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SHOULD INSOLVENCY RISK BE MUTUALISED?

Amendments to the Maritime Labour Convention 2006 designed to protect abandoned seafarers are due to enter force in early 2017. Some insurance intermediaries and commentators are predicting that the International Group of P&I Clubs could, and perhaps should, provide the necessary cover to enable shipowners to meet their enhanced MLC obligations. But, contrary to the impression circulating in some parts of the market, this is anything but a done deal. Mutualising the risk of financial insolvency is just one option to set alongside other initiatives from the commercial insurance market and /or other providers of financial security.

This would not be the first time, for example, that the IG has declined to intervene in contentious coverage issues, leaving owners instead to find alternate risk transfer solutions in the non-mutual market. Examples of recent abstentions include additional cover for piracy risks and OPA - Certificates of Financial Guarantee.

In the case of piracy, it was not deemed to be in the interests of public policy for the clubs to become involved in this 'modern-day' insurance requirement, whilst numerous arguments have also been raised against clubs becoming involved in underwriting any form of financial guarantee. In February last year, marine insurance broker Marsh reacted to the proposal by the Standard P&I Club to offer OPA COFRs directly to its members by arguing that the legal defences relied on by owners and their clubs could become blurred if the insurer covering the underlying risk was also the insurer providing the financial guarantee. Marsh questioned how certain the Standard Club could be that the distinction between itself as a COFR guarantor and its conventional role as a P&I insurer would be upheld in a contested court hearing.

It has long been the overarching view of the clubs that they should not offer financial guarantee insurance to their members. This is exemplified by one IG club which in 2001 issued a circular in connection with the International Guidelines to Flag States on Seafarer Abandonment, which had just been adopted. The circular provided the following advice to members; "Unfortunately the guidelines produced are not only of doubtful utility, they are also of doubtful practicality. The IG clubs have indicated that they would be unable to issue notifications to individual seafarers. In addition, they have pointed out that claims for liabilities to seafarers are always subject to club rules and terms of entry (including deductibles) and that payment could not therefore be guaranteed to individual seafarers. This means that IG clubs will not be able to issue the certificates envisaged in the guidelines."

The circular refers to the very same guidelines that have now been included almost verbatim into the Maritime Labour Convention and will come into force in early 2017.

So, aside from the mandatory nature of the forthcoming amendments, it is hard to see what has changed since 2001 which would now negate this particular club's former position on this matter of regulatory compliance. Why would the clubs abandon their position of not wanting to write COFR business, to now begin writing financial guarantee insurance in respect of abandonment risks as required under MLC 2006? Surely the same rationale should be applied to the latter type of risk as is applied to other categories of financial guarantee insurance? Surely the clubs face an insurmountable conflict of interest when balancing the interests of seafarers with those of their members?

Unlike the OPA COFR, is it a question of the perceived loss cost and realistic disaster scenarios (RDS) being manageable from the club's perspective? Most recently, in December last year, Marsh reportedly advocated that the clubs should pool liability for owner insolvency, warning that, "The payment of four months' wages to seafarers on even a 30-vessel fleet would exceed the $9m risk that individual clubs currently retain". If this is proven to be an accurate loss cost, then what cost would the clubs have to assign to their RDS calculations - all this coming at a time when clubs have the pressure of Solvency II to concern themselves with.

It follows that, if the clubs are to intervene in the case of seafarer abandonment, they must be willing to use the mutual funds of their solvent members to enable them to act as financial guarantors to cover the debts of their *in*solvent members. Moreover, as a matter of insurance law and MLC regulatory compliance, as it is the seafarers who have the 'insurable interest', mutual cover in respect of seafarer abandonment would involve the clubs granting their members' employees (the seafarers) direct access to the club's financial security. Direct access for seafarers would present an interesting claims management challenge for the clubs.

By mutualising the risk of financial insolvency, the industry risks tilting the playing field against well-founded, financially solvent shipowners who, at significant financial cost, employ best practice throughout their operations. Why should such operators assume liability for the debts of less-well-found competitors? And why should such a 'ticket to trade' be demoted to just another 'club benefit'?

Moreover, can seafarers who are utterly abandoned and in need of immediate relief truly rely on their employers' insurance clubs to overcome the obvious conflicts of interest involved in the mutual underwriting of such risks?

There is comparatively little time to reconcile these major issues and to deliver on the true intent of MLC to create a 'seafarer's bill of rights'. To provide a quick fix and engineer further regulatory mediocrity should not be an option.

The question is whether or not to mutualise financial insolvency. The answer is as yet unknown, and we should not presuppose an outcome which has yet to be decided. The real question that merits further discussion and clarity is whether mutualisation of this

risk is in the best interests of either shipowners or the seafarers they employ? Until we have clarity on this question from the IG, it will always present a barrier to new product innovation.