owners are with the services of the foreign clubs.

For the Law Sector

5.6.2.4. A policy should be followed imposing the claims handling of the Turkish club to be established in Turkey as far as possible. If so:

- i. Legal accumulation regarding maritime law and insurance in Turkey gets richer.
- ii. Turkish Corporate Arbitration gets stronger.
- iii. Turkish attorneys get stronger.

5.6.3. What are the challenges to face in establishing and operating a Turkish P&I Club?

5.6.3.1. A club that does not meet the following two requirements will not have competitive power:

- i. Low prices (contribution - premium), and
- ii. Quality of services (claims handling - letter of commitment).

Low Prices

5.6.3.2. If the club will be a mutual pool, the ships within the scope of the pool will be much less than the international clubs, and collected contributions can



be inconsistent. Compared to the big clubs, in some years much less contribution can be collected, but in some years, it can be necessary to collect more.

5.6.3.3. If the club will be a fixed premium insurer, Turkish insurance companies can be reluctant to invest their funds in a field that does not bring any or only little profit.

5.6.3.4. Reinsurance is highly important for both a mutual pool and a fixed premium insurer. This should be provided from abroad. Reinsurance will be purchased more expensively when compared to the big clubs and many fixed premium insurers. This is a factor creating an impact which is challenging for raising the prices and decreasing the competitive power of the club to be established.

#### Quality of service (claims handling - letter of commitment)

5.6.3.5. A club that is not able to give a world-wide, high quality claims handling service does not benefit the ship owners. Besides, how cheaply the claims of the third parties (cargo damage, collision .) are handled affects the price of the insurance. Handling the claims cheaply or expensively depends on the professionalism of the central claims office of the club and the correspondents.

5.6.3.6. Claims are handled with the help of commercial correspondents who should be responsible for duties like survey and legal correspondents who should be responsible for things like litigation.

Therefore, there is a necessity for a correspondent network ready to serve in each of the important ports of the world. Regarding this, it can be considered to make contracts with the correspondents existing in the current network of the big clubs; however, it should not be more expensive to get service from them.

5.6.3.7. As the third parties have the ship arrested as being the first thing in case of any kind of disputes, a guarantee should be provided to release the ship. Both the third parties and the courts accept letters of undertaking (LOU), depending on the reputation of the club. This reputation is gained through recognition of the club and

rating scores. If the letter is rejected, the club or the ship owner can receive a letters of guarantee from a bank in that country in order to provide a counter guarantee. Bank commissions can be an important item playing a role in the rise in the prices. Regarding this, cooperation with one of the biggest clubs can be achieved. Letters of Undertaking issued by the national P & I provider would probably be more easily accepted in other countries if they were guaranteed by the government. Governmental guarantees always have stronger backing than bank guarantees.

#### 5.6.4. What to do, and what not to do?

What to do?

5.6.4.1. Big ship owners should be willing to participate in administrative functions of the clubs. Here is the place for real influence in every kind of relationship between the club and the ship owner (insurer and insured). This should make limitless contribution indirectly to both that ship owner and the Turkish shipping sector. Ship owners can have themselves selected to the administrative council by collecting the votes of the other ship owners with a proxy method, even if their own marine fleet is not sufficient.

5.6.4.2. In order to establish a Turkish club, creating a pool insuring the ships with government funds can be a correct point to start. İDO is a good example because of the sailing area of the company ships. They are sailing in cabotage. Instead of having these insured under the big clubs, ensuring only reinsurance from those big clubs can be cheaper. It can be understood that whether it is the case or not, through a cost benefit analysis performed by using retroactive premium and indemnity records, the scope of the pool can be expanded with the participation of other big fleets.

5.6.4.3. High quality with low prices depends on the quality of the management. In the establishment of a P&I institution, it is inevitable to have a professional management. This contains technical specialty and good relations. Fund

management, reinsurance regulations, claims handling and marketing are among the management tasks. Although it is unnecessary to be conservative about foreign management, it is fair to consider that as a transition period to train local staff.

5.6.4.4. For a Turkish club to be established, providing convenience in the subjects like corporate tax, and benefiting from the funds can affect the competitive power, as it will decrease the cost and the price. As duties are currently not collected in this field, because Turkish ship owners are still provided insurance from foreign clubs, such a convenience will not decrease the state's tax incomes.

What not to do?

5.6.4.5 With an amendment in Insurance Law, including the club insurance in the scope of obligatory insurances, can make a positive contribution to the enhancement of Turkish clubs. However, this impact should not be as big as in the other insurance types. Furthermore, it is a slippery field requiring attention. If the Turkish club does not meet the requirements of Turkish ship owners (See Par. 5.6.3.1), escaping to foreign flags can start to get insurance from the foreign clubs which can lead to problems like lower tax incomes.

## CONCLUSION

1- It is seen that marine insurance track back to Roman Law before Christ and marine insurance contracts aiming to indemnify possible losses for a certain premium are encountered in the beginning of the 13th century in Italy.

Marine insurance law in Turkey is included in the fourth paragraph entitled “Insurances against maritime risks” (art. 1339-1459) of the 5th Book in the Turkish Commercial Code.

Marine insurances are described in Article 1339 of the Turkish Commercial Code as “Any person who has an interest measurable by money in experiencing maritime risks of the ship or cargo safely may insure this interest.” From the provision of the article, it is understood that interest and risks are the necessary factors for insurance. Maritime risks are any kind of risks related to a marine adventure. The one to suffer physical damage by being exposed to maritime risks can be defined as interest owner in terms of marine insurance.

Insurance contracts in Turkey are signed in compliance with the general conditions approved by the Undersecretariat of Treasury. There are two general conditions in place, 'Cargo Freight Insurance General Conditions' and 'Ship Policy', in the field of marine insurance. Another source for the contract in freight and hull insurance practice is the clauses prepared by the International Underwriting Association composing the content of the insurance contract.

Hull insurance is a marine insurance type covering a decrease of the ship owner in his/her property, likely to occur as a result of a damage or loss to the ship. In practice, hull insurance provides an insurance with a ratio of  $\frac{3}{4}$  in terms of collision liability, reasons taken in assurance coverage in the UK market. The upper limit of the protection provided by the hull insurance is the insurance value of the hull. The insurance value in hull insurance is the full value of the ship subject to the owner's interest. The insurer and insured can agree how to determine the value of ship in the contract and it usually is for a certain amount of money. If the ship value

is not determined in the contract, the value of the ship when the risk starts is taken as a basis.

2- P&I insurance is defined as an exceptional insurance contract in which a member ship owner insures liabilities and expenses against third parties not covered by hull insurance in accordance with mutual insurance principals. A member, the party of the club insurance contract, is the ship owner who secures indemnity for liabilities and expenses of his/her ship against third parties not covered by the hull insurance policy in return for the premium s/he has paid.

Club insurance is a mutual insurance. In this insurance, ship owners come together to secure their interests within the scope of the club insurance. Therefore, each of the ship owners composing the club gets member ships and deposits a certain 'premium' to the club to meet potential losses. Premiums collected at the beginning of policy year are directed to investment. On the other hand, at the end of the policy year, all loss cases are closed with the collected fund.

If the money collected in club fund is not enough to pay the losses, then the members are asked for additional premium. As the club does not seek profit, additional premium is only collected for such a case. Again, according to the case, if the collected premium is not used up despite paying for all losses, the club can put it in reserve or distribute it among the members.

Rights and liabilities of the club and members are determined in a deed of partnership and the Rule Book. Again, in the deed of partnership, there are conditions for acceptance of the member to the club, termination conditions of the membership and regulations related to management.

Clubs are separated into classes providing insurance cover with different features. The main categories of insurance that clubs provide are collected under classes of, Protection, (Indemnity), F.D.D ( Freight, Demurrage, & Defence), Strike and War.

The reinsurance provider of the club insurance is the International Group of P&I Clubs, which is an association consisting of the clubs providing club insurance. The basic purpose of this association is to share the risk that each club carries among the group members. Conditions related to this are regulated in the contract named Pool Agreement. Other than the reinsurance function of the International Group, the group has the function of representing its members in international platforms and providing information among its members.

In club insurance, the basic liability of the member is to pay premium. In mutual clubs, premium is the amount emerging as a result of sharing the claims losses, which the club has paid within the year for the members. Another responsibility of the member is to inform the club about the risk type. This responsibility can arise before the contract, during the contract and after the contract. Among the duties of the member towards the club, there are preventing losses from occurring, named protection measures, and taking necessary actions to prevent increasing losses after the damage occurs. The club is on the other hand, liable to the member for meeting the demands, paying the claims and providing financial security.

3- There has not been any P&I clubs established in Turkey until now. Therefore, Turkish ship owners meet their needs for P&I insurance from the clubs established abroad. Turkish owners get insurance mostly from English clubs. The English P&I club sector is a sector which is not flexible and in this sector insurance is maybe provided with a different amount for every kind of ship with considering the characteristics of the ship. However, as a result, ships with smaller tonnage have to purchase insurance in higher limits than their needs (by paying more premiums).

Whereas the owners of ships with greater tonnage and less risks among Turkish ship owners tend to register their ships in English clubs and other relatively stronger clubs, ship owners with smaller tonnage and old age, comprising the majority of the Turkish merchant marine fleet, prefer generally fixed premium insurers or the clubs less recognized worldwide. P&I insurance policies issued by

these clubs with bad reputation are not accepted in certain fields<sup>152</sup> per the list (recognized club list) published by the Turkish Maritime Administration, the authority for marine matters in Turkey. The clubs which appear on the aforesaid list are determined via evaluation reports published by international credit rating institutions on a yearly basis regarding the financial situation of the clubs and annotations prepared jointly by the Undersecretariat of Treasury and Turkish Maritime Administration using the credit ratings of the clubs. The Turkish Maritime Administration currently includes the clubs with the credit rating of "BBB" and above obtained from independent credit rating institutions.

Although there is not any legislation issued for P&I insurance, P&I insurance has entered into Turkish legislation as compulsory as a result of international conventions agreements in recent years. It is inevitable for this legislation to increase as environmental responsibilities expand. In relation to this development, the definition and scope of insurance type should be involved in the Turkish Commercial Code and the establishment type should be included in the Insurance Law in terms of a possible local club initiative. Actually, it is possible to establish a club cooperatively within the scope of the regulation in Article 3 of the Insurance Law no. 5684. However, the provision regarding the number of partners which cannot be below 200 in this article, is an obstacle for the establishment of a club according to the aforementioned article. The regulations to be made considering the structure and characteristics of the club in terms of establishment and operation should be included in this Law.

P&I insurance is not an existing insurance type in Turkey. This field, even in the insurance sector, is a field that very few correspondents have a grasp of. In direct proportion, many ship owners do not have enough knowledge of the characteristics of P&I insurance. The fact that ship owners do not have sufficient knowledge of the scope of the insurance coverage they purchase in return for the premiums they pay may result in paying higher premiums for the insurance not providing any claim

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<sup>152</sup> In club insurance required for ships bought within the scope of the credit received from abroad to obtaining CLC 92 certificate in terms of tankers and again per relevant legislation.

payment. One of the things which initially is necessary to do about this subject is to organize training activities in order to give information regarding P&I insurance by the Turkish Maritime Administration, maritime sector and even insurance sector. Especially, sharing the reports published by the clubs in renewal periods with the maritime sector at certain intervals will make the ship owners act more consciously. In order to ensure this sharing, it could be proper to create a committee where the representatives of the maritime sector are involved with the Chamber of Shipping. This will contribute to the shaping of the 'Recognized club list' published by the Turkish Maritime Administration that the problems faced in the field of P&I insurance are conveyed to this committee first and then to the Turkish Maritime Administration. At the same time, the work of this committee will give positive results in terms of directing the ship owners to certain clubs.

The fact that ship owners focus on certain clubs is important to show their strengths. This will have positive impacts on both the premiums to pay and indemnities to be recovered.

The opinion to establish a mutual club with the participation of Turkish ship owners is brought forward frequently by various interests in Turkey diversely. This is a well-intentioned opinion, yet hard to bring into action in a short time. A Turkish club to be established may provide knowledge accumulation and raise professionalism in this area. A Turkish club can be a national source of pride, providing guarantees abroad. However, establishment of a local club is not considered as a first solution to solve the problems related to the P&I insurance needs of the maritime sector in Turkey. Ship owners are highly reluctant to invest in establishing a local club.

Even if such a club is established with government funds or support, the ship owners are likely not to be involved in an organisation which is new, unknown and inexperienced. Yet, from the results of a questionnaire made by the Turkish Maritime Administration, it is understood that the ship owners will mostly approach a Turkish



club with caution (even though 35% of the ship owners who participated in the inquiry stated that they have problems with their clubs).

Some of the reasons for keeping the interested people away from a local club opinion are insufficient size of the Turkish merchant marine fleet, containing mostly old and small tonnage ships and low awareness of insurance in the sector.

Besides, there is not sufficient statistical data to allow for making proper analysis regarding what kind of a club to be established in the maritime sector can provide assurance. It should be ensured that a study should be started by the Turkish Maritime Administration to fulfil the need of data in question and at least, premium paid by the ships registered under TUGS to the clubs, their claims and damages recovered.

This is the case for mutual clubs, yet the issue can differ for fixed premium insurance. Fixed premium insurance is an activity which can be conducted by any of the insurance companies currently operating in Turkey. However, the work of the mutual clubs without profit making purpose will lead the ones desiring to do fixed premium insurance business to continue this activity with very low profits in terms of competition and the insurers will prefer to invest in the fields that bring more profits when they face a situation incompatible with the realities of life. However, an insurance company owned by government can provide club coverage with fixed premium insurance. A decision of a public authority in this direction will be enough to achieve that.

Particularly, the progress of this system may in time be followed by starting to provide P&I insurance coverage for the ships used in internal waters, ships owned by the government, sea busses and ferries. Such a structure will raise the knowledge level and will help to fill the deficiency of qualified manpower existing in Turkey in the field of P&I insurance. Furthermore, it will help fulfil the need for data to some extent.

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