Title: Post-Implementation Review of the Merchant Shipping (Compulsory Insurance of Shipowners for Maritime Claims) Regulations 2012 **PIR No:** DfTPIR0017 **Lead department or agency:** Department for Transport **Contact for enquiries:** Andrew Angel (tel: 07825 231803, email:andrew.angel@dft.gsi.gov.uk)	Post Implementation Review **Source of intervention:** EU **Type of regulation:** Secondary legislation **Type of review:** Statutory - other **Date measure came into force:** 05/10/2012 **Recommendation:** Keep
Summary: Intervention and Review	**RPC Opinion: GREEN**

1. What were the policy objectives and the intended effects?

EU Directive 2009/20/EC on the insurance of ship-owners for third-party maritime claims was transposed into UK law through the Merchant Shipping (Compulsory Insurance of Ship-Owners for Maritime Claims) Regulations 2012 and applies to vessels of 300 gross tonnes (gt) or over. The Regulations came into force on 5 October 2012.

The legislation ensures that ship-owners maintain insurance in order to cover third-party liabilities up to the limitations set out in the international Convention on the Limits of Liability for Maritime Claims. Such third-party claims include damage to docks or harbour walls, pollution and injuries to passengers or crew. Evidence had shown that the types of incidents most prevalent involved vessels of 300 gt or over operating in EU waters, for which there was previously no specific compulsory insurance requirement. The requirement to have third-party insurance also extends to non-EU vessels entering the port of an EU Member State.

Whilst it was widespread voluntary practice already for UK ship-owners to have insurance against such liabilities, the Directive was adopted to discourage ship-owners from cutting costs by not having such insurance. If uninsured vessels were involved in incidents where the ship-owner was liable for third-party costs, the typical magnitude of such costs means it is unlikely the ship-owner would have been able to pay them in the absence of insurance cover. If the ship-owner is unable to pay, there is a potential liability on the UK government for significant third party costs.

The intended outcome of the Directive was to ensure that EU ship-owners maintained adequate insurance cover to deal with the costs incurred on third parties from general maritime incidents.

2a. Describe the rationale for the evidence sought and the level of resources used to collect it, i.e. the assessment of proportionality.

The level of resource used to collect the evidence for this report was low, given that the Regulations put on a statutory footing what was largely already performed on a voluntary basis. The original impact assessment[1] had estimated that the cost of implementing the EU Directive for ship-owners was low – the net cost to business per year was not quantifiable, due to the lack of sufficiently robust data, although the evidence gathered suggested that most UK ship-owners had taken out voluntary third-party insurance. Moreover the requirements of the Regulation were not identified as being either risky or contentious. At the time of consultation, industry had responded positively, seeing this as a minor legal change and having little practical effect.

On that basis the level of evidence sought for this report was also correspondingly low. As the legislation was expected to have a negligible impact on UK ship-owners, it was not deemed proportionate to undertake a higher level of evidence gathering, especially as the evidence sought was considered sufficient to answer the research questions related to the review.

[1] http://www.legislation.gov.uk/uksi/2012/2267/impacts

2b. Describe the principal data collection approaches that have been used to gathering evidence for this PIR.

A very light touch impact evaluation was used to identify any effects of the legislation on the UK shipping industry arising from any maritime incidents that involved third-party claims. In particular the review sought to evaluate:

- Whether there had been changes in third-party insurance premiums;
- Whether there had been an increase in ship-owners seeking third-party insurance;
- Whether there was fresh evidence to quantify or qualify any such changes to premiums;
- Whether the legislation had been a benefit or hindrance to the UK shipping industry;
- Whether there had been a change in the number of maritime incidents involving third-parties and insured vessels at the 300 gross tonnes end of the market

3. To what extent has the regulation achieved its policy objectives?

It has been difficult to ascertain whether the Regulations have achieved its policy objectives. The adoption of the Directive was part of a wider package of EU and international measures introduced into the maritime liability regime between 2012-2016.

Despite an extensive engagement exercise with industry, through regular informal discussions and a formal consultation, particularly with the International Group of Protection and Indemnity Clubs IGPANDI, we have been unable to draw out any evidence to better understand the impact of the legislation. It is worth noting that the nature of maritime liability insurance is predicated on a number of different factors which, in turn, may affect the premiums that a ship-owner pays. Such matters can relate to the type of vessel, its cargo, its operational area, the frequency of claims and the resilience of the market. Given such diversification it has not been possible to secure a broad consensus or provision of data from industry.

As there is little Government oversight of the payment of maritime insurance claims, and the reticence of industry to provide data on such claims, we do not know whether the policy concerns have been properly addressed and that compensation to victims have been paid out. We do know that there have not been any recent claims on Government for costs incurred by third parties as a result of a maritime incident, either prior to the adoption of the Directive, or since.

As a result, it has not been possible to inform existing assumptions developed in the original Impact Assessment with any new or additional evidence. The lack of data from industry since the introduction of the Regulations may be indicative of industry's general support for the provisions and that current arrangements have been seen as a welcome addition in the wider international maritime liability regime. As the Regulations, at the time, were considered to be a relatively minor change and uncontroversial, it is perhaps unsurprising that there has been little engagement on the issue, particularly given how widespread voluntary insurance was at the time.

There has not been any indication from industry that the legislation creates an expensive imposition, nor is there any evidence to suppose that the requirements have led to an increase in the proportion of pay-outs settled satisfactorily.

4. Have there been any unintended effects?

In the five years since the legislation was introduced the Maritime and Coastguard Agency (MCA), which has responsibility for port state control inspections on vessels entering UK ports, were not aware, even anecdotally, of any problems or difficulties with the requirement to have third-party insurance in place. On an annual basis, the MCA carry out a significant number of inspections – for example, in 2012 when the regulation came into force, they inspected nearly 1500 foreign vessels and carried out over 3800 UK vessel surveys, within which vessels of over 300gt were included. The MCA did not report any deficiencies in this regard and no vessel has been reported as not having the insurance. No penalties were issued and no action was required against ship owners.

The Department and the MCA have not been made aware of any unintended consequences, either through the engagement exercise for this PIR, or prior to that during regular engagement with industry trade associations.

However, the review did prompt a particular point from industry regarding the type of insurance referred to in the legislation and the potential difficulties the victim of an incident may face when trying to bring a successful claim against the ship-owner which is discussed in Section 8.

5a. Please provide a brief recap of the original assumptions about the costs and benefits of the regulation and its effects on business (e.g. as set out in the IA)

Due to the limitations of the available evidence base at the time of the original impact assessment[2] (no evidence was provided by consultees at the time of the consultation process) it was not possible to monetise any of the costs that were identified. Two costs were identified, potentially: (a) an obligation to purchase insurance to cover the lower end of vessels (nearer 300 gt). However, the prevailing view was that the vast majority of UK registered vessels already maintained general third-party insurance, so the impact was considered small at most; (b) familiarisation costs, but there was no evidence at the time available for this. This cost was not, therefore, monetised.

5b. What have been the actual costs and benefits of the regulation and its effects on business?

The questionnaire sought further evidence and information regarding costs and benefits to industry, but industry was unable to provide any data. Unfortunately, the section of industry most likely to have been affected by the regulations (those operating vessels closer to the 300gt limit) are less easily visible to Government. Whilst efforts have been made to identify such businesses and understand better from them whether the Regulations have affected them, these efforts have not been successful. So a more detailed assessment cannot be made on the actual impact of the Regulations on business.

6. Has the evidence identified any opportunities for reducing the burden on business?

Industry did not take the opportunity to provide any evidence, nor did they indicate that they wished to see the effects of the Regulations lessened or removed altogether. It is on that basis that there does not appear to be any need to consider reducing any burdens, since none have been identified by industry. Even though the need for such insurance is intended to provide greater protection to port and harbour authorities, amongst others, and to remove the liability risk to Government, in the event of an incident, these stakeholders did not indicate that the regulation should be removed or changed.

7. For EU measures, how does the UK's implementation compare with that in other EU member states in terms of costs to business?

The European Commission is required to report to the European Parliament and the Council every three years on the application of the Directive relating to the insurance of ship-owners for maritime claims. The first such report (7424/16 (COM (2016) 167 final)) was published on 30 March 2016[3], and a subsequent Explanatory Memorandum (No. 37626) was provided to Parliament on 12 April 2016.

Member States were required to transpose the Directive into national law by 1st January 2012 and all notified the Commission of their national implementation. The Commission did report that different Member States had different approaches when it came to ensuring compliance with the Directive for their domestic vessels[4]. Some Member States do not explicitly check their domestic vessels for compliance with the Directive, relying indirectly on the port state control of other states. For the purposes of port state control, vessels entering or leaving EU ports are checked to show that they have appropriate insurance in place to meet their liability

[2] http://www.legislation.gov.uk/ukia/2012/377/pdfs/ukia_20120377_en.pdf
[3] http://data.consilium.europa.eu/doc/document/ST-7424-2016-INIT/en/pdf
[4] Maritime regulations are generally enforced in two ways. Flag State Control is where the country where the vessel is registered, conducts enforcement activities to ensure compliance with domestic and international regulations. Port State Control is where foreign-registered vessels are inspected when they arrive at a UK port, to ensure compliance with international regulations and *relevant* domestic ones.

obligations under the Insurance Directive. As indicated in Section 4, the MCA have responsibility for carrying out such checks to ensure that vessels entering or leaving UK ports have the appropriate insurance in place.

Based on compliance records the Commission concluded that the vast majority of vessels entering or leaving EU ports had sufficient insurance in place and that this, in turn, would ensure that victims of incidents could obtain appropriate compensation from the ship-owner. The Commission noted that some obligations on Member States relating to implementation and enforcement could be improved through the enhanced use of the existing operational information and data exchange systems in order to achieve a more uniform approach, but did not suggest any new proposals. Nor was there any new evidence to indicate that there were any additional costs related to Implementation for EU ship-owners (e.g. increased premiums).

8. Assessment of risks or uncertainties in evidence base / Other issues to note

The EU Directive describes the type of insurance that ship-owners should have in place for the purposes of meeting third-party liabilities as being "…indemnity insurance as currently provided by members of the International Group of Protection and Indemnity Clubs (IGPANDI) or other effective forms of insurance…". In most cases ship-owners will use indemnity insurance, either that which is provided by the Clubs, or from non-Club P&I insurers. Such indemnity insurance is usual for such maritime liabilities, as opposed to straight liability insurance. Indemnity insurance works on the basis of the "pay to be paid" rule which, in effect, means that a ship-owner with P&I insurance does not make a claim for a liability loss from their insurer, but instead effectively makes a claim for reimbursement from the insurer following the insurer's controlled settlement on negotiated terms, or as awarded to the claimant by way of a court or arbitral ruling.

However, a perceived risk arises when a ship-owner may not be able to pay the victim "up front" and so discharge the liability or expenses because of lack of funds or even insolvency. The P&I insurer could, therefore, potentially walk away from the insolvent ship-owner and his related liabilities, since the current legislation does not allow direct action against the insurer. However, such behaviour is unlikely to occur within the IGPANDI insurers. Nonetheless, a P&I insurer, who does not belong to the international group, may seek to reduce costs at the potential expense of the victim, unless the victim can secure redress through the Courts.

The Third Parties (Rights Against Insurers) Act 2010 partially deals with the situation that requires the prior discharge by the insured of the insured's liability to the third party, but only to the extent that it covers – and in particular regarding marine insurance – liabilities involving death or personal injury. The amendments made in 2016 to the 2010 Act did not further modify those elements, having the effect that the "pay to be paid" arrangements remains a valid contractual agreement with the insured and the insurer.

Although the issue may be a matter of importance to third-party claimants, it is of limited value for the purposes of reviewing the effects of the current legislation to which this report alludes. Ship-owners will continue to use indemnity insurance, particularly through the IGPANDI as it provides the best cover for their liabilities and at a competitive rate. Possible options might be to amend UK legislation so that UK ship-owners (and ship-owners whose vessels enter UK waters) are required to have liability insurance in place instead (and thereby removing the "pay-to-be-paid" rule) or, alternatively, to be able to take direct action against the insurers, but this might force ship-owners to purchase limited or more expensive insurance as a result. These would, however, be significant adjustments to the existing arrangements, gold-plating existing EU and international legislation. To date, no further analysis or discussion with industry has taken place concerning such options, or any other options, and none is currently envisaged since there is no reason to suppose that this is a significant issue that needs addressing.

9. What next steps are proposed for the regulation (e.g. remain/renewal, amendment, removal or replacement)?

This review has been unable to come to a concrete conclusion on whether the Regulations have met all their objectives. The Regulations have addressed a concern in relation to the potential gap in third party liability insurance (and implications this has on third parties incurring costs from maritime incidents). This ensures that third parties enjoy better protection because ship-owners maintain appropriate insurance,

which discourages the operation of sub-standard vessels. However, it is still unclear to what extent the Regulations addressed a real problem.

Nevertheless, we believe that the Regulations are a sensible addition to the maritime insurance framework by providing a regulatory backstop. As we have not found any evidence to suggest that the costs of the Regulation have been significant, it is unlikely that there would be much benefit from repealing the Regulations, which would also have the effect of putting the UK in breach of its EU obligations.

On 23 June, the EU referendum took place and the people of the United Kingdom voted to leave the European Union. Until exit negotiations are concluded, the UK remains a full member of the European Union and all rights and obligations of EU membership remain in force. During this period the Government will continue to negotiate, implement and apply EU legislation. The outcome of these negotiations will determine what arrangements apply in relation to EU legislation in future once the UK has left the EU.

Sign-off for Post Implementation Review:

I have read the PIR and I am satisfied that it represents a fair and proportionate assessment of the impact of the policy.

Signed: Lyu Georgiev **Date:** 04/05/2017