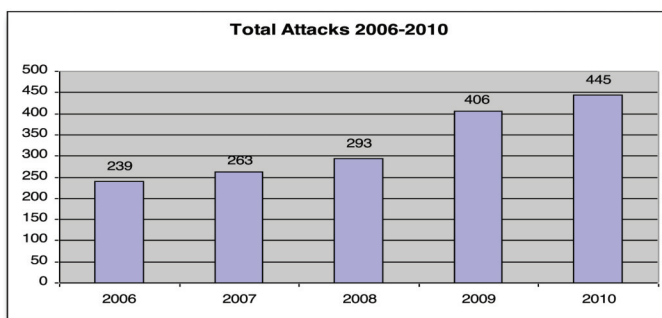




Piracy and Insurance — Don't Walk the Plank Without a Parachute

For many, discussions of pirates conjure up visions of Captain Jack Sparrow. This fictional Disney character creates the aura that pirates are adventuresome, swashbuckling, somewhat dated caricatures of yesteryear. In fact, pirates remain a very clear and present danger and pose an interesting risk dynamic for cargo owners, vessel operators and insurance companies to consider.

Piracy attacks have increased almost two-fold since 2006—especially off the coast of Somalia and in the Gulf of Aden. Their frequency and the accompanied brutality are particularly disconcerting, with associated ransom demands skyrocketing into the tens of millions of US dollars. According to the International Maritime Bureau (IMB), hijackings off the coast of Somalia alone accounted for 92% of all ship seizures last year with 49 vessels captured, 1,016 crew members taken hostage and 8 crew killed.

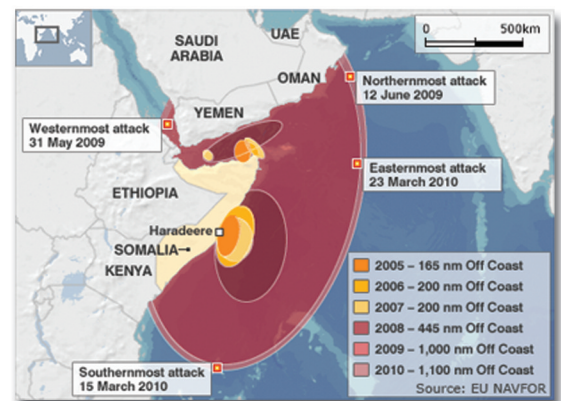


Data source: ICC Commercial Crime Services | Graph prepared by: Roanoke Trade Services, Inc.

Somali pirates will often capture a fishing or merchant vessel for use as a “mother ship” which allows them to extend their range and provides them with a disguise of legitimacy. As demonstrated on the following map, the Somali pirates theater of operations has increased exponentially since 2005 based on the application of this strategy and now includes the entire Gulf of Aden and surrounding area. Whereas IMB used to recommend a “buffer zone” of at least 75 miles for vessels passing off the Somali coast, attacks are now occurring as far as 1,300 nautical miles out to sea. Since vessels must transit this area to access the Suez Canal, the situation is especially challenging for commercial vessels which in some cases have re-routed their ships around the southern tip of Africa in order to avoid the region. Obviously, this decreases efficiencies by increasing transit times and fuel costs.

At first glance, it is easy to wonder why these massive commercial vessels are not able to defend themselves from a few pirates in a small speed boat; however, it is important to remember mariners are not mercenaries. While they may be trained to navigate the world’s oceans or repair diesel engines, many have never held a firearm or fired a rocket. Additionally, there are also strict regulations at many of the world’s ports which prohibit vessels from carrying these types of weapons into harbor. Even if these challenges could be overcome, an escalating arms battle would likely ensue and most agree it is safest for the mariners not to engage the pirates in this fashion. As a result, commercial mariners are often forced to resort to non-lethal and often ineffective means of defense, including water cannons and long range acoustic devices (LRADs).

Due to the multitude of diverse interests affected by pirate attacks (vessel owners, crews, charterers, cargo owners, intermediaries etc.), there can be no single, all-encompassing insurance product which addresses all claims. Initially, the release of a hijacked vessel was seen as the owner’s problem alone, with cargo interests kept in the background until the matter was resolved by the owner, possibly with assistance from their P&I (Property and Indemnity) insurance underwriter. In recent years, owners have begun to consider declaration of General Average so that they might claim contributions from the hull and cargo insurers; however, the academic debate over the legitimacy of a GA declaration in the case of hijacking is still ongoing.



Map source: EUNAVOR/IMB (International Maritime Bureau) as seen on www.bbc.co.uk

Piracy is included as a standard marine peril in most Shipper's Interest Cargo Insurance policies; however, this coverage is strictly predicated on physical loss or damage and consequential losses are not covered. Cargo insurance policies exclude claims for delay or loss of market which are likely to occur when a vessel is seized by pirates and held for weeks or months while a ransom payment is negotiated. Additionally, there is a growing concern as to whether ransom payments made to release cargo/hostages are illegal, and moreover whether the vessel and cargo insurers can contribute to an "illegal" activity. Worldwide, anti-terrorism laws prohibit payments to groups tied to terrorism, and while there is no established formal link between piracy and terrorism, many suspect that these activities are closely related.

There are a few steps which cargo owners and vessel operators can take to manage their exposure to piracy related claims; however, there are unfortunately some exposures which simply cannot be managed through any of the standard forms available in the market today. Most importantly, cargo owners should always secure All Risk Shipper's Interest Cargo Insurance for all of their goods in transit. This product will not only answer claims of loss or damage arising from piracy, but will also pay any General Average contributions for which the cargo owner is responsible. Cargo owners should also have detailed conversations with their service providers to determine the routes traveled and the risk mitigation techniques employed by all vessels, especially those traversing the known "hot spots," including (but not limited to), the Gulf of Aden, Somali coast, South China Sea, and various areas around Southeast Asia and the Indian Subcontinent. If either the routes or mitigation techniques are not satisfactory, the cargo owner should consider alternative service providers with more acceptable risk avoidance/mitigation practices. Finally, although consequential losses associated with delay or loss of use are generally uninsurable in the standard markets, cargo owners may choose to examine the possibility of securing manuscripted policies through specialty markets which may have a desire for this type of business.

As you can see, piracy has matured...the days of walking the plank have now turned into hostage situations with ransom demands. The times where chests of gold and silver were the norm have now become containers of any cargo with resale value. In response to these changing dynamics, it's always best to sit down with your insurance provider and take a closer look at your risk profile each year.

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