

# **End of Year Review 2010**

For the year ended 20th February, 2010



Total Number of Ships Entered

3,446

Total Funds

£52 million

End of Year Reserves

£19 million

For the year ended 20 February, 2010

## Chairman's Statement



"You can rest assured that the Club, its Directors and Managers remain as committed as ever to providing a cover that is not only responsive to Member needs but is able to deliver quality service, cost effectively."

As my second year as Chairman draws to a close it has made me realise the ever increasing importance of the Association's cover. None of us will have been immune in some shape or form from the impact of the 2008 financial collapse. In this period Members quite naturally sought to enforce contractual obligations and minimise any potential exposure without delay.

It is therefore of no surprise at all that the Association, like all other providers of FD&D cover, has seen a significant increase in claims in the past few years. The Association has assisted Members in all manner of disputes, including questions relating to early redelivery, terminations of long term charterparties and contracts of affreightment, sale and purchase and also newbuilding disputes.

In the main these disputes have involved London arbitration under the auspices of the LMAA, however, some have involved other jurisdictions, including the US and Hong Kong. Rule B applications in the US were a particularly potent weapon against recalcitrant parties and it is indeed unfortunate that the US Supreme Court has refused to overturn the decision of the Appeal Court which dealt a death blow to this type of application. No doubt South Africa and France will again be the venue of choice when it comes to security steps.

The LMAA, however, by far and away continues to be the venue of choice for many Members. Its depth of experience is second to none, which is to be welcomed. Notwithstanding the continued commitment of Members to the LMAA, there are criticisms in some quarters about the London arbitral process, particularly concerning case management, speed and cost. In my view all those involved in the arbitral process have their part to play and all parties need to do more to reinforce the values which the LMAA stands for. The arbitrators are however the ones who have the power under the LMAA terms to actively direct proceedings so that claims are dealt with effectively and efficiently.

I mentioned last year that the Managers were enhancing their Value for Money programme. The name of this programme says it all: better value from those service providers for your Membership premium. To enable this to be achieved the Managers are endeavouring to focus work on a smaller number of legal suppliers. This of course does not preclude the use of other firms as appropriate, however, in order to realise the programme's goals it is important that we all try to play our part.

In terms of the Association's financial position for the year-end I am pleased to be able to report that the Association continues to be in a strong position. Over a number of years your Board has been committed to consolidating the Association's financial strength in order that Members are provided with a cover which is cost effective, avoids material increases in premiums year on year and provides the broadest available FD&D cover amongst all its competitors. This financial position is one of the reasons why your Board decided that a general increase of 5% was appropriate for the 2010/11 policy year along with no alterations to the underlying terms of cover. This in itself should provide considerable comfort to Members in a period of continuing uncertainty. Of course no one is complacent and the Directors and Managers are committed to maintaining this sound financial base.



## Chairman's Statement (continued)

The Association's free reserves for the year end stand at £19.0million with combined funds totalling £52.4million. In terms of ship numbers the Association continues to have a strong membership base with 3,446 ships currently entered. All of these factors place the Association in a strong position to meet the challenges ahead, not just in terms of market uncertainties but also with regulatory changes on the horizon. New EU wide solvency regulations, known as Solvency II, come into force in November, 2012. This seems some way off, however, considerable work needs to be done to achieve compliance and your Board and the Managers are actively engaged in this process.

Throughout this year your Board has worked tirelessly in order to provide Members with the cover you have come to expect. A considerable number of cases have been considered by the Board with the vast majority, in the order of 97%, receiving support or a substantial measure of support.

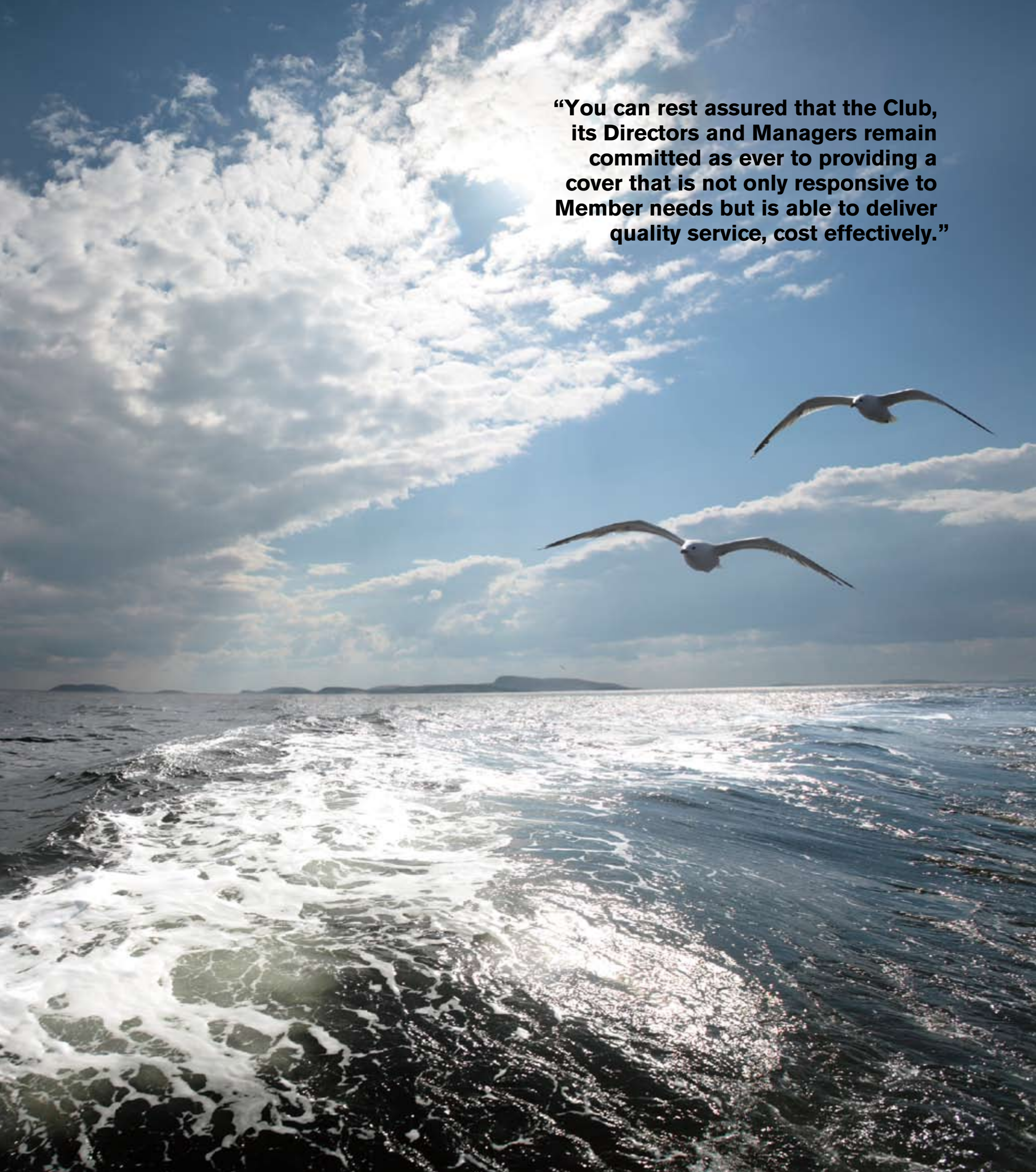
I would like to thank my fellow Directors for their considerable insight and support during the year. Their insight, experience and dedication to the affairs of this Association is unquestionable. The time and effort that the Board devotes to the affairs of the Association is one of the many strengths of the Association. There has been some change in the Board's membership this year with Mr Decavèle having stood down. His contribution was significant over many years and we are sad to see him leave. Two new Directors joined the Board during the year; Mr Richard Kendall of The China Navigation Co Ltd and Mr Yannis Triphyllis of Gourdomichalis Maritime S.A. Both in a short time have contributed a great deal to the Association's affairs. I would also like to thank the Management team for their significant assistance to the Board and Members.

In my view the Association's cover is invaluable. Not only does it provide Members with a level of expertise and knowledge which is unparalleled, it also cushions the impact of the costs associated with litigation which costs can be a significant proportion of the overall claim amount.

This Association is of course about you as Members. It exists for you. On behalf of the Board and the Managers I would like to personally thank you for your continuing loyalty. You can rest assured that the Club, its Directors and Managers remain as committed as ever to providing a cover that is not only responsive to Member needs but is able to deliver quality service, cost effectively.

**P.C. Laskaridis**  
Chairman

United Kingdom Freight Demurrage  
and Defence Association Limited  
June, 2010



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## Claims – Managers' Report

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The fall-out from the financial crisis of 2008 and the collapse in the shipping markets has brought a marked increase in the number of shipping disputes. London maritime lawyers have reported unprecedented levels of work and increases in turnover. In its 2009 statistics, the London Maritime Arbitrators' Association reported the number of arbitration appointments made during the year as 4,326 – an increase of 70% since pre-crisis days. The number of awards published has seen a similar rise. In an effort to manage workloads, some arbitrators have even set monthly quotas on the number of appointments they are prepared to accept.

Against this background, an increase in the number of claims reported to the Association was inevitable. As ship operators found themselves facing significant difficulties in meeting contractual obligations and sought reductions in hire rates the services of the Club were in significant demand from owners and charterers looking to protect their positions. In many of these cases, liability was not in issue, rather the priority being a race to identify and attach assets. The sale and purchase market was heavily affected, with buyers seeking to renegotiate, or even withdraw from sale agreements reached at the peak of the market. Early terminations of long term contracts were also a feature of this period. The sums at stake in all of these cases often ran into many millions of dollars and involved intense activity, bearing in mind the counter-party risk.

The number of shipbuilding disputes reported to the Club also increased, as yards encountered construction delays and liquidity issues leading to Members electing to cancel contracts. These cancellations were frequently disputed by the yards, and demands made under refund guarantees were blocked. The Association has assisted a number of Members in recovering advanced payment instalments, either through negotiation or in some cases contested arbitration hearings.

Away from market related matters, the subject of piracy has arisen in a number of cases. Several ships which are entered in the Association have been taken by pirates. Aside from the pressing issues of getting crew, ship and cargo released, legal questions have arisen, as in the SALDANHA, as to whether hire remains payable during the period of seizure. The English High Court recently upheld this issue in favour of a Member of the Association. Aside from ships which are taken, a significant number of queries have been made as to an owner's obligation to transit the Gulf of Aden or other areas of piracy risk; each case has turned on its own facts, depending, amongst other things, on the charterparty wording, the type of ship and the volume of pirate activity at the time.

## Claims (continued)

One of the most significant events in the FD&D world in 2009 was the demise of the Rule B attachment.

The Association has been involved in a number of other high profile disputes. In the case of the TS SINGAPORE the ship was damaged during a typhoon in China, and ordered by Class to proceed to Hong Kong to discharge her cargo of containers, and then to a repair yard in China. She was trading under a charterparty, which gave the charterer an option to cancel were the ship to be off-hire for more than 20 consecutive days. With market rates having fallen, the charterer cancelled the charter 20 days after the initial damage whilst the ship was on en-route to Hong Kong. However, the owner disputed this, because the charterer had ordered the ship to proceed to Shanghai after Yokohama, and in doing so, the ship would, for a period, have inevitably travelled on the same course as the ship had taken to Hong Kong. The owner therefore claimed that this period interrupted the 20 days of off-hire.

An arbitration tribunal supported the owner's position however the charterer appealed to the English High Court which overturned the award. The Court ruled that when assessing whether a ship was on-hire, it was necessary to examine the underlying commercial purpose of the charter, and that on any interpretation, if the ship was proceeding under the orders of Class, and ultimately bound for a repair yard, she could not be said to be performing the charterer's service.

The PARAGON was a dispute arising from the late redelivery to the Member under a time charter. The charterparty in question contained a clause – referred

to as the "last voyage clause" – whereby if the charterer failed to make a proper voyage duration assessment when giving its last voyage orders, and that the ship was redelivered late as a result, an uplifted hire rate would be payable for the last 30 days of the agreed charter period. Arbitrators ruled that the last voyage clause was a penalty clause, and therefore unenforceable under English law. This conclusion was upheld both by the English High Court and the Court of Appeal. Whilst the judgment focused very much on the wording of this particular clause, it is likely that any future attempt by shipowners to rely on similar clauses will not succeed.

One of the most significant events in the FD&D world in 2009 was the demise of the Rule B attachment. The Southern District of New York Court's ruling in *SCI v. Jaldhi* effectively brought to an end the possibility of attaching funds passing through New York bank accounts as security for maritime claims. This has had a significant impact on the conduct of some shipping disputes, as what was once a relatively cheap and highly effective method of securing claims against parties with few visible assets is no longer available. Debate has continued intensively as to the effect of the *SCI v. Jaldhi* decision on attachments which had been obtained previously. Many theories were given by New York law firms, however the Association's experience suggests that much comes down to the discretion of any individual judge.

Another much talked about ruling, this time from the English Court, was that of the ZENOVIA, whereby a charterer who gave a notice of redelivery was allowed to withdraw that notice when the possibility of an additional voyage within the agreed charter period presented itself, even when the owner had already taken steps to refix the ship in reliance on the original notice. The decision has been heavily criticised, however, it remains the position that unless there is clear wording in a charterparty to the contrary, approximate notices of redelivery can be given and withdrawn at will.

Throughout 2008 and 2009 the Association has seen a significant increase in claims and indeed the cost of claims. In one sense this was inevitable given the size of the claims and the level of intensity required. The Managers expanded their Value for Money programme ("VfM") in order to provide much better value to Members for the legal services provided. The implementation of Preferred Legal Partners and Approved Providers means that the Association is much better able to work with these providers to achieve the overall goals of the VfM programme. The firms recognise the importance of the Association and its Members, their collaborative responsibilities and the need to work to achieve the most appropriate outcome in any given case. The Managers and the Board are committed to this programme and will be seeking further enhancements in the years ahead.

One area which the Association is focusing upon is in the area of active claims management. In the Managers' view much more needs to be done by all those who participate in the English litigation process. With LMAA arbitrations the arbitrators play a key role in how the litigation is conducted. A more active engagement in the process leads not only to a speedier resolution of claims but as importantly a more cost effective results driven process. The Managers are committed to making sure that LMAA arbitration, which continues to be the venue of choice for maritime dispute resolution, is responsive to the needs of Members and is adaptable to changing market circumstances.

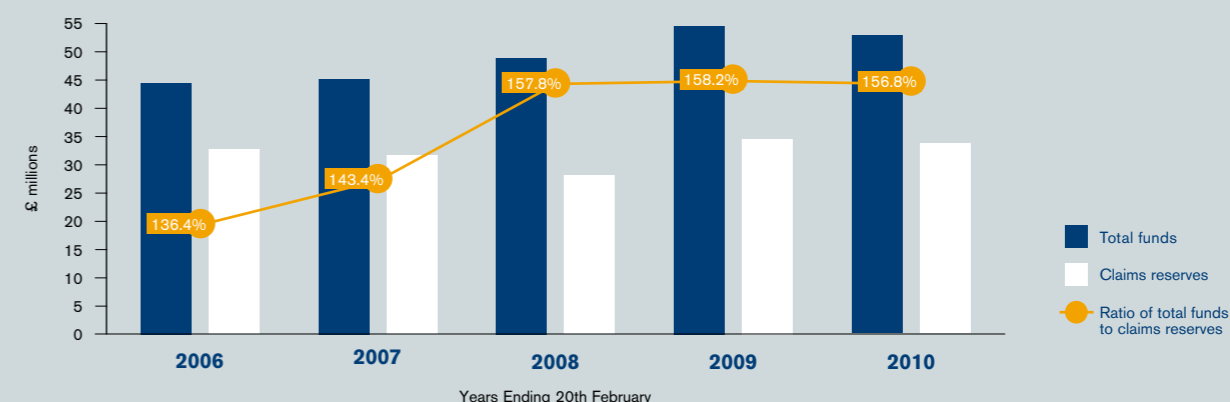
Looking forward, the consequences of the 2008 financial crisis will continue to be reflected in both arbitration awards and Court decisions in the years ahead. Market conditions in part appear to have stabilised which should result in claims trends returning to normal levels. There are nevertheless, other challenges on the horizon – the impact of the EU Low Sulphur Directive, proposed sanctions against Iran – these issues will impact on Members and legal advice will undoubtedly be necessary in order to guide Members appropriately through these and other uncharted waters.



## Financial Highlights 2010

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### Total Funds & Claims Reserves



The table set out below presents the combined results and reserves of the Club and its quota share reinsurer, the UK Defence Insurance Association (Isle of Man) Ltd, for the financial year ending 20th February 2010.

- Premium income rose by 28% in 2009/10, to £18.3million, assisted by the strengthening of the US Dollar exchange rate against Sterling compared with the previous year.
- Investment return totalled £1.8million, reflecting the Club’s conservative approach to investment policy. However, there were net exchange losses resulting from the hedging of premium income and the weakening of the US Dollar against Sterling during the course of the year.
- Net claims incurred, including the change in provisions, rose from £14.5million to £14.7million. Although the 2008 policy year showed a further deterioration as a result of the continued impact of the financial crisis and downturn in shipping markets, and 2009 policy year was also affected to a lesser extent, these were balanced by improvements in prior years’ reserves.
- The net result is that despite the turbulence caused by the 2008 financial crisis and market downturn the Club continues to be strongly placed financially with assets of £52.4million, free reserves of £19.0million and a ratio of assets to liabilities of 157%.

Year ended 20th February 2010	2010 £'000	2009 £'000
<b>Income and Expenditure Account</b>		
Calls and premiums	18,344	14,301
Reinsurance premiums	(383)	(363)
	<b>17,961</b>	13,938
Net claims incurred	(14,674)	(14,466)
Acquisition costs	(2,102)	(1,955)
Net operating expenses	(1,549)	(1,379)
	<b>(18,325)</b>	(17,800)
Operating deficit	(364)	(3,862)
Investment return and exchange (losses) / gains	(621)	6,467
(Deficit) / surplus before taxation	(985)	2,605
Taxation	89	(460)
(Deficit) / surplus after taxation	<b>(896)</b>	2,145
<b>Reserves and Capital</b>		
Total funds	52,374	54,043
Claims reserves	(33,397)	(34,170)
Free reserves and capital	<b>18,977</b>	19,873
Total funds / claims reserves	<b>156.8%</b>	158.2%

Strength with independence.

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