

PROTECTION AND INDEMNITY

Few signals forthcoming on antitrust

A rigorous probe is underway by the new Brussels team with scrutiny of the clubs more detailed than in previous inquiries.

Jim Mulrenan

London

Seventeen months into an anti-trust probe of the protection-and-indemnity (P&I) clubs and an outcome to the investigation still appears to be a long way off.

A ruling is not expected before the latter part of this year at the earliest and at least so far there are few signals from Brussels about the likely result.

But an obvious conclusion is that a rigorous investigation is underway and the scrutiny of the clubs and the International Group cartel is more detailed than the two previous antitrust inquiries.

The current investigation has been delayed by major changes to the case team examining competition in the P&I market.

The delay appears to be down to normal personnel turnover, al-

though the extended investigation may not be to the advantage of the group clubs hoping for clearance of restrictions on price competition in the P&I market.

The continued uncertainty and attempts to second guess what the outcome may be is leading to questioning of many aspects of the way the clubs operate, possibly generating pressure for change.

There has been a recent extensive questionnaire to brokers that seeks proposals for improving competition in the P&I market with answers requested by next week.

As can be seen from the questions (*see facing page*), the anti-trust team is interested in a wide variety of topics, from the fundamental restraints on premium quotations to the arcane workings of the 30 September procedure.

There are questions about the way the release-call system works and whether they are set at justified levels or in effect handcuff an owner to a club.

A further topic is whether the current P&I system favours certain shipowners at the expense of others.

There seems to be a renewed focus on the core issue of how the co-operation between the 13 members of the International Group and restrictions on price competition affect the market, as well as release calls.

But there may be reduced interest in the impact of the clubs' joint reinsurance programme and whether this inhibits competition to the 13 clubs in the International Group.

The broker questionnaire is understood to have been prompted



BRUSSELS: The EC is requesting answers by next week.

by a limited response to parties other than the clubs and there are suggestions that there could also be further efforts to solicit shipowner views.

But interpreting what is going on in the European Commission (EC)'s competition directorate has something in common with observing events in North Korea, with a lot of potential for developments to be misread.

The new antitrust team is understood to have been asking about the 30 September procedure — which on the face of it provides a way a shipowner can escape

price fixing at the 20 February renewal — but in practice is virtually unused.

To take advantage of this procedure an owner must enter into a firm commitment to move ships to a new club by 30 September — nearly five months before the normal renewal date.

The new club gets the premium pricing and claims record of the owner from the old club and is free to quote a different premium providing it is not unreasonably low.

But it is a bureaucratic and involved procedure that a shipowner may be reluctant to invoke —

The broker questionnaire is understood to have been prompted by a limited response to parties other than the clubs and there are suggestions that there could also be further efforts to solicit shipowner views.

QUESTIONNAIRE ISSUED TO BROKERS

The European Commission (EC) is currently investigating the International Group Agreement (IGA) of the International Group of P&I clubs, as well as the pooling agreement and their implementation by the International Group of P&I clubs and the P&I clubs.

The investigation of the EC into the P&I clubs is mainly focussed on the provisions concerning release calls and quotation procedures in the IGA.

Brokerage services for shipowners — clients

1. Please inform us about the type and size of your P&I brokerage business. For how long you have been working in the P&I business. How many shipowner-clients for P&I insurance you have for your brokerage services. Please detail the tonnage and number of vessels your company insures for your shipowner-clients. According to your estimates, what would be approximately your market share in tonnage and number of vessels in P&I insurance brokerage market?

2. Please inform us with how many P&I clubs that are members of the International Group Agreement (IGA), with how many independent P&I clubs and with how

many commercial insurers you usually deal with in your brokerage capacity.

P&I insurance market

3. Please inform us of your views on the P&I insurance market. How is currently competition functioning in this market? What improvements would be advisable to make competition work better in this market?

Release calls

4. Please describe your views towards release calls and their current levels. Do you consider that the release calls are a necessary component in the IGA to ensure the functioning of the claim sharing in the pooling agreement (PA)?

5. It is the commission's understanding that two P&I clubs have none or much lower release calls than most of the other members of the IGA. What are in your opinion the reasons why not all P&I clubs of the IGA apply release calls? To what extent does that affect their position on the market?

6. Do you estimate that the current level of release calls is reasonable and justified in terms of

ensuring the functioning of the claim sharing in the pooling agreement? What would you consider to be a reasonable/justified level?

7. How would you explain the different level of release calls between P&I clubs? What are the main reasons for clubs to set a high level of release calls?

8. Do you consider that the current level of release calls could discourage shipowners from switching between P&I insurers? If so, please explain your reasoning.

9. Is there any other approach you might favour or propose towards setting the level of release calls? Please elaborate on your reasons.

10. Please estimate which percentage of shipowners chose a bank guarantee instead of a release call when switching to another P&I insurer.

11. Do you believe that it is possible for a shipowner to obtain a bank guarantee at present? Please explain and distinguish between categories of shipowners when relevant.

12. The commission understands that the level of release calls was



TIME FOR A SMOKE: The ruling is not expected before the latter part of this year at the earliest.

Photo: Scanpix

different and possibly much lower in the past. Do you agree with this? What was the level of release calls in the past?

Quotation rules

13. Do you consider that the quotation rules procedure is a necessary component in the IGA to ensure the functioning of the claim sharing in the PA? Please elaborate on your reasons.

14. It is the commission's understanding that one P&I club of the IGA does not have this procedure in place. Do you confirm this understanding? What are in your opinion the reasons why not all P&I clubs of the IGA apply quotation rules? To what extent does that affect their position on the market?

15. Do you consider that the quotation rules procedure could discourage shipowners from switching between P&I clubs of the IGA? If so, please explain your reasoning.

16. How do quotation rules affect the negotiation position of a shipowner? Would you consider that quotation rules affect the negotiation position of certain shipowners more than others?

17. Do you have experience that the quotation rules are circumvented in practice? If so,

a. Please explain how quotation rules can be circumvented

b. please estimate how often this happens (in % of switches between P&I clubs).

c. which category of shipowners is more likely to be able to circumvent the rules and in which



Photo: Bloomberg News

and this may be the reason it is hardly used.

There also seems to be interest in the sanctions that could be imposed on a club that fails to toe the pricing line and whether these are so disproportionate they are unreasonable.

The penalty for undercutting the holding club's rate for a ship or a fleet is that if there was a "relevant loss", the new club would not only lose the right to pool the claim but also reinsurance up to the \$150m mark for two years.

So instead of a club facing a maximum of an \$8m loss it would be facing a \$150m loss — an amount sufficient to make a very large hole in the free reserve — unless reinsurance had been bought on a costly specific basis to cover the risk.

There is also more questioning about the way the International Group restrictions on price competition operate at a practical level, although there are limits to the extent most market participants are prepared to rock the boat.

The International Group clubs have always argued that restraints on price competition are modest and necessary to sustain co-operation between the clubs.

But even if this is the case the restrictions may also be contributing to market distortions that may not be to the advantage of the clubs or shipowners.

Churn is the well-known phenomenon where restrictions on competition for existing vessels leads to competitive battles for newbuildings or newly acquired tonnage where there is freedom to quote.

Churn operates to the advantage of owners of new vessels that benefit from this competition but to the disadvantage of owners of older more stable fleets where rates will have drifted upwards through general increases at successive renewals.

But an aspect of churn that is rarely mentioned is that it may also be operating to the detriment of the clubs, contributing to the mispricing of risk and the underwriting deficits seen in most years.

But how significant is the discount for new vessels that churn produces? The evidence is anecdotal but brokers TradeWinds has quoted over the past few years have suggested it might amount to as much as 7% of club premium income with the difference between new and old vessels in at

least some cases as wide as 50%.

Accountants Moore Stephens, who issue an annual survey of the cost of operating vessels, put the P&I premium for a 300,000-dwt VLCC at almost \$225,000 based on an average of 124 vessels. But a broker at a seminar for Greek owners put the premium for a similar-size newbuilding at \$184,000.

The same broker quoted a premium of \$76,500 for an 180,000-dwt bulker newbuilding but Moore Stephens puts the average P&I premium cost for a 148,000-dwt capesize at \$136,000 based on a 90-vessel sample.

There is also some market gossip on whether there is room for compromise between competition regulators' ingrained antipathy to any agreements that involve price fixing and the fact that the current

system works, appears to be acceptable to owners and to not be to the disadvantage of victims of shipping losses.

Does there, for example, have to be a single group covering all the 13 clubs or could there be two or three alliances that would be big enough to offer advantages of scale in terms of claims pooling and reinsurance buying but would increase competition in the P&I market?

There could perhaps be one grouping offering the current high limits of cover for passengerships, tankers and other vessels, where owners need insurance running to billions of dollars.

But one or more groups could provide cover to owners of bulkers, boxships, reefers and other vessels that might be content with lower level cover.

way this usually takes place?

18. Would you consider that certain P&I clubs of the IGA are more active in circumventing quotation rules than others? If so, please substantiate your reply.

19. Has the September procedure been used in the past decade? It is the commission understanding that it was taken up in 1990-1992 but then ceased functioning. In particular, there were 86 requests in 1992 and then only one in 1993. Could you provide explanations for this?

Brokerage services in P&I insurance

20. Please explain what services regarding P&I insurance you provide to shipowners and explain your role as an intermediate between shipowners and P&I clubs.

21. Please estimate what percentage of shipowners buy P&I insurance via brokers versus directly with P&I clubs?

22. Is there a certain category of shipowners that would rather negotiate and deal directly with the P&I clubs instead of using a broker? If you think so, please explain which categories of ship-

owners this would concern.

23. As a broker, do you pro-actively compare terms and conditions of P&I clubs or do you do so at the request of a shipowner? Please explain how you compare such terms and conditions.

24. Do you negotiate on every annual renewal with the P&I clubs for your shipowner-clients or rather in case of switching of a shipowner-client between different P&I clubs? Please describe in general terms the different steps of such negotiations.

25. Do you receive a higher remuneration or a bonus payment if the shipowner-client switches to a different P&I club in comparison to the remuneration you receive in an annual renewal situation? If so, please give examples of the importance of such additional remuneration, expressed as a percentage of the premium. Please estimate in what percent of switches a broker receives an additional or higher remuneration.

26. Does the size of broker remuneration differ from one P&I club to another? If so, please give an example of the differences.

27. Please elaborate on the incentives a broker has to offer and/or

negotiate a better price for the respective shipowner-client?

Switching of shipowner-clients between P&I insurers

28. Please estimate the percentage of shipowners that switch or partially switch on an annual basis. How does this rate of switching compare to other forms of insurance? If you can, please also estimate separately the percent of switches p.a.:

a. between P&I clubs,

b. between a P&I club of IG and a commercial insurer or a non-IG P&I club.

29. From your experience, which are the factors shipowners take into account when considering switching?

30. Do you see impediments for shipowners to switch between P&I clubs or between a P&I club and a commercial insurer? If so, please state the main ones and explain your reasons.

Shipowners and the P&I insurance industry

31. Do you think that the shipowners that buy insurance via brokers are aware of the precise rules and mechanisms that govern the re-

lease calls and the quotation procedures? Please explain. In case that awareness/knowledge would be limited, please explain to what extent brokers increase the awareness/knowledge of shipowners.

32. Do you think that certain groups of shipowners might benefit from the current system of P&I club insurance in the IGA whilst other shipowner categories might suffer? If so, please substantiate which categories of shipowners benefit/suffer and what the underlying reasons are?

Changes to the IGA pursuant to the 1999 Commission decision

33. Do you think that the changes which were done to the IGA and the PA previous to the 1999 commission decision, which were (1) lowering of the common minimum cover from \$18bn to \$4.25bn and (2) taking the administrative costs out of the IGA so that the quotation rules no longer apply to them, changed the functioning of competition in the P&I insurance market?

34. Do you estimate that the current level of common minimum cover offered by the P&I clubs in the IGA is necessary in this in-

dustry? Please elaborate on your reasons also in comparison to claim statistics and the level of highest claims.

35. Please estimate how much administrative costs differ between the P&I clubs?

a. How are administrative costs individualised in a quoted rate, ie as a percentage of the rate or do P&I clubs rather tend to offset them from the investment income?

b. Do brokers have statistics on these and look at these when advising a shipowner whether to switch or not?

c. In your opinion, are P&I clubs competing on the basis of the administrative costs?

Commercial P&I insurance

36. Do you think that the demand exists between shipowners for the fixed-premium commercial P&I insurance? If yes, what types of shipowners are more likely to be interested in this? What are in your view main advantages and disadvantages of the commercial P&I insurance offering?

Additional information

37. Please provide any other comment that you would judge relevant for the on going investigation.