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Towage Liabilities – Am I Properly Covered? (An Overview of Protection and Indemnity Insurance for Tugowners made simple)

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SYNOPSIS

A potential threat arising from a declining freight market is that recognised towage conditions associated with the towage industry will be increasingly challenged. There are many aspects to towage that attract different risks and in turn different towage conditions such as harbour towage, ocean towage of rigs and platforms and offshore structures, river towage and salvage. What are your liabilities when performing these towage services? How can your P&I entry respond to the liabilities during a towage operation? Does the standard P&I entry cover you for these towage risks? And can different worldwide trading jurisdictions impact on your risks? What should you be looking out for and what experiences can be shared by the P&I industry?

INTRODUCTION

Sometimes, through complex legal jargon and an assumption that the audience will understand the technicalities of the subject, we can overcomplicate a topic. This appears to be an industry-wide issue and perhaps plans to introduce plain English into many documents will help... we will wait and see. Consequently this paper, which focuses on towage liabilities, is hopefully free of jargon and free of complicated case studies. It aims to clarify, in simple language, what your liabilities are as a tugowner, how your protection and indemnity (P&I) entry can respond and also tries to share some experiences gained from insuring the liabilities of tugowners.

THE CLUB

After almost 20 years at the Shipowners' P&I Club I have seen many changes when it comes to insuring

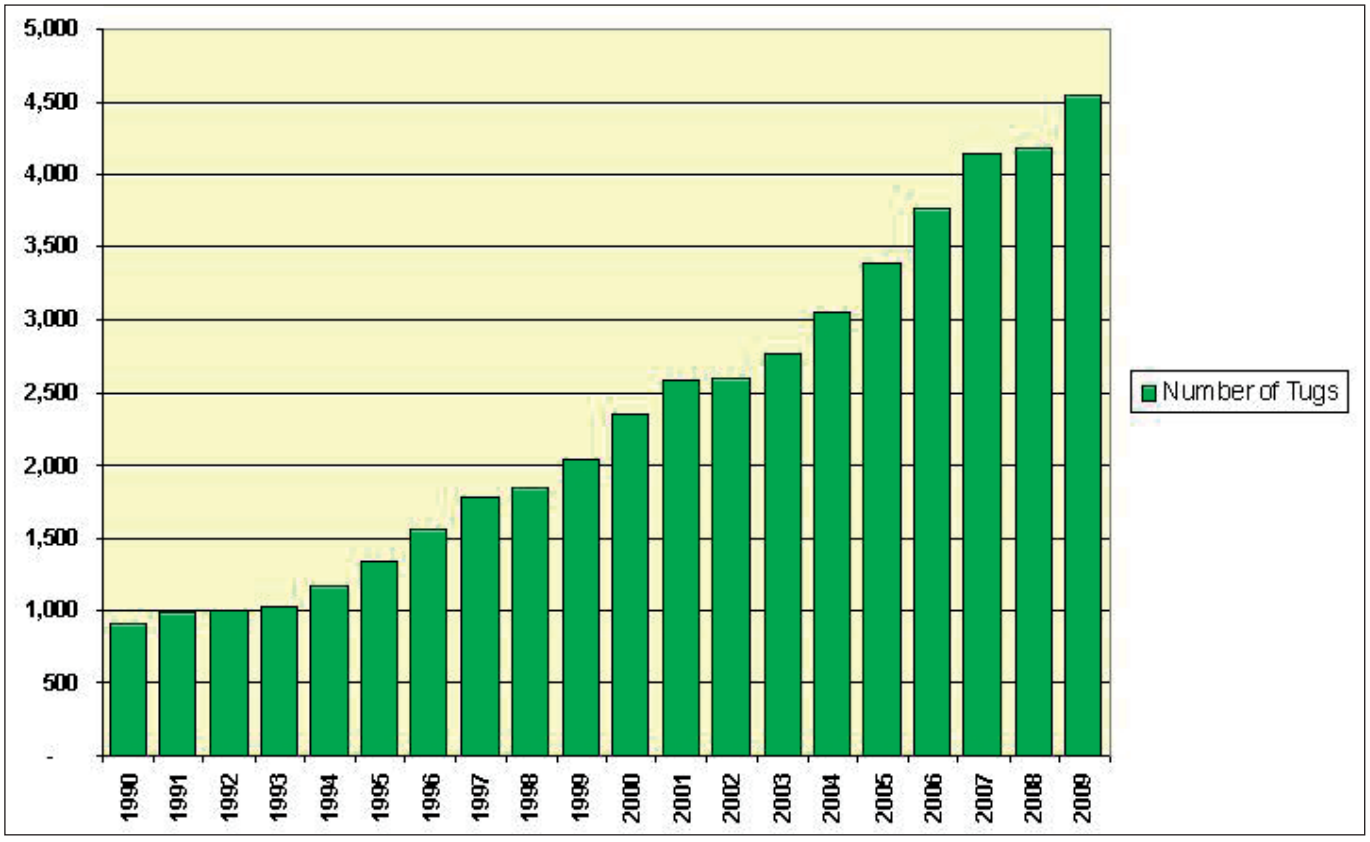

Figure 1: Increase in the number of tugs.

the legal and sometimes contractual liabilities of vessel owners and all too often the industry has the habit of overcomplicating the subject.

In 1990 the Club had approximately 10,000 vessels insured for P&I risks, of which 900 were from the towage and salvage industry. Today that number has grown significantly to more than 27,000 vessels, with more than 4,500 from the towage and salvage industry (*see Figure 1, previous page*).

But why the increase? I could suggest that we have done an exemplary marketing job – perhaps we have, although more than likely tugowners and their insurance brokers are becoming increasingly aware of the costly and sometimes complex nature of a vessel's liability. Instead of self-insurance, confident that exculpatory clauses in towage conditions minimise the exposure of a tugowner to any possible claim, owners are moving to an insurer who can structure a liability package to cover the varied operations of a tug.

All too often we are seeing that tried and tested conditions of towage and salvage are being challenged by charterers requiring vessel owners to assess their insurance provisions, which can lead to substantial increases in insurance premiums.

OUR STATISTICS

Let us start by looking at what is happening to the cost of liability claims. I am using 1991 as a start date for no other reason than personal choice, as this is when I was persuaded to move from the 'dark side' of the insurance industry, that of an insurance broker, to the role of a P&I Club underwriter.

The examples provided could relate just as easily to a small, singleton harbour tug or to a large offshore deep-sea tug forming part of a substantial fleet – your liabilities have changed and so have the costs of claims.

In 1991 the Club had total gross claims (that is total claims before any reinsurance recoveries – noting that we buy reinsurance to protect the Club), of US$24.8m; the largest claim was just over US$2m for a wreck removal in Fiji. We also experienced three claims in excess of US$1m during the year.

Looking at 2007 (I chose this year as it is slightly more mature than the more recent years) the Club incurred gross claims of US$149,180,000. Many of these claims are still open today, illustrating the protracted nature of Protection & Indemnity Insurance. The largest claim was a wreck removal incident of US$27m and the Club incurred 21 claims in excess of US$1m.

In 1991 the total number of claims to the Club involving tugs was 124, with an average cost of US$13,800 for each claim. In 2007 the figure increased to 476 claims and an average value of US$48,000 (*see Figure 2, below*). These are average costs and so while the increase in our tug business has been significant, it is on the average cost of claims that we should focus.

So why have claim costs soared and are owners properly covered through their P&I entry to address the increasing risks? Before we suggest reasons as to why the cost of claims have increased, let us contemplate what a tugowner needs to consider, often with his broker, before arranging third party liabilities insurance to cover the liabilities that flow from the vessels' operations.

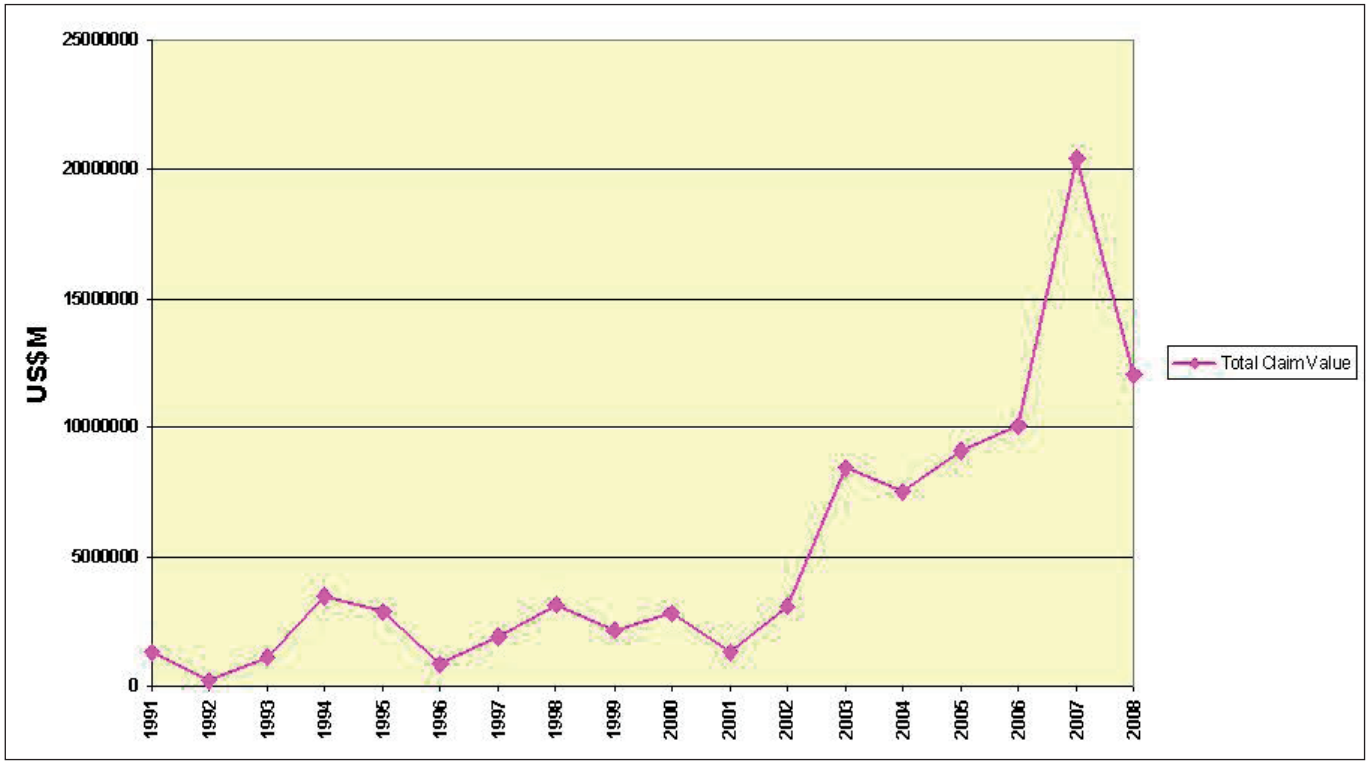

Figure 2: Graph demonstrating the increase in the total value of claims to our insured tugs' excess of US$50,000 for the period 1991-2008.

THE COVER

It is exactly because we expect all tugs to operate on internationally-recognised towage and contractual provisions that all the Clubs within their conditions of insurance specifically exclude: “Any liability for loss of or damage to or wreck removal of the towed object and any cargo and property on the towed or assisted object”.

Firstly, we do not expect any tugowner to want to pick up these risks and, secondly, these risks are traditionally covered within the insurances arranged by the assisted vessel or barge or offshore structure or, for that matter, the salved vessel. Why should the tugowner increasingly be required to carry these risks? Is it equitable for a small harbour tug to accept an increasing liability for damage caused to a sophisticated, high-value LNG carrier? To do so could result in the cost of the insurance far outstripping the contract value.

Yet we have seen traditional towage forms coming under pressure, whether a tug is engaged in terminal towage or deep-sea towage operations. The risks are changing, becoming increasingly more onerous and, in turn, more costly.

Will P&I insurers be able to continue to cover the liabilities of tugowners competitively or will they be forced to increase premiums, which will thus increase the impact on the profits of a tug operator?

Prior to reviewing the different types of towage operations and how it impacts on a vessel’s insurable risks, let us consider in more detail what protection and indemnity insurance is and how it relates to the towage industry.

While we are familiar with the role of hull and machinery insurers, who insure the property of the vessel owner for any loss or damage to the owned property, it was in 1855 that the shipping industry became more aware of its exposure to liabilities, at the time uninsured, and that these exposures represented an increased risk.

Owners decided to group together to pool these risks. While a premium did not change hands in those early days, owners would share the liabilities of others and indemnify the owner for his loss, so the insured also became the insurer and the protection and indemnity associations were born.

In its 155 year history, P&I insurance has evolved not least with the establishment of the International Group of P&I Clubs consisting of 13 International Group P&I Clubs. Yet the fundamental mutual principles of serving the vessel industry have remained unchanged and, with it, the benefits of mutuality and being part of a non-profit making insurer.

Some owners today choose to place their P&I risks with their hull insurance, something quite common in the towage industry, but as vessel values increase and liabilities become more complex, P&I insurers have developed a role in this specialist marketplace, most especially through the International Group of P&I Clubs.

Over the years we have come to realise that the liabilities of a tug can be varied from the harbour tug engaged in ship berthing, a deep-sea offshore tug operating in the offshore towage industry to a tug-and-barge operation along a river system.

The liabilities traditionally associated with a towage operation can also vary according to the legal jurisdiction where the vessel operates. In the United States for example, a tugowner invariably has to accept a contributory responsibility for his liabilities during towage. In contrast, European courts generally accept, as is customary in the towage industry, the exculpatory clauses contained within internationally recognised towage conditions.

It is generally assumed that a prudent tugowner/operator, whether engaged in ship berthing or general towage duties or any other port duties, will operate in accordance with contractual conditions. These may be his own in-house conditions as constructed by a local maritime lawyer or the internationally recognised forms referred to earlier in this paper.

When we consider the history of towage there are really two different aspects of towage law which must be strictly separated: the first concerns tortious issues, mainly of tug and towage liabilities with third parties; the second concerns the contractual relationship between the tug and the tow themselves. This is usually regulated by a standard form of towage contract as referred to above.

In general it can be said that a third party during a towage operation is not prejudiced by the towage contract. In particular the tug will continue to be liable for its own negligence to the third party, although it may have no liability to the tow by virtue of the exclusion clauses in the towage contract. Although we have seen increases recently to the limits of liability for which a tugowner may be permitted to limit his liability in law through international conventions, it has nonetheless traditionally been important to find liability on the part of the tow, ie the vessel or barge that the tug is engaged in assisting.

It is important that towage is defined as ‘the expediting of a vessel’s progress’ and must be distinguished from salvage, which is described as ‘the services performed to a vessel in distress’.

While the traditional areas of P&I cover are well known, for example Clubs respond to the liabilities of a vessel owner for:

- Collision claims;
- Damage to third party property;
- Injury or illness or death of crew;

- Liability to passengers;
- Liability to cargo;
- Liability for wreck removal;
- Certain fines and penalties.

These risks are covered as per the Rules of the Club (which are generally the same among all Group Clubs) and as per the tugowner's own terms and conditions of insurance as agreed with the insurer. It is the liabilities assumed while towing that can cause so much misinterpretation when looked at in conjunction with the Rules of the Club.

There are three principal sub-sections to the towage Rule:

- Customary towage of an insured vessel;
- Non-customary towage of an insured vessel;
- Towage by the insured vessel.

When assessing towage liabilities, the P&I Club, the insurance broker and the vessel owner must first review towage by the insured vessel. Because the potential liabilities taken on by an insured tug towing another vessel are very significant, bearing in mind the disparity in size and value of the tug and tow, and the difficulties inherent in towing, it is essential that the insurer fully understands the basis of the tug's liability under the contractual conditions on which the tow is carried out. Although towage by an insured vessel to save life or property at sea will always be covered, any other towage by an insured vessel is subject to agreement of the terms of towage by the P&I insurer concerned.

We all know that the UK standard conditions or, for the matter the Eastern Canada conditions, the Dutch and German conditions represent the most favourable allocation of liabilities that would usually only be applicable to harbour towage. In contrast, ocean towage by an insured vessel under a Towcon, Towhire, Supplytime or other contractual form that allocates liabilities on a knock-for- knock basis may also be covered without qualification.

If a tug is towing on one of these contract forms there should be no liability for loss of or damage to a wreck removal of the tow or cargo on the tow in any event, but in very special circumstances the risk of such claim may be covered if, for example, the claimant for whatever reason, was able to break the contractual provision.

If a tug is not towing on one of these towage forms the conditions of insurance will apply in that there can be no cover for loss or damage to the towed object. However, it may be possible to underwrite these risks through some form of extended insurance policy to cover any additional contractual liabilities. Most P&I insurers today, who provide insurance for tugs, will be able to provide some form of contractual extension.

Under the UK standard conditions of towage ,or the BIMCO Towcon, Towhire, or Supplytime forms, the tow accepts liability for its own damage and for any damage that it may cause to third parties. Other knock-for-knock contract forms may be silent on the allocation of liability for damage caused by the tow, in which case the tug may end up with a liability as it will usually follow that the tug has been negligent in handling the tow which would have caused the damage to the third party. This is a liability which can be covered by the P&I Club, even if there is no contract at all, yet there remains no specific cover for loss or damage to the tow.

It is also important in such circumstances to consider the extent to which towage liabilities may be covered within a vessel's hull and machinery policy up to the vessel's hull value. This appears to be a traditional way in which tug operators, for example in South America, address their towing liabilities but always up to a vessel's hull value and generally in accordance with forms of hull insurance such as the American Institute tug form. In such circumstances, and when towage is undertaken without the use of an approved towage form, Club cover can be structured to address the additional tower's liabilities excess of the vessel's hull value, to specified limits for any loss or damage or wreck removal of the towed object, but this would form a special cover and such additional insurance would need to be placed by the P&I Club or the tugowner's broker, in other insurance markets.

THE RISKS

It is clear that terminal towage does generally represent a better risk to most P&I Clubs, but it could be argued that the risks are great and that tugs can be engaged in towing very high value vessels, particularly the new generation of container vessel.

This has been recently illustrated by the best practice/ safety guidelines issued by the European Tugowners Association where they have recognised concerns associated with the speed in which some of the large containerships enter the port. However, most tugowners can safely stand behind their towage conditions and it would be the P&I Club of the large container vessel that would respond in the event that any claim was to occur, even if it resulted out of the negligence of the tug, and through their own customary towage rule.

A worrying trend these days is the increasing number of claims arising from the more traditional brown-water tug and barge operations. For example, we have seen an increasing number of towage claims arising out of bringing barges into collision with third party vessels and property, especially when transiting busy shipping lanes or areas in which vessels are moored awaiting orders. Are charterers placing additional pressure on tugowners to take short cuts to ensure that they meet deadlines, when skirting around a busy anchorage would greatly reduce the risks? Perhaps consideration should also be given to providing some form of escort tug to direct the barge while in tow to avoid potential collisions?

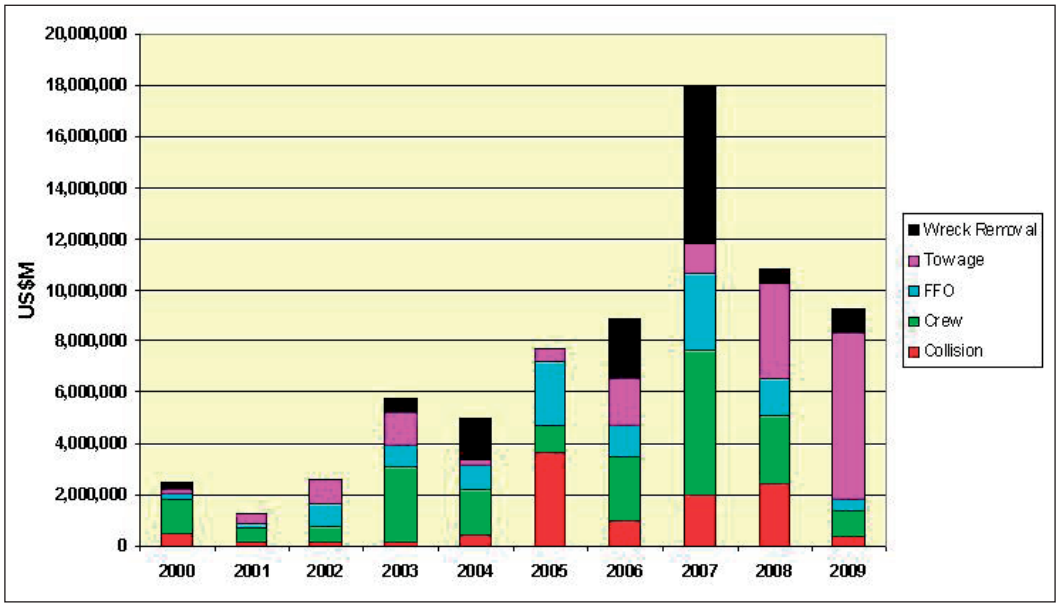

Figure 3: An illustration of the development in our tug claims by value.

While the above illustrates an increased risk to the P&I insurer, the risks can be covered in accordance with a P&I entry. Nonetheless, if the risks are enhanced, it is inevitable that the costs of P&I will have to go up, as will the level of deductibles, ie that part of the claim for which the owner has to contribute.

Notwithstanding the fact that additional insurance can be arranged to extend a tugowner's P&I insurance entry to cover the additional contractual liabilities that may be assumed during towage, in the absence of a contract of towage in the case where a tug is accepting a liability for loss or damage to the towed object, it is always anticipated that most if not all towage operations would be performed in accordance with acceptable towage condition. Likewise towage will be undertaken in acceptable jurisdictions where generally towage conditions are upheld.

It is perhaps worth mentioning our own recent experience where we have seen jurisdictional challenges to the traditional towage conditions, for example in South Africa and Australia where the UK towage conditions have come under scrutiny. Here in British Columbia the widely used Eastern Canada towage conditions, so traditional on the East Coast of Canada, are not generally accepted. As a result, bespoke conditions have been adapted, particularly to address the local tug and barge industry. In the US there remains the continual challenges where tugowners generally cannot contract out of their negligence.

While it may be customary in the trade, particularly the tug and barge industry, that towage forms are not utilised, it is generally accepted that knock-for-knock principles should be maintained during any towage operation. Therefore to the towage industry reading this paper we ask that collectively, through Associations such as ITS, the British Tug Owners' Association and the European Tug Owners' Association and, for that matter, any other industry body, tried and tested towage conditions are maintained so that we do not allow charterers to adapt them to their own favour. Quite simply to do so will result in insurance costs increasing and in some cases insurers will withdraw from the market.

To an owner and operator of a tug undertaking any form of towage or salvage, utilisation of acceptable contract forms is essential. Liabilities falling on the tug for loss or damage to the towed vessel, which could also extend to an element of downtime, could be extremely costly and should be customarily avoided by utilisation of the internationally recognised forms for towage.

In conclusion, it remains of fundamental importance to any operator of a tug to be aware that the insurance cover provided by a P&I Club will always traditionally exclude any loss or damage to the towed object and its cargo yet, via the managers of the P&I Club, who always seek to provide insurance solutions, additional cover can be arranged. If you have any queries concerning towage cover and how it interrelates in the strange world of P&I, please do not hesitate to contact your insurance broker and your insurer.