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THE CHANGING PICTURE OF RISK



CEFOR ANNUAL REPORT 2006



contents

The Chairman's Address	4
Managing Director's Report	6
The CEFOR Marine Insurance Market 2006	8
Ocean Hull	14
Solvency II	20
Norwegian Marine Insurance Statistics (NoMIS)	24
P&I	32
Coastal and Fishing Vessels	36
Cargo Insurance	38
CEFOR Board of Directors 2006	40
CEFOR Organization and Staff	42
CEFOR Members 2007	43

THE CHANGING PICTURE OF RISK

IUMI	
In search of the best and the brightest	11
INTERTANKO	
Adapting to the dynamics of change	12
BARBER SHIP MANAGEMENT	
Meet the risk: Rethinking shipping's collective future	18
ABS	
Risk, class and the courts	23
IMO	
Safeguarding the engine of the global economy	35

The changing picture of risk

The rapid growth of global economic development, combined with a corresponding reduction in trade barriers, has created a Golden Age of world trade. The global flow of goods, raw materials and energy has put pressure on global shipping capacity, resulting in high newbuilding orders and record freight rates.

These changes have had a significant impact on marine insurance. Increased day rates and focus on potential loss of revenue create larger values for Loss of Hire insurance. Shipping companies have revalued their fleets' values upwards, creating higher risk severity. Tighter schedules, increased competition, and crew rationalization have resulted in increased insurance claims.

International political, judicial and regulatory changes have contributed to a growing uneasiness among marine insurers. And as the global marine insurance market continues to evolve in response to shrinking capacity, reduced coverage, increasing rates and greater insured retentions, marine insurers no longer have the luxury of taking a "business as usual" approach.

Today, producing the most comprehensive risk policy with competitive terms and conditions requires time and highly specialised underwriting expertise. Gone are the days when shipowners could make a simple phone call, and within the space of a few hours, receive a quote.

Welcome to the changing picture of risk.

The changing picture of risk



The main theme of the 2006 CEFOR Annual Report is the changing picture of risk in the maritime insurance industry. While this year's contributors to the report will review risks from different perspectives, my comments will focus on how new market realities have influenced the industry.

The fundamental concept of marine insurance is to spread the financial consequences of a single risk on many risk carriers. The idea is simple but smart: The likelihood that an individual or company will be struck by an accident is limited but, if such an accident does occur, the company could face financial ruin. However, if a large number of people or economic entities which are exposed to similar types of risks pool their interests, the financial exposure for the individual is diluted. This concept works more efficiently if the number of risk carriers are large compared to the ultimate financial consequences of the common risk.

When marine insurance was first conceived many centuries ago, it is likely that it operated more as a collective security scheme than a business. The fundamental economic idea was that the unlucky few who were hit by accidents could rely on some financial protection from their luckier peers with the understanding that in time, their roles may be reversed. As a result, insurers were united by their mutual interests. Participants did not focus exclusively on generating profits from the scheme, but to benefit from sharing risk in order to minimize the financial burdens associated with accidents.

In today's global economy, financial realities are challenging the cornerstones of marine insurance. For example, there are many alternative opportunities for investment. Inventive minds with creative business ideas are chasing surplus liquidity in order to transform theories into goods and services that can be traded in the marketplace. Those who are able to present the business world with investment opportunities, where prospects

for profit outperform the likelihood of failure, are the winners of the game. Consequently, the allocation of capital is guided by an equation called risk versus reward. Financial capital has become a faceless commodity with a price tag named "investment return."

Mutual interests and shared destinies are not the concern of modern capitalism. Any project, business proposal, economic activity or industry has to provide the outlook for a net financial gain that outbalances the inherent risks involved. Marine insurance is no longer precluded from this economic reality. Marine insurance has to be profitable not only in absolute terms but also related to risks carried by our industry in order to attract and preserve from investors the capital base needed to protect the long term interests of the insured. This fact is independent of the legal framework in which marine insurance is performed. Mutuals and limited companies are facing the same competition for a scarce resource called risk capital. The uniting forces of common interests are about to be defeated by the interests of the individual. For this reason, we can conclude that the cornerstone of marine insurance, mutuality based on common destiny, is under attack.

Economy of scale is another buzzword in modern economics in line with the concept of return on investment. Larger economic entities are regarded as better equipped to make use of financial resources more effectively than smaller entities. As in other industries, this trend has led to consolidation, both via mergers and acquisitions, and through reinsurance. Consider that in the 1970's, some 130 syndicates at Lloyd's wrote marine insurance. Today, probably no more than ten to fifteen syndicates are still in the marine market. A similar trend has occurred in Norway. In the mid-1970's there were some 30 insurance companies writing marine risks. Today, there are less than ten.

The net consequence is that the financial risk of the system is increasing because fewer participants are carrying the financial load. In addition, manifold, the other cornerstone of marine insurance, is under attack. For marine insurers, managing these new market realities will require that we keep our own house in good order by writing sound business, and stay focussed on the balance sheet.

Bjørn Hildan
Chairman

"Chi non risica, non rosica"



"Before long, we may find more sailors behind bars than in bars."

Tore Forsmo

Over the last few years, shipping has seen a boom as never before. New fortunes are being made and old fortunes are growing larger seemingly every day. At the same time, the maritime industry is operating within a global framework of increasing complexity and risk exposures.

A large shipbuilding orderbook combined with relatively few vessels scheduled for scrapping has created an urgent demand for properly trained and qualified crews. The crewing issue represents a tremendous challenge for the operators of new vessels, operators struggling to retain crew on existing vessels, and the entire industry, which cannot afford to cannibalize manpower supply. For marine underwriters, the scarcity of experienced qualified seafarers remains a significant challenge.

Another emerging issue is the ever expanding size of today's vessels. We are seeing cruise vessels bordering on 6000 pax, while the latest generation of container vessels have a capacity of 13,000 TEUs. These massive vessels represent huge risk exposures per keel, which is creating a growing concern among insurers.

At the same time, legal and operational restrictions have become more complex. With industry organisations, individual companies and regulators adopting zero-tolerance policies, there are increasingly severe consequences for environmental discharge and loss of human lives – including criminal sentencing and higher limits on liability. Today, seafarers and ship operators may face jail time for accidents – even when their conduct was appropriate during critical situations. Indeed, before long, we may find more sailors behind bars than in bars. Shipowners are already facing a trend where experienced masters, first officers and chief engineers leave the ships for jobs on land simply because they no longer want to have the threat of criminal investigation hanging over them for accidents they did their best to avoid. While governments are constantly working for safer shipping both for people onboard the ships and the environment, the criminalisation of seafarers is threatening to drive the best seafarers off the ships which is undoubtedly counterproductive to safer shipping.

The increasing volume of cargo and number of both seafarers and passengers at sea, combined with more stringent environmental regulations, will challenge underwriters to carry more risk with increasing liability.

The European Solvency II and new solvency regimes will introduce requirements on insurers to properly address the risks and improve the management of their capital. This may have a substantial impact on our industry and the way we run our business.

A greater focus on Corporate Social Responsibility, Corporate Governance, business ethics and transparency will continue to influence how underwriters interact with the shipping industry.

While all these issues are changing the picture of risk, the question remains: Should marine insurers view these changes as a threat or an opportunity?

"We are capable of taking risks and assessing them beforehand. Others may be brave out of ignorance, but when they stop to think, they begin to fear." These words are just as true about CEFOR and our market today as they were more than 2400 years ago, when Pericles in his famous Funeral Oration to the fallen Athenians described their remarkable ability to assess risks before making decisions.

Marine insurance is all about how to correctly identify, analyze, prize and transfer marine risks. Our business is not to avoid risk, but deal professionally with the risks we and our clients face at any given time. Indeed, the ability to define what may happen in the future, assess associated risks and uncertainties, and to choose among alternatives lies at the heart of any risk management system.

The word 'risk' derives from the early Italian word *risicare*, which means 'to dare'. The notion of risk is therefore related to 'opportunity' rather than to 'threat'. By understanding risk, measuring it and weighing its consequences, risk-taking has become one of the prime catalysts that drive modern society. Our development and constant progress is fundamentally based on our ability to understand and properly handle risk. Risk is not something to be feared, but rather, represents potential and opportunity for growth and prosperity.

We only fear what we do not know. To put it another way: Nothing ventured, nothing gained. Chi non risica, non rosica!

Tore Forsmo
Managing Director

Building competence

Summary

Gross premium income for direct marine insurance in the CEFOR market in 2006 totalled USD 1,530.1 million (NOK 9,823.9 million), compared to USD 1,259.7 million (NOK 8,123 million) in 2005. (Note: The 2006 figures are not directly comparable with the 2005 figures as explained in the "Ocean Hull" and "Coastal and Fishing Vessels" sections.) Premiums for marine hull and P&I insurance are paid in US dollars.

Norwegian Ship Safety Act and the Professional Secrecy of Marine Insurers

In last year's Annual Report, we addressed the problem CEFOR experienced in gathering enough political support to create a legal basis for the right of Norwegian marine insurers to share and exchange information about the condition of ships and how they are being managed, maintained and operated in order to avoid insuring sub-standard vessels. We are pleased to report that this issue is now addressed by Section 71 of the Norwegian Ship Safety Act, which entitles marine insurers to share information which is directly relevant to the safety of the ships they insure with other insurers, classification societies, international marine insurance and maritime organisations, or Norwegian and foreign maritime authorities.

The Ship Safety Act was passed by the National Assembly in the beginning of February 2007 and is expected to enter into force 1 July 2007. From that date forward, Norwegian underwriters will be able to fully take charge in international efforts to reduce substandard shipping.

The Ship Safety Act will apply to all Norwegian vessels worldwide and foreign vessels in Norwegian waters. The concept of seaworthiness as a measure of ship safety, which is a term in the current Seaworthiness Act, has been abandoned in the new Act in favour of the concept of safety management derived from the ISM Code. The new Act names

the shipowner as the main party responsible for the ship and management.

Nordic education scheme for marine insurance

In the last few years, marine insurers have had a challenge recruiting qualified marine insurers to manage the complexity of the changing picture of risk. To deal with this issue, CEFOR has been active in developing training and educational programmes.

In the autumn of 2006, a course in Marine Insurance Law was established at the Scandinavian Institute of Maritime Law, University of Oslo. The course will run for the first time in the spring term 2007. The course in Marine Insurance Law deals with the rules and regulations regarding marine insurance. The course is purely contract law, and includes the Norwegian Marine Insurance Plan 1996, conditions relating to Insurance for the Carriage of Goods and P&I insurance conditions. The course is divided into two main parts. The first part relates to the rules that are common for all or most marine insurance branches. The second part relates to the rules for the individual branch, i.e. hull insurance, insurance on interest, war risk insurance, loss of hire insurance, P&I insurance and cargo insurance.

This course is offered both as a Bachelor and Master short course, and will be taught every spring term at the Faculty of Law in Oslo.

Looking forward, CEFOR is also involved in an exciting new initiative to further develop industry competence. Planning is currently underway to establish a Master's degree in Marine Insurance and Risk Management. While the project is still in its preliminary stages, the process has been encouraging. Developed in co-operation with the University of Oslo, the University of Gothenburg, Copenhagen Business School, and the Norwegian University of Science and Technology, the programme is intended to comprise four modules and a Master thesis, totalling 90 ECTS (European Course Credit Transfer System) credits. The programme will run for two years on a part-time basis, and lectures will be held at the respective universities. All tuition and exams will be held in English. The modules will consist of Marine Insurance Law in Oslo, Average Adjusting in Gothenburg, Risk Management - economical aspects in Copenhagen and Risk Management - technical aspects in Trondheim.

Norwegian Ship Safety Act, Section § 71

Regardless of the obligation to professional secrecy described in the Act of 10 June 2005 No. 44 relating to insurance companies, pension funds and their activities (section 1-6), marine insurance companies are permitted to share information which is directly relevant to the safety of the ships they insure with other insurers, classification societies, international marine insurance and maritime organisations or Norwegian and foreign maritime authorities. The first paragraph of Section § 71 applies

correspondingly to ships that have been insured by the entitled insurance company during the last three years prior to the date upon which information is requested, or upon the date the insurance company hands over the information without being requested.

The insurance company has the obligation to send the assured a copy of the information rendered pursuant to subsection 1. Where the information has been given orally, it shall be sufficient to notify the assured that such information has been given and to whom the information was given.

The programme will be coordinated from the Scandinavian Institute of Maritime Law, and candidates will be awarded their degree from the University of Oslo. The admission criteria will be three years of Bachelor-level education, two years of relevant work experience, as well as documented proficiency in English.

Ocean Hull

Premium income in the CEFOR ocean hull market for 2006 amounted to USD 766.7 million (NOK 4,922.5 million) excluding war risk. The 2005 figures were USD 576.9 million (NOK 3,720 million) but are not quite comparable to the 2006 figures, due to the fact that the 2006 figures include the Nordic accounts of Codan and TrygVesta Marine.

Despite the fact that the capacity within the international marine insurance market continues to exceed demand, it has remained stable over the last few years. This does not mean that the situation will remain static. Margins remain thin and changes to the legislative environment will certainly put pressure on some insurers to improve their performance and strengthen their capital base.

It is therefore no surprise that Solvency II became an issue for marine underwriters in 2006, despite the fact that it is not likely to be implemented until 2010. The revised measure will introduce a new regulatory capital framework for the non-marine and marine insurance industry that will better reflect the insurer's overall risk position.

There are a number of trends which are expected to continue over the medium-term which will require underwriters to analyse risks more carefully in future. One is the further development of shipping technology and the increased size of ships found in most segments.

Recently, the market has suffered some sizeable marine claims. Irrespective of the direct causes

of these claims, it is evident that extreme weather has had a direct impact, and there is no evidence that these unusually severe weather patterns will not continue. This is an international, global challenge, one that marine underwriters must be prepared to meet.

However, at the current premium levels, and with the existing claims trends, it has become increasingly difficult for marine insurers to write profitable Hull & Machinery coverage, leaving little margin to manage the challenges listed above.

P&I

The CEFOR P&I Clubs Gard, Skuld and Swedish Club booked USD 549 million (NOK 3,524.5 million) for the 2006/2007 policy year.

While the number of claims per vessel decreased over the last eight or nine years, this positive trend has turned and once again, we are seeing an increase. During the last few years, many clubs have reported an increase in claims and in particular claims costs. This trend in increasing claims costs has now been confirmed by all clubs, and it is clear that the increase is quite dramatic.

According to the International Group, pool costs are also increasing. In the Group's more than 30 year history, 2004 was the most costly with a combined cost of over USD 350 million spread on about 16 cases. Unfortunately, 2006 may well exceed this figure, with costs running as high as USD 450 million divided between more than 20 cases.

P&I clubs have noted that owners, operators and charterers work their ships harder in a booming freight market, which has caused an upsurge of navigation-related incidents such as groundings, collisions and strikings. Good freight markets mean generally higher cargo values, which serve to increase claim costs for loss of, damage to or delay in delivering cargo.

In addition, new technologies have made it possible to construct vessels that can take 14,000 containers and passenger vessels with a capacity of 6,000 individuals. The risk exposure for both these categories of vessels has increased dramatically due to the vast numbers involving individual risks.

The right to limit liability is a well established practice within shipping. Many will go as far as claiming that this is one of the



In search of the best and the brightest



Deirdre H. Littlefield
President of IUMI and Director of Business Development for Starr Marine

cornerstones of the carriage of goods by sea. Clubs are now observing a clear trend among European politicians to limit this fundamental right, and in some instances challenging its whole existence. From a shipowner and insurance perspective, this trend is of great concern.

Coastal and Fishing Vessels

In 2006, gross premium income amounted to USD 120.3 million (NOK 772.5 million) compared to USD 102.7 million (NOK 661.9 million) in 2005. However, it should be noted that the 2006 figures include the Nordic hull account of TrygVesta and are thus not comparable with the 2005 figures.

Strong competition in the coastal and fishing vessel market continues to hold premiums down in most segments, leaving margins insufficient to cope with large losses. This is especially evident in the supply and offshore vessel segment where insurance values are increasing steadily. Rating should be based on proper risk evaluations rather than short term considerations.

Cargo

The premium income for the Norwegian cargo insurance market (excluding war risks) totalled USD 58.1 million (NOK 373.1 million) in 2006. Premium income in 2005 amounted to USD 63.1 million (NOK 406.7 million). Premiums for cargo insurance are mostly paid in Norwegian Kroner. The 2006 figure is not comparable to previous years due to the fact that CEFOR member Industriforsikring no longer does business with the former Norsk Hydro company, Hydro Agri. In 2004, Hydro Agri was listed on the Oslo Stock Exchange as an independent company under the name Yara International ASA.

Vigorous competition in most market segments continued throughout 2006, both among CEFOR members and in international markets. The pressure on cargo premiums increased during 2006, when both new and established domestic companies, combined with international players, sought a larger share of a limited domestic market. In spite of fierce competition and sliding rates, Norwegian cargo business remains profitable.

The CEFOR Marine Insurance Market 2006 Market shares, all sectors

Gross premium income, direct insurance 2006: 1530.1 USD m

USD 1= NOK 6.42	NOK mill.	USD mill.	%	
Hull	5887.0	916.9	59.9 %	
P&I	3563.6	555.1	36.3 %	
Cargo	373.1	58.1	3.8 %	
Total	9823.7	1530.1	100.0 %	
OCEAN HULL*				
Gard	1582.5	246.5	32.1 %	* hull, hull interest, freight interest, loss of hire, builders' risks and mobile offshore units
Norwegian Hull Club	1013.1	157.8	20.6 %	
Swedish Club	402.5	62.7	8.2 %	
Bluewater	434.6	67.7	8.8 %	
Gerling	415.4	64.7	8.4 %	
NEMI	293.0	45.6	6.0 %	
Codan (Nordic)	534.8	83.3	10.9 %	
TrygVesta Marine	246.5	38.4	5.0 %	
Total	4922.4	766.7	100.0 %	
DNK (war risks)	211.9	33.0		
COASTAL AND FISHING*				
Gjensidige	168.4	26.2	22.4 %	* hull, hull interest, freight interest, loss of hire, builders' risks and fishing (catch & gear)
If	109.7	17.1	14.6 %	
Norwegian Hull Club	110.9	17.3	14.7 %	
TrygVesta Marine	94.4	14.7	12.5 %	
Gard	25.7	4.0	3.4 %	
NEMI	45.0	7.0	6.0 %	
Coastal Marine Clubs*	198.6	30.9	26.4 %	
Total hull	752.7	117.2	100.0 %	
P&I				
Gard	2141.7	333.6	60.4 %	
Skuld	1081.1	168.4	30.5 %	
Swedish Club	301.7	47.0	8.5 %	
P&I coastal & fishing	19.8	3.1	0.6 %	
Total	3544.3	552.1	100.0 %	
DNK (war risks)	19.3	3.0		
Cargo (all insurers)	373.1	58.1		

While catastrophic events such as terrorism and natural disasters certainly pose serious threats to the marine insurance industry, our inability to attract top flight talent to our business poses a far greater threat to the long-term health of marine insurers.

There is perhaps no greater challenge facing marine insurers than attracting top flight talent to our business. There are a number of reasons why this issue has become so important. First, the marine insurance sector has become increasingly complex, and requires experienced professionals to manage emerging challenges.

For example, one of the most pernicious threats to shipowners is misdeclared cargo on containerships. It threatens the safety of the vessel, and the thousands of containers they can now carry put the crew in harms way, present a potential pollution hazard and make it impossible for underwriters to accurately judge the risk they are assuming. It is also something that could be dealt with if all parties involved – Vessel Owner, Classification Society, IMO, Cargo, Hull and P&I Underwriters – were to join forces and find ways to address.

In a recent IUMI speech, Captain James McNamara of National Cargo Bureau said that as much as 20 per cent of cargo in international trade is potentially dangerous and is incorrectly declared (either intentionally or in error). He pointed out that containerized cargoes have always presented an easy opportunity for misdeclaring or smuggling cargoes into or out of a country. With the emphasis on "just in time" delivery and the constant pressure for speed, Captain McNamara said security in this mode of transportation has become a major concern for us all.

Managing such complex issues will require marine insurers to develop strategies and work with the industry, regulators and class societies. However, without the ability to attract skilled professionals to our industry, marine insurers may struggle to protect its interests as these vital issues are addressed in future.

Today, marine insurers must compete with other businesses that are perceived to offer higher wages and greater opportunities. Consider that the bonuses paid this year by global investment firms provide a financial incentive to prospective employees against which marine insurers (and most others) cannot compete.

In addition, insurance – in many nations – is not viewed as highly as other financial services and professions. To counter this perception, marine insurers need to do a much better job of letting college students and their career advisors know of its critical place in the global trading community and the fascinating challenges that result from that.

At the same time, we should take a closer look at ourselves and ask some hard questions. Do we appropriately value young talent in our own enterprises? Do we encourage a culture of innovation and creativity? Can we remove obstacles to advancement of younger employees? Do we aggressively seek women and minorities to work in our business?

IUMI is working hard in this area. We have an obligation to identify the marine leaders of tomorrow and introduce them to IUMI. We are encouraging our member associations to bring new talent to our annual conference and participate in our committee structure. Our website also is being revamped to encourage its use by marine insurers regardless of their tenure.

Marine insurers justifiably pride themselves on their great traditions. Let us make sure our commitment to these traditions does not impede our ability to attract the best and the brightest to join us.

“The future of both marine insurance and the shipping industry are tied to our ability to hire, train and retain talented professionals.”

Deirdre H. Littlefield

“The greatest threat to the industry today comes not from external sources, but from how we as an industry reflect the dynamics of change.” Peter Swift

Adapting to the dynamics of change

Peter Swift
Managing Director, INTERTANKO



Perhaps no other sector in the industry is more sensitive to the changing picture of risk than the tanker industry. And with fresh challenges emerging seemingly every day, the pressure is on for the industry to be more responsive to change.

From regulatory challenges to crewing issues, hard worked vessels to environmental concerns, the tanker industry faces many challenges. Yet perhaps the greatest threat to the industry today comes not from external sources, but how we as an industry reflect the dynamics of change. Are we moving fast enough? Are we reactive or proactive? Are we working together to meet these challenges?

As a somewhat conservative industry, shipping is not known for rapidly embracing change – and tanker owners are no exception. INTERTANKO, which represents about 260 tanker owners throughout the world, works with members to try to identify common challenges and helps set the agenda. However, getting so many members from so many different parts of the world to act together to manage emerging risks can be a challenge. We cannot wait for everyone.

In today's rapidly changing industry, inaction is not an option. First, the work to recruit, train and retain qualified seafarers has become critical. Most accidents, incidents and near misses involve a degree of human error, and in a climate of zero-tolerance, increased regulations and tough punitive measures for substandard performance, skilled crews are not only an advantage, but a necessity. This challenge is complicated by the fact that the growing shortage of skilled crews is being felt by the entire industry, creating increasingly fierce competition for manpower.

Second, tanker owners may also find themselves the victim of their own success. With the industry reporting another strong year, demand for transportation of oil, chemicals and products has

continued to rise. For this reason, owners may in some instances have found fewer opportunities to take vessels off-hire for running repairs, or may have decided not to retire older tonnage. While the industry's accident record shows a long-term improvement trend, and there is no correlation between older tonnage and accidents, there are some concerns that a recent increase in incidents may in part be due to the harder working of vessels, machinery and people.

Indeed, we may have seen signs of a shift in this trend in 2006. While not all data has been collected or analysed, preliminary reports suggest that there was a measurable increase in reported engine stops, several of which had the potential for more serious consequences, as well as an increase in the number of collisions (contacts) and groundings. This trend may be explained to a large part by the industry's increased transparency, as more tanker operators are willing to share information.

However these emerging risks may affect the tanker industry, we cannot afford to sit idly by and react to each incident as it occurs. Rather, tanker owners have learnt to work more closely together, and find common ground with other organisations, including class societies and marine insurers. In addition to encouraging members to share information, and pushing for legislative and other changes to permit greater information exchange, INTERTANKO works closely with class and marine insurers to gather and publish information to benefit the industry as a whole.

It is certainly true that the only constant is change. However, in today's rapidly evolving maritime industry, it is the pace of change that is never the same. To manage the changing picture of risk will require not only that tanker owners learn to be more proactive, but that they ensure that our industry more fully recognises the dynamics of these changes.

2006 – Navigating the challenges

Premium income in the CEFOR ocean hull market for 2006 amounted to USD 766.7 million (NOK 4922.5 million), excluding war risk. The 2005 figures were USD 576.9 million (NOK 3,720 million) but are not quite comparable to the 2006 figures, due to the fact that the 2006 figures include the Nordic accounts of Codan and TrygVesta Marine.

The shipping market

2005 saw a 6 - 7% increase in the world's tonnage, a trend that continued throughout 2006 with the world's shipping markets seeing significant fleet expansion in Germany, Greece and Asia. In 2006, consistent with the previous few years, the growth in seaborne transport has been driven by the continued economic growth in China and increased trade with all parts of Asia.

With the market continuing to grow through 2007, the shipping industry will face a number of short-term challenges going forward. The first is the availability of sufficiently qualified crew. This issue is likely to become more challenging in the years to come – one that is closely related to the growth in accidents being caused by human and/or navigational errors. The other challenge is new technology, which while being vital to the industry's ability to move forward, often creates difficulties in its initial stages of adoption.

Claims development

Utilisation rates in most shipping segments continue to be very high and this, combined with the short term challenges noted above, means that the marine insurance industry should be prepared to pay increased claims costs in the coming years. Although the frequency of claims has fallen slightly, costs have continued to rise, driven by the scarcity of yard capacity, increasing raw material and labour, growing cargo values and the high price of oil.

World-wide, shipyards are operating at full capacity. The waiting time for repairs is often several months

and prices have increased considerably. As a result, the cost of Hull & Machinery and Loss of Hire claims has increased, often resulting in heavily damaged vessels being declared total losses.

While there are difficulties in finding a solution or formula for these issues in the short term, the marine insurance market needs to put these vital issues on the agenda. With an increasing focus from charterers, international bodies and the insurance market itself, we believe that the shipping industry will find solutions, and marine underwriters are expected to look closely at these topics in their risk evaluations.

The insurance market

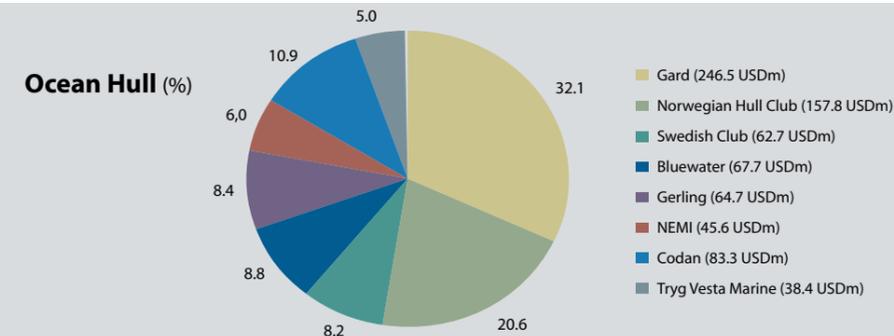
Despite the fact that the capacity within the international marine insurance market continues to exceed demand, it has remained stable over the last few years, with only a few new entrants from Bermuda, Hong Kong and Singapore and no particular changes to the coverages offered.

This market stability has come about for two reasons. The first is that businesses appear to be exercising improved underwriting discipline – not pricing to gain market share – and are therefore controlling potential losses. The second is the recognition that clients place a greater value on security and service, attributes which cannot be created overnight by new capacity. This trend has created barriers to entry for new players.

This does not mean that the situation may not change as margins remain thin and changes to the legislative environment will certainly put pressure on some insurers to improve their performance and strengthen their capital base. Despite the fact that it is not likely to be implemented until 2010, Solvency II legislation became an issue that started to demand the attention of our industry in 2006. The Solvency II legislation will introduce a new regulatory capital framework for the non-marine and marine insurance industry, which will better reflect the insurer's overall risk position.

Challenges

There are a number of trends which are expected to continue over the medium-term and will require underwriters to analyse risks more carefully in the future. The first is the further development of shipping technology and the increased size of ships found in most segments. Certainly, investment in larger, more technologically



advanced vessels represents creative and courageous developments by the shipowners. The marine insurance industry must both participate in this process, and contribute to its development.

However, these innovations place additional pressure on underwriters to more fully understand new technologies and the possible consequences which may arise from their operation or failure, from an underwriting point of view. The industry must be willing and able to price these increased risks appropriately.

Another consequence of a prosperous shipping market is the extension of a vessel's working life and how this impacts quality. The insurance industry needs to improve the risk selection and segregation based on the differences in the quality of these vessels if it is to underwrite profitably.

Recently, the market has suffered some sizeable marine claims. Irrespective of the direct causes of these claims, it is evident that extreme weather has had a direct impact, and there is no evidence that these unusually severe weather patterns will not continue. This is an international, global challenge, one that marine underwriters must be prepared to meet.

However, at the current premium levels and the existing claims trends, it has become increasingly difficult to write Hull & Machinery business profitably, and there is certainly little margin left to cover the challenges listed above.

The human element

Over the last few years, H&M insurance statistics reflect an increasingly alarming trend, not in the frequency of incidents, but of claims costs of a nautical nature related to human errors and omissions claims. This class of claims encompasses

groundings, collisions, strikings and others. A number of causes for this disturbing trend have been suggested, but so far, none fully explain this adverse development.

However, it should be noted that there is a shortage of quality, experienced seafarers. Shipowners and ship management companies have struggled to recruit new seafarers, and retain them throughout their whole working career. This particular issue is complicated by the fact that vessels have become increasingly sophisticated, requiring crews with more technical training.

In addition, it should be noted that the number and pace of newbuildings will increase the total world fleet substantially over the next five years. Even taking into account the expected scrapping of vessels, the industry will require an estimated 60,000 seafarers by 2011. As shipping companies scramble for good crews, it may not be wise to assume that all of the 60,000 new personnel entering the shipping industry will have and maintain the desirable standard and quality – even if they are in compliance with the minimum international crewing certification standards. Underwriters must take an active stand on this potential increase of insurance risk associated with the shipping industry – an issue which will result in an even more unpredictable claim situation for nautical claims.

The main task of any member of a ship's crew, and the officers in particular, is the obligation to bring the cargo and the ship safely and undamaged from the loading position to the point of discharge. During a voyage, the ship will encounter a number of challenges including those created by nature and those created by man. It may be argued that ship operators, charterers and governmental authorities alike are pushing the crew beyond acceptable limits in their efforts to make transportation as efficient and cost effective as possible.

Forced to manage an increasing amount of demands from the outside world, the crew may at times operate the vessel at an unacceptable fatigue level. Marine underwriters note with disbelief that the IMO (International Maritime Organization), the UN body looking after maritime affairs, recently decided not to support the efforts to limit the working hours of vessels' crew by regulating the resting time. Crew fatigue has caused, and will continue to cause, casualties, and underwriters should ensure that this risk element is a part of their risk assessment.

Commercial concerns

Commercial pressure from clients, intermediaries, management and outside stakeholders places a heavy burden on the daily life of underwriters. Clients want maximum security and coverage for less premium, while intermediaries want to prove their value to their clients by creating sophisticated insurance and risk relief arrangements not previously seen and tested. At the same time, insurance companies and underwriting entities seek profitable growth on behalf of the capital invested, and rating and governmental bodies require risk management systems to ensure an adequate capital base and return on capital.

Thanks to non-competition regulations, larger underwriting entities assuming more of the risk themselves and the emergence of new markets joining the global marine insurance scene, the marine insurance market has become more fragmented over the last ten years. Meeting the demands of this fragmented market represents a significant challenge for the prudent underwriter. Today's underwriter lacks the comfort and security previously enjoyed by the underwriting community and a strong slip leadership. Often operating alone, underwriters face significant risk evaluation and pricing challenges. For this reason alone, underwriters must learn to resist pressure from both clients and intermediaries to reduce or waive the minimum standards required in the evaluation of coverage, compliance with safety measures and the pricing of risk.

The Norwegian Marine Insurance Plan, Version 2007

The Permanent Revision Committee concluded its work on the 2007 Version of the Plan in the beginning of October 2006. The printed edition was made available in December and the website for the Plan was fully updated with the Commentary in January this year. Quite a number of clauses are amended in the 2007 Version. In this section we shall briefly highlight the most significant amendments from the 2003 Version.

Nuclear and biochem exclusions (RACE II)

The release of nuclear energy exclusion in § 2-8 (d) and § 2-9 subparagraph 2 (b) is replaced by a wording which is identical to the London market's RACE II Clause. Subsections (1) to (4) correspond to the previous "release of nuclear energy" exclusion with one exception. The exclusion in this subsection (applied only in § 2-8) does not extend to radioactive isotopes, other than nuclear fuel, when such isotopes are being prepared, carried, stored, or used for peaceful purposes. Subsection (5) excludes perils related to chemical, biological, bio-chemical, or electromagnetic weapon.

Perils related to the use of weapons are rarely regarded as marine perils but the same exclusion applies to the war peril clause § 2-9 and represents a new exclusion in relation to the 2003 Version of the Plan.

The RACE II Clause was incorporated in the Plan because the Clause is part of all reinsurance contracts. Consequently, insurers have to include this clause in their insurance contracts in order to avoid any uncertainties and to ensure that there is no gap between the direct insurance contracts and the reinsurance schemes.

War insurance – special clauses for the DNK Cover

The special extended cover offered by the Norwegian Shipowners' Mutual War Risks Insurance Association (DNK) was incorporated in the 2007 Version of the Plan where a new Section 9 was added to Chapter 15. Previously, the special clauses for DNK were part of various clauses such as e.g. § 2-9 of the Plan in addition to the DNK rules.

The concept of unseaworthiness abandoned

The former provision regarding unseaworthiness, § 3-22, has been deleted, since the term is no longer used in the new Norwegian Ship Safety Act. The former § 3-24 regarding safety regulations has been moved to § 3-22. The concept of seaworthiness was introduced

into the Plan in 1930 but over the years, the term became more vague, serving a lesser legal purpose as more and more safety rules were introduced. With this amendment, underwriters will have to hold the assured to the more explicit requirements laid down in the safety regulations.

Change of classification society

Change of classification society shall no longer result in termination of the insurance. Such changes are now subject to the general rules regarding alteration of the risk in § 3-8. Suspension of class, however, will still lead to automatic termination of the insurance pursuant to § 3-14 of the Plan.

Compensation for unrepaired damage

Subparagraphs 1 and 2 of § 12-2 have been amended so as to make entitlement to cash settlement for damage a general right, and to specify the time of settlement and the calculation of compensation. By this amendment the Plan is brought in line with the English Institute/International Hull Clauses.

Inadequate maintenance

Subparagraph 2 of § 12-3 concerning repairing costs of defective frames etc. has been deleted because it is no longer considered to have any practical significance.

Trading Limits

Some adjustments have been made in the Appendices to § 3-15 regarding excluded and conditional trading areas. The waters between Sakhalin and the south tip of Kamchatka have become a conditional trading area.



THE CHANGING PICTURE OF SAFETY AND SECURITY

The development of new, larger and more technically sophisticated vessels has created a renewed focus on safety issues. For example, in the past five years, cruise ships broken the conventional boundaries in terms of concept, design and sheer size.

Yet these remarkable technical achievements have placed a greater burden on designers and operators of cruise ships and ferries to ensure the safety and security of passengers and crews. While much of their focus has been developing systems to manage accidents at sea, new threats are emerging.

According to the RAND Center for Terrorism Risk Management Policy, cruise ships and ferry boats need more protection against terrorist attacks that could kill and injure many passengers and cause serious financial losses.

The RAND study noted that because cruise liners and ferries must allow passengers to move freely, security improvements should focus on developing more stringent and effective means for screening passengers, crew and luggage. Terrorist attacks involving on-board bombs or biological contaminants inserted into the food supply, could strike maritime targets.



At EUR 900 million, the new generation cruise vessel on order by Royal Caribbean International is the most valuable ship ever ordered in the history of commercial shipbuilding. The 220,000 GRT, 5,400 passenger and 2,000 crew ship, a prototype developed under Project Genesis, will be delivered from Aker Yards, Finland in autumn 2009.

“Effective manning strategies must be consistent with the business and competitive strategy of the ship owner or operator in a global economy.”

Geir Sekkesæter

Meet the risk: Rethinking shipping's collective future

Geir Sekkesæter
President, Barber Ship Management



The widespread lack of forward collective planning by the shipping industry threatens to impede the industry's efforts to gain access to an adequate supply of qualified seafarers. And so far, shipping has yet to understand that manning is a collective problem not resolved by unilateral efforts.

As President of the industry's largest global ship management group Barber International, which is responsible for over 8,500 seafarers, Geir Sekkesæter has a unique insight into this issue. And according to him, the industry's current manning initiatives are unsustainable and if not rectified quickly, the industry will face one of the greatest risk periods of all times.

“The shipping industry has been whining and moaning about the shortage of skilled seafarers for the last decade. The majority of ship owners and managers have been scrambling to find their own solutions, trying to solve the problem themselves. No one company, including Barber itself, can solve the manning issue. This is a major, major issue which will take the collective efforts of several dedicated parties,” says Sekkesæter.

Today's unilateral approach to the manning shortage has created a highly competitive and unsustainable crewing market. Many shipping companies have invested heavily in developing and cultivating a pool of trained seafarers, only to lose skilled people to companies willing to pay higher salaries.

“Like other market players, we are under the constant threat of losing our skilled people to companies that don't invest in training, that don't build up quality seafarers. In today's global market, we train them, but might not keep them. Few have taken the responsibility to manage the situation responsibly,” he says.

So what can be done? For Sekkesæter, rectifying the manning problem is neither simple or complicated. It's just a matter of engaging likeminded partners, ready to create a shared pool of quality seafarers: Partners that view seafarers as strategic global assets.

“We cannot bear the costs of training ourselves, but we can work collectively with ship managers and owners to develop a deep, educated and qualified pool of seafarers. An aggregate of partners can establish first-class crew career incentives and retirement packages,” says Sekkesæter.

Though competitors, Barber sees no reason not to link up with ship managers like V-Ships, Hanseatic, Columbia or others to build maritime colleges or universities from which to extract competent crew. “In a global world with increased transparency, we have to stand together. Like other segments in the industry, ship managers, owners and governments, must consolidate their crewing strategy into a common agenda. We must work together,” says Sekkesæter.

The era when individual shipping companies established their own crewing offices in India or The Philippines fleet is over. Global shipping demands a united effort is to map the collective responsibilities and capabilities to best manage the future manning challenges. Widespread industry cooperation will define what factors are predominant to build and best manage critical seafarer resources.

To manage shipping's greatest risk, manning, the industry needs cooperative strategic planning to formulate an integrated seafarer strategy outlining where the industry should be heading.

“Cooperative strategic planning is a tool to help do a better job, focus talents and energies, assess and adjust our direction in light of performance and a changing shipping environment. Being strategic is to be clear about manning objectives, resources and expected results and combining these in response to the wider shipping context in the short- and medium term,” says Sekkesæter.

Disturbing news, such as the industry's shortfall of 3,500 new and experienced crewmembers required to to man 150 LNG newbuilds does not sway Sekkesæter.

“Collectively, the shipping industry can meet the future manning demands, but continued independent efforts will create a highly volatile situation. At Barber, we have formulated clear strategic seafarer objectives. We have defined our strategy to be pursued, outlined clear and measurable expected results and identified a range of partners and their respective roles.

“Effective manning strategies must be consistent with the business and competitive strategy of the shipowner or operator in a global economy. Shipowners must examine manning issues and strategic planning with a long-term perspective. Together, and only together, can we solve the manning problem and the potential risk this represents,” says Sekkesæter.

Solvency II – A capital issue involving more than capital



Although Solvency II is getting well deserved attention, the public marine insurance debate has so far been rather shallow, limited to pecuniary issues regarding lack of reserves and bold company statements of the opposite.

Marine Insurers' perspectives on change is aptly described by Ibsen's Peer Gynt: "Thinking it, wishing it, yes even wanting it – but doing it!?"

When change is something you rather await than initiate, it's no wonder that any spot on the horizon is studied with the same fascination as Moses waiting for a sign to leave the desert.

Background

Solvency II is one of several related reforms involving accounting, solvency and risk management in recent years. A few years ago a similar frenzy raged in accounting and actuarial circles over the new International Financial Reporting Standards (IFRS) set out by the International Accounting Standards Board (IASB). The project changed both name and content several times in the course of its development, and currently the direct effects on non-life insurance seem less than first anticipated. Indirect effects could still be challenging though, especially if IFRS' abolishing of fluctuation reserves eventually gets tax implications.

Another recent development is the rating agencies' reform of capital models and increased focus on enterprise risk management. Rather than focusing on the companies' choice of models, systems and guidelines, the rating agencies are now considering how these tools affect daily decisions. A showroom supercomputer is of no use – if the gut is still in command.

The EU Solvency Regime

European solvency margin requirements have been in place since the 1970s and were only moderately updated with the Solvency I directives in 2002. In Norway and most other European countries,

the current EU requirements have limited relevance, as domestic regulators have developed more comprehensive and sophisticated regulation. Usually this also implies tougher capital requirements.

Although similar in name, Solvency II is fundamentally different in nature. Whereas Solvency I had a pure insurance focus, Solvency II explicitly adds investment, credit and operational risks. Though capital is still seen as the prime guarantor of a company's ability to fulfil its liabilities, the company's strategy, risk management and internal processes are increasingly acknowledged as important factors in the company's financial solidity in general and in the assessment of capital requirements in particular. The scope of the solvency project is thus far beyond (current) solvency. Solvency II is built on three "pillars":

1. Quantitative capital requirements – established by internal or market-wide capital models.
2. Qualitative review of companies' ability to assess and manage relevant risks in strategic planning and daily operations.
3. Disclosure of key information, relevant to market participants (shareholders, policy holders, regulators etc.)

In the first stage of the project, the second pillar was highlighted. The aim was not to implement detailed rules and regulations, but rather agree on general principles for individual company application. The company is best positioned to assess and manage its own risk, and detailed general rules are thus considered counterproductive when encouraging company-specific development of tools and rules. This is also reflected in calls for unprecedented industry participation in the development of the regulations.

All companies in the European Union are encouraged to participate with estimates, calculation techniques and other relevant comments in several rounds of "quantitative impact studies" (QIS). QIS1 was conducted in the autumn of 2005, QIS2 in the summer of 2006 and

QIS3 is scheduled for April-June 2007. In parallel, numerous and voluminous consultation papers and technical specifications are issued, often replaced by new versions before the ink dries on the previous ones. The scale of the project is nicely illustrated by the Solvency II glossary – which is currently a 30 page document. The current timetable forecasts implementation of Solvency II in 2010.

QIS1 and QIS2

In the first round of the Quantitative Impacts Studies (QIS1), very limited guidance was given regarding how to calculate the various estimates, much in line with the spirit of the solvency project. In the better known second round (QIS2), detailed formulas for calculating Solvency Capital Requirements (SCR) and Minimum Capital Requirements (MCR) were defined.

SCR is defined as the capital necessary for the company to meet its liabilities in a 12 month perspective with 99.5% probability¹. This is approximately equal to S&P's capital requirement on an A rated company. If the capital drops below SCR, regulators will follow the company with greater scrutiny. Currently limited guidance has been given as to what this entails. MCR is defined similarly with a 90% probability of survival. If the capital drops below MCR "ultimate supervisory action" will be triggered. As recapitalisation or takeovers are usually considered a better alternative than run-off, MCR is sometimes interpreted as "sufficient capital to make it attractive to take over the company's assets and liabilities for a non-negative price". In QIS2 the MCR requirement was usually slightly above half of the SCR requirement.

The public debate on QIS2 focused on the capital

requirements implied by the proposed regulations. Especially small, mono-line insurers were punished for lack of diversification and volume. This effect was exacerbated by simplistic modelling of the risk mitigating effects of reinsurance and company limits on line size. The smallest companies (< USD 26 million in gross written premium) would thus face a capital requirement of more than two times its net written premium, before adding investment-, credit- and operational risk. Even for the biggest marine mono-liners a dollar of premium would generate capital requirements of between approximately USD 0.8 (short tail) and USD 1.25 (long tail), before considering diversification with the other risk groups.

West of England Ship Owners Mutual Insurance Association made headlines by stating that it needed to double its free reserves to comply with the requirements. Other companies made bold statements that Solvency II was of no concern for them. Willis concludes likewise in their 2006/2007 P&I market review. Statements of this nature seem somewhat premature, given that both the calculations of capital requirements and the companies' capital are bound to change by 2010. Even for companies likely to comply with the capital requirements, appetite for risk might be impaired for fear of breaching the regulations.

This aspect is of special concern for mutuals with limited means of raising capital (apart from reinsurance) and reluctance to jettison members to meet capital requirements. For these companies it is not sufficient to have enough capital to withstand a 1 in a 200 year scenario – they should in addition have enough capital to avoid breaching this criterion. If no post-loss dynamics regarding reinsurance or investment risk is assumed, a capital of MCR + SCR would be required to meet this objective in 9 of 10 years. Few, if any, companies meet this target. In addition, Solvency II involves important compliance issues outside the realm of dollar and cents.

How will Solvency II impact the marine market?

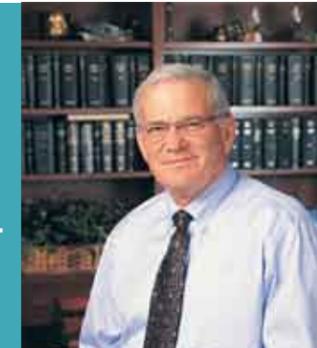
Firstly, insurers with good risk management practises will get a competitive advantage by lower capital requirements and more efficient utilization of its capital. As the marine direct market has a proud tradition of not rewarding risk-taking, this might imply increased risk-taking on investments and other lines of (re)insurance.

¹ Currently SCR is more precisely defined as the 99% Tail Value at Risk – i.e. the expected loss conditional on the loss exceeding the 99% percentile. This is usually fairly similar to a 99.5% percentile (which is also the median of the losses exceeding the 99% percentile).

Risk, class and the courts

In 2006, more ships moved more cargo more safely than at any time in history. Yet that provides no cause for complacency. It is incumbent upon all members of the safety regime to jointly recognize their inter-related responsibilities to further safeguard life, property and the natural environment.

Robert Somerville
President and CEO, ABS



If one more dollar of marine net premium requires the same capital as X more dollars of equity investment, it's straight forward to calculate whether it's advisable to swap marine insurance exposure for equities². Secondly, all companies will have to improve their risk management function and thus gain increased insight in the risks they undertake. Thirdly, barriers to entry will be higher due to tougher capital requirements on small companies and increased requirements on risk management and reporting. This might be counterbalanced by reinsurers seeing newcomers as an interesting niche – due to particular reliance on reinsurance. Finally, increased disclosure of underwriting results might make capital providers reluctant to invest in multi-liners and reinsurers with a complacent perspective on marine results. The same argument applies to P&I and/or H&M mono-liners subsidising core products with profits from more profitable niche products.

Applying Darwinism to the above can lead to different conclusions. The best case scenario is a world where risk is priced correctly, premium cycles are a phenomenon of the past and a culture of sound risk management prevails in every company. The worst case scenario is a world where all the intelligent insurers exit the marine market, leaving the pond for crazy underwriters ready to spend reinsurers' and capital providers' money like drunken sailors. The comfort is that the worst case is not much different from status quo...

Christian Irgens
Norwegian Hull Club

² A real world, somewhat simplistic, QIS2 example goes as follows: 1 dollar of additional net premium written generates the same capital requirements as 2.5 dollar of increased equity investment. If the excess return on equities is 3%, this implies the discounted combined ratio should not exceed $1 - 2.5 * 3\% = 92.5\%$. At a rate of discount of 5% this implies a maximum combined ratio of $92.5\% / (1 - 5\%) = 97\%$. This threshold will increase as equity investments increase and drop as net premium volume grows. The figures will vary substantially from company to company depending on premium volume, length of claims tail, the risk free interest rate and premium vs. investment risk. Recalibrating the Solvency II parameters will also impact the results. The point of the argument is primarily that these calculations can easily be done.

In today's industry, ships and offshore facilities are larger, more complex, more sophisticated and more valuable than in the past. At the same time, new transportation modes for which no empirical experience exists are poised to become realities. These changes have set tremendous technical challenges for the classification societies. The introduction of formalized risk concepts into the classification process is now widespread and covers aspects as diverse as the initial approval in principal of a novel design concept to the establishment of risk-based inspection programs to supplement traditional survey practices.

In practical terms, there is nothing surprising about this technical evolution. Innovation has always been the most marked characteristic of the international shipping and offshore businesses. Classification societies have long been in the forefront of these developments and the remarkable safety record of these industries can, in large part, be attributed to the manner in which owners, designers, class and underwriters have approached these challenges over the last 150 years.

This effective, long standing process is, however, facing a completely new risk that threatens maritime safety. This peril is not of the sea but of the courts. Specifically, classification societies now find themselves exposed to unreasonable claims against which there is no mechanism available to limit liability.

Existing case law has, until now, offered protection to class societies against third party suits and many flag Administrations do extend some degree of protection to their Recognized Organizations (RO). But what has been a long standing, if largely latent concern on the part of the classification societies with respect to this potentially ruinous and unfair liability exposure has become a pressing issue due to two recent developments.

Currently a claim, amounting to USD one billion dollars, has been lodged against a single class society by a third party. And, within the EU a small number of flag States (Italy, France, Spain) have required class societies to accept unlimited liability if they are to be accorded RO status. Additionally, the EU, through its applicable Directive governing the recognition of class societies as ROs (article 6 of Dir.94/57/EC), imposes unlimited liability on ROs acting in a statutory capacity on behalf of an EU Member State in certain cases.

Unlimited liability for claims, even when a party is found to be liable, is not the standard in the maritime field: shipowners, ship managers, charterers, captain and crew, pilots, tugs, salvors, port authorities and all their servants and insurers have a right to limit their liability for negligence pursuant to international conventions. Their liability becomes unlimited only if it is proven that they acted "recklessly with the knowledge that damage would occur."

Flag States may also benefit from protection or immunity granted by national and international public law (sovereign immunity). In most cases, class societies, whether acting in their classification capacity or as ROs, are the sole party not accorded the right to limit their liability pursuant to the specific terms of an international convention.

In the case of a major incident, most, and probably all ROs would not have sufficient financial resources to withstand the relevant claims made under an unlimited liability regime. Should judgment be entered against a class society under such circumstances, the society could be forced out of business as a consequence of a single event stemming from, perhaps, no more than a judgment call made by the attending surveyor.

The threats posed by this two pronged exposure to extraordinarily large claims are sufficiently serious to warrant concerted action by the maritime industry in support of class' attempts to introduce a balanced instrument that would extend to class comparable liability limits to those accorded the other principal sectors of the industry.

"Classification societies now find themselves exposed to unreasonable claims against which there is no mechanism available to limit liability." Robert Somerville

CEFOR: By the numbers

Since 1985, leading members of CEFOR have compiled and analysed statistical information relevant to their Hull & Machinery insurance portfolio. By the end of 2006, the Norwegian Marine Insurance Statistics (NoMIS) database comprised 108,183 vessel years and 33,345 claims. These figures encompass the underwriting years 1985 through 2006.

Portfolio Characteristics

The CEFOR members underwrite a wide range of tonnage. In addition to the conventional segments, the portfolio contains specialized tonnage, such as car-carriers and energy-related units. In terms of number of vessels, the portfolio reached a new "all-time-high" with 10,804 vessels registered on underwriting year 2006, compared to 8,751 vessels reported last year (the latter figure does not include Swedish Club). Excluding vessels below 300 GT, and vessels in the "Other" group, this leaves 10,309 vessels, 338 mGT and 493 mDWT. This represents 25% of the world fleet in terms of number of vessels, 53% in terms of GT and 52% in terms of DWT¹.

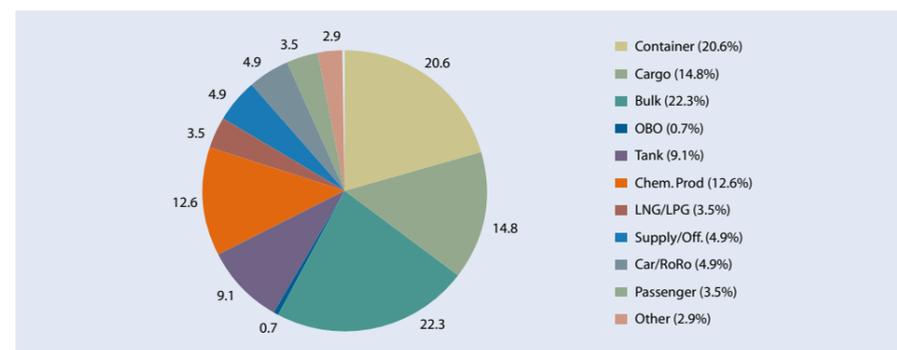
Quality Indicators

Three years ago, we started reporting portfolio "quality indicators". As noted when introducing the concept, it is generally hard to find correlations between "vessel quality" and underwriting profitability in a sound insurance portfolio. Sound underwriting will ensure that only the best vessels with exotic flags and classes will be written, whereas vessels from reputable flags and classes will be accepted with less scrutiny. The resulting portfolio of "exotic vessels" might thus be of higher "quality" than the average vessel in the portfolio.

The average age of registered vessels in 2006 was 12.5 years. This is about the same as in 2005, but lower than earlier years' average of 13.5-14.0 years. The youngest ships in the fleet are as before

¹ World Merchant Fleet above 300 GT by January 2006: 41,110 vessels with 640 mGT and 945 mDWT. Source: ISL Bremen. The NoMIS portfolio does contain some US and Canadian Lakers, not included in the world fleet. On the other hand, the world figures include some of the specialised tonnage excluded in the above comparison.

Number of vessels per type of vessel 2006



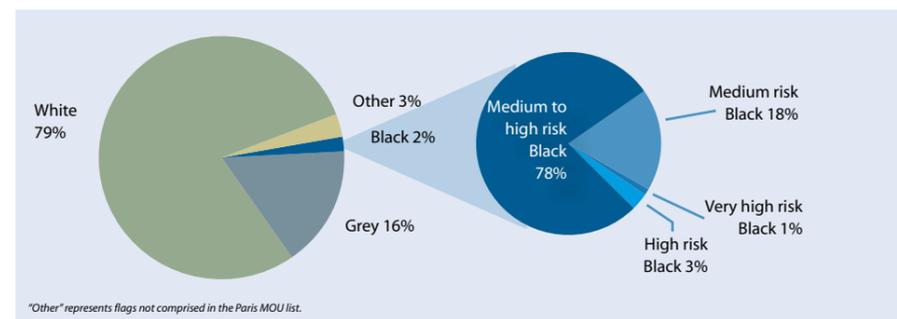
container and tanker vessels, with an average age of 9 years. For tankers this represents a sharp decline from an average age of 13 years only a few years ago. The segment with highest increase in number of vessels is container vessels, which represent 21% of the portfolio in 2006 up from 18% in 2005. Tanker vessels showed a slight decrease from 10% to 9%, while representation of the other types remained quite stable.

DNV, LR and GL have classed the major part of the NoMIS fleet with a share of 20% each. Their combined share in 2006 thus is 60% in terms of numbers and 69% in terms of DWT. Earlier, ABS represented the third largest class in terms of number of vessels, but GL's portfolio increased steadily since 2001, overtaking ABS in 2003.

When it comes to flag states, there are no universally accepted criteria to define quality. Based on analysis of European detention statistics, the Paris MOU annually issues updated blacklists of poor

Vessels by flag

Based on Paris MOU classification 2006



performers. This blacklist has growing importance regarding vessel inspection and banning practices in European waters. Based on the classifications in the latest edition of the list (effective 1 July 2006, updated 17 October 2006) the NoMIS portfolio has 2% of its vessels with blacklisted flags. This is a further substantial reduction in "black" exposure in the NoMIS portfolio compared to 11% last year. The improvement is mainly due to the fact that Panama improved its performance in 2005 and thus moved from the "black-medium" to the "grey" risk sector in 2006. Flags posing medium-to-high to high risk constitute 1.7% of the portfolio, compared to 2.1% the year before. Most of these vessels are registered with St. Vincent & Grenadines flag.

Long term claim costs

The table "Key Figures" includes annual and long-term claim costs per vessel, per sum insured and per DWT. These ratios can be applied to forecast future profitability. In general, the appropriateness of the various ratios depends on the type of vessels comprising the portfolio and the development of this composition. Neither the results nor conclusion regarding stability can be directly transferred to other portfolios. Changes in the long-term portfolio composition pose challenges when using these indices. The increase in average values would normally suggest a reduction in the claims per sum insured. The downward trend in this ratio supports this assertion up until 2003. The 2004 underwriting year deviates from this development, with the highest claims per sum insured in the ten-year period.

Claims per vessel showed remarkable stability over a long period of time. By using the claim per vessel approach to estimate partial losses and the claim per sum insured approach to estimate total losses, one can derive a simple combined model as illustrated in the following table. This model returns an estimate of expected loss ratio at the 2006 premium level.

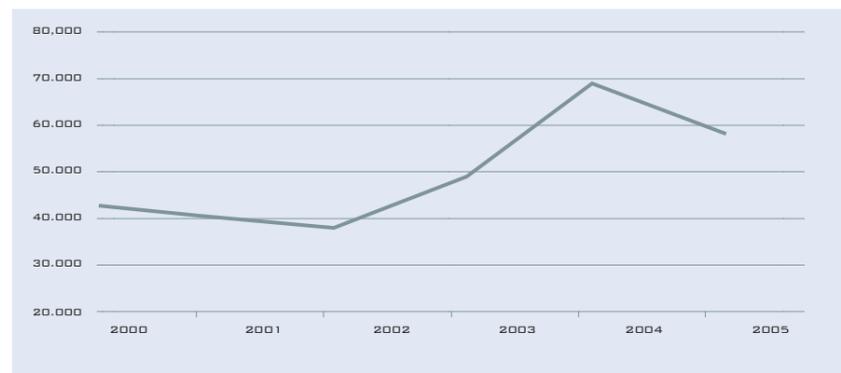
A new claims-climate

As the graph "Partial claim per vessel" indicates, there is a clear trend towards higher partial claims per vessel since 2002. To estimate future claims based on a 5-year-average for partial claims would thus be misleading and underestimate the risk. To take the trend into account, the 2-year-average of 2004 and 2005 is used in the following calculation:

Contribution	Calculation	Normalized Loss Ratio
Partial Losses	$\frac{04-05 \text{ PA claims per vessel}}{06 \text{ premium per vessel}}$	59' / 81' = 72%
+ Total Losses	$\frac{01-05 \text{ TLO claim rate}}{06 \text{ premium rate}}$	0.065%/0.28% = 23%
= Overall Loss	Partial + Total Losses	95%

Total losses on the other hand are more erratic over time without any clear trends, so here a longer period of time has to be taken into account.

Partial claim per vessel



The 2005 underwriting year is about in line with the above model. It is too early to reach any definite conclusions regarding the 2006 underwriting year, but results based on the actual claims figures for 2006, including IBNR estimates, indicate a loss ratio of 107%. As with all statistical expectations, deviations will occur when it comes to the actual incurred loss ratio for individual years. If the trend towards higher partial claims further increases, this will give even higher expected loss ratios.

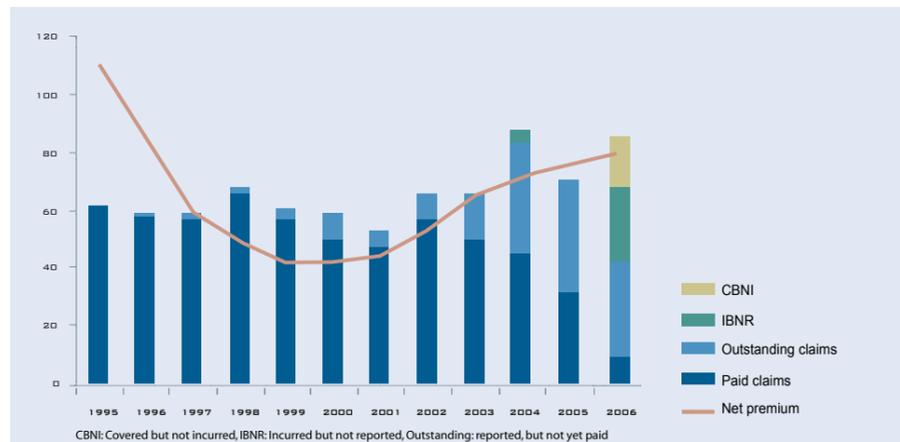
Premium rates

Development in premium rates can be monitored in a number of different ways. Earlier reports focused on changes in premium on renewed vessels with a stable sum insured. From 2003 to 2006, we experienced a systematic increase in the insured values within certain segments. The average CEFOR vessel increased its value with 10% in 2004, 13% in 2005 and 5% in 2006. Some segments and individual vessels show a significantly larger increase. The sample of renewed vessels with a stable sum insured is thus not representative, and the traditional way of calculating rate increases is not feasible.

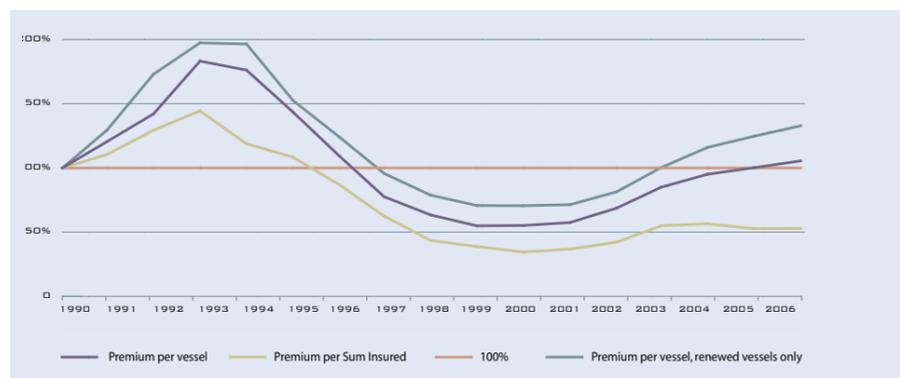
The main purpose of monitoring average premium rates is to derive consequences for expected profitability. Any feasible rate index should therefore not only consider the premium, but also consider any changes that can impact the claims cost. In terms of both age, vessel size and vessel types the composition of the portfolio is fairly stable going from 2005 to 2006. The average deductible was stable until 2005, but showed an increase in 2006.

An increase was however only seen in deductibles exceeding USD 500,000, whereas the average deductible below USD 500,000 was stable from 2005 to 2006. The fundamental change is the increased values. In addition, the market sees a number of "performance bonuses" likely to affect the final premium negatively. As a result, the 2006 premium rates are currently somewhat overestimated, even if the exact effect is difficult to assess. This issue set aside, the stability in terms of age, size, deductible and types of vessels from 2005 to 2006 suggests that simple indicators such as premium per vessel and premium per sum insured could be used to monitor the premium rate development. The indices show a rate stagnation in the premium per sum insured and an increase of 5% in the premium per vessel.

Premiums and claims per vessel per underwriting year in USD 1000



Premiums indices, 1990 = 100%



Loss ratio in a long-term perspective

The graph labelled "Loss ratio in a long-term perspective" illustrates that the NoMIS H&M portfolio reflected a technical loss continuously from 1997 to 2005. In the period 2001-2003, high-profile events had a significant impact on results reported by CEFOR. In these years, the largest claim accounted for 10-12% of the total and each year, the largest claims exceeded all earlier claims. The 2004 and 2005 underwriting years share none of the characteristics of the years before. The largest claims in 2004 and 2005 only account for 4% to 5% of the total. The 2006 underwriting year is still developing, but currently the largest claim accounts for 10% of the total registered claims.

Loss ratio in a long-term perspective



Key figures

The Fleet Insured with NoMIS members

Underwriting Year ¹⁾	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	Average	
													2000-2005	1995-2005
Number of vessels	5 545	6 117	7 220	7 222	6 677	6 120	6 919	7 165	8 125	9 450	9 868	10 804	8 305	7 312
DWT (millions)	262.0	281.9	318.3	316.0	319.5	304.9	336.7	346.5	385.9	438.6	467.4	496.0	395.0	343.5
Premiums														
Net Premium per vessel	110 005	85 951	62 033	50 422	43 315	44 409	45 235	53 026	66 021	73 468	77 740	81 179 ²⁾		
Net Premium per dwt	2.33	1.87	1.41	1.15	0.91	0.89	0.93	1.10	1.39	1.58	1.64	1.77 ²⁾		
Net Premium per sum insured	0.582	0.478	0.345	0.243	0.215	0.196	0.205	0.241	0.298	0.301	0.282	0.280 ²⁾		
Claims														
Number of claims	1 641	1 711	2 107	2 254	1 878	1 760	1 893	1 760	2 202	2 465	2 395		2 143	2 006
Claims frequency	0.30	0.28	0.29	0.31	0.28	0.29	0.27	0.25	0.27	0.26	0.24		0.26	0.27
Loss ratio (%)	54	77	91	124	137	125	117	121	95	111	92		105	99
Claim per vessel	59 850	65 988	56 200	62 739	59 180	55 592	53 030	64 240	62 937	81 378	71 659		67 780	63 964
Claim cost per dwt	1.27	1.43	1.27	1.43	1.24	1.12	1.09	1.33	1.32	1.75	1.51		1.43	1.36
Claim cost per sum insured (%)	0.317	0.367	0.313	0.302	0.293	0.245	0.240	0.292	0.284	0.334	0.260		0.283	0.292
Partial losses														
Number of partial losses	1 633	1 698	2 093	2 237	1 870	1 746	1 883	1 747	2 191	2 450	2 381		2 130	1 994
Partial losses frequency	0.29	0.28	0.29	0.31	0.28	0.29	0.27	0.24	0.27	0.26	0.24		0.26	0.27
Partial losses per vessel	44 436	50 037	40 563	53 911	51 927	41 804	41 092	39 408	47 212	67 209	59 616		52 344	49 870
Partial losses per dwt	0.94	1.09	0.92	1.23	1.09	0.84	0.84	0.81	0.99	1.45	1.26		1.10	1.06
Partial losses per SI (%)	0.235	0.278	0.226	0.260	0.257	0.184	0.186	0.179	0.213	0.275	0.216		0.219	0.228
Total losses ³⁾														
Number of total losses	8	13	14	17	8	14	10	13	11	15	14		13	12
Total losses frequency (%)	0.14	0.21	0.19	0.24	0.12	0.23	0.14	0.18	0.14	0.16	0.14		0.15	0.17
Total losses per sum insured (%)	0.082	0.089	0.087	0.043	0.036	0.061	0.054	0.113	0.071	0.058	0.044		0.065	0.064
Average vessel														
Size DWT	47 618	46 343	44 683	44 801	49 027	50 982	49 619	49 570	48 490	47 549	48 434	46 862	48 732	47 920
Age (years)	13.0	13.4	13.8	14.0	13.9	13.7	13.6	13.3	12.9	12.7	12.6	12.6	13.0	13.3
Value USDm	18.9	18.0	18.0	20.8	20.2	22.7	22.1	22.0	22.2	24.4	27.6	29.0	23.9	21.9
Standard Deductible USD	162 992	144 876	138 310	128 947	128 933	138 955	143 504	139 031	134 432	138 487	138 513	152 253	138 793	139 725

1) The figures in the table are 100% figures, per vessel underwritten by CEFOR companies. They do reflect the CEFOR portfolio as a whole but NOT the shares or results of the CEFOR members. The 2006 underwriting year is still at risk. Approximately 60% of the premium is earned as of 31.12.06.

2) Premium and claim figures per vessel, DWT and sum insured can be used to calculate "expected loss ratios" at the current premium level. As a simple example, an estimate based on claims and premium per sum insured is derived as follows: Average claim per SI / 2006 premium per SI = 0.283/0.280 = 101%

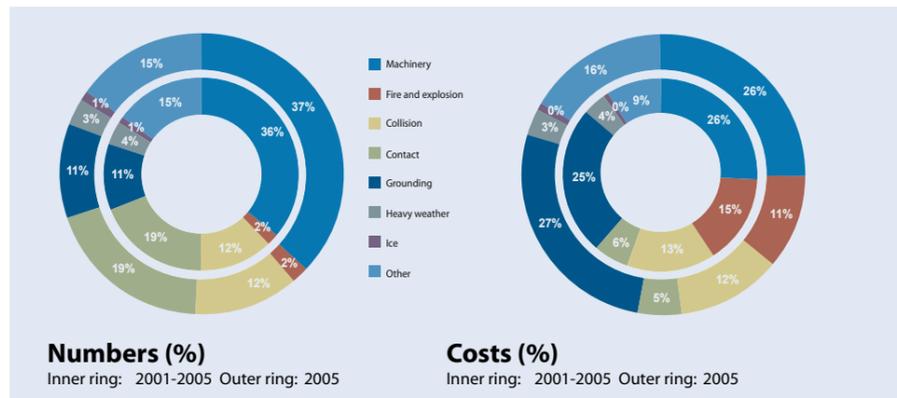
3) Total losses are defined as claims in excess of 75% of the sum insured of the vessel.



Claims by type of casualty

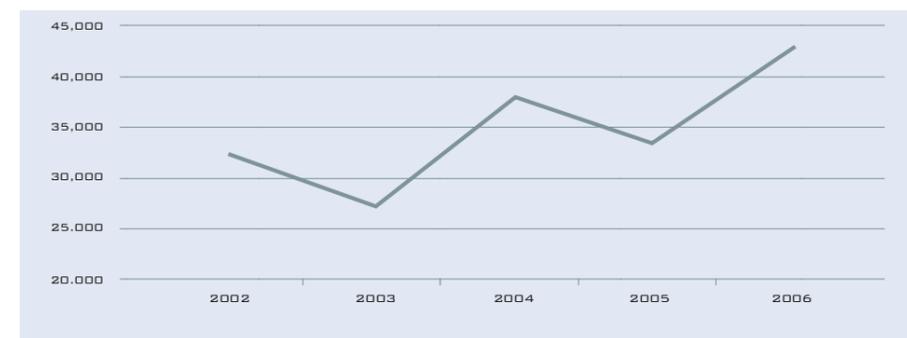
In terms of frequency, the 2005 underwriting year shows the same stable distribution between claim types. With 37% of the overall number, engine-related claims are still the single most frequent claim type. Nautical-related claims (grounding, collision, striking, ice) account for another 42% of the number of claims. In terms of claim cost, the split between types is more volatile. In general, fire, explosions and groundings represent few but costly claims. Engine-related claims, on the other hand, include many minor claims. In 2005 there is a further decrease in the cost of fire/explosions, and an increase in the cost of groundings. The increased cost of "other" claims is caused by one large claim.

Distribution of claims by type of casualty



This is significantly up compared to earlier years. Grounding is by far the single most significant cause followed by Fire and Explosion, but it is Collisions followed by Groundings that have caused the increase in both number and costs. It is also interesting to note that for the first time in NoMIS history we have an engine claim larger than USD 10 mill.

USD Claim per vessel as reported pr 4th quarter



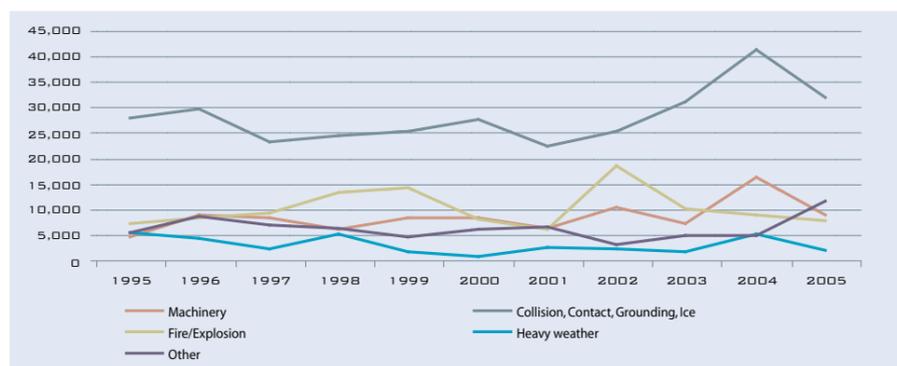
Higher claims costs can be caused by a number of reasons: Increased costs for steel, spare parts, salvage, and lack of availability of yards. A weaker USD and increasing vessel values are also risk factors that have an adverse impact on the claim cost.

on each vessel can have a large impact on the results, and thus (in theory) all contributing companies can have a better result than the average given in this report.

Large claims on the rise

NoMIS statistics show a significant increase in the average claim size (= total claim cost divided by number of claims). Average cost per incurred claim has gone from a relatively stable USD 200 000 to approximately USD 300 000 for 2004 and 2005. For 2006 the average is likely to change as the year develops, but the claim per vessel reported as of 31.12.06 is higher than the 12-month status of any previous year.

Claim type development - USD Claim per vessel

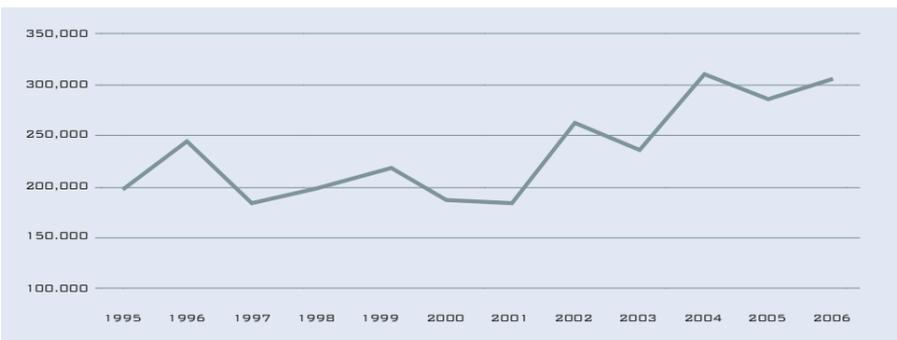


Nautical claims continue to be a major concern within the insurance industry. The probability of an incident becoming a major claim seems larger than before. The current extensive newbuilding programme, combined with low scrapping, results in lack of qualified crew and raises concerns with regard to future claims.

The figures are reported on an underwriting year ("risk attaching") basis. This implies that premium and claims are reported on the year the policy was written. The premium from a policy written at the end of 2006 is thus included in the 2006 figures, whereas the claims will be added when reported. Premiums are reported net of commissions to brokers.

Claims frequency shows a stable to slightly downward development for 2004 and 2005. We also saw a slightly lower than average claims costs due to total losses and claims larger than USD 30 million.

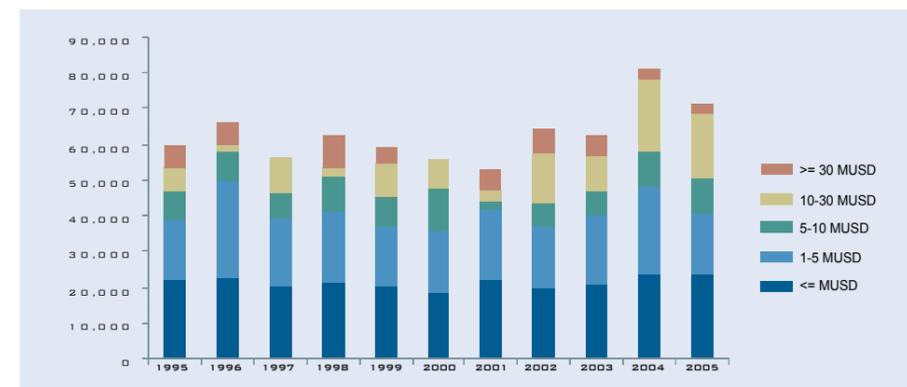
Average claim amount - USD



Data

To increase the reliability of the results, vessels without valid IMO-numbers are excluded. This excludes the risk of double counting of some vessels, the risk of including irrelevant accounting data and improves the quality of vessel specifications (age, tonnage etc.). In addition, data from the Swedish Club was included in 2006, which applies retrospectively to all underwriting years 1995-2005 and leads to an increase of 500-800 new vessels per underwriting year.

USD claim per vessel



In the tables and graphs seen here, all claim and premium information is based on 100% shares. This approach gives representative statistical key figures, but can be somewhat misleading regarding the technical results of the contributing companies. For the contributing companies, the written share



NoMIS and the CEFOR Statistics Forum

Norwegian Marine Insurance Statistics (NoMIS) as shown in this report comprise data from:

CEFOR members	Joined NoMIS in:	Data reported for Underwriting years:
Bluewater	2004	2002 - 2006
Codan	2005	2001 - 2006
Gard	Co-founder of NoMIS (as Storebrand, Vesta)	1985 - 2006
Gjensidige	Co-founder of NoMIS	1985 - 2001 (run-off)
NEMI	2004	2002 - 2006
Norwegian Hull Club	2003	1995 - 2006
Swedish Club	2006	1995 - 2006
Zurich Protector	Co-founder of NoMIS	1985 - spring 2002 (run-off)

Traditionally, the database only contained vessels written from Norway. The current database contains an increasing number of vessels written from other Nordic Countries.

Further statistics:

In addition to the statistics presented in this report, CEFOR publishes an annual statistics report at www.cefor.no ("The 2006 CEFOR NoMIS Report"). This report shows breakdowns of many of the above statistics by vessel type and age group.

CEFOR Statistics Forum 2006

- REIDUN HAAHJEM**, Gard, Chairman
- CHRISTIAN IRGENS**, Norwegian Hull Club
- MATS LINDAU**, Swedish Club
- ERIK LUND**, Bluewater
- FRODE LUND**, Codan
- BJØRN OLAV NORBYE**, NEMI
- ASTRID SELTMANN**, CEFOR Analyst



THE CHANGING PICTURE OF SHIPS AND VALUES

The Eidesvik Offshore order for a large offshore construction vessel of the type ULSTEIN SX121 is a good example of the changing picture of ships and values. Representing the latest in ship design and high technology equipment, the new vessel is an inspection-, maintenance-, repair- and construction vessel (IMR/OCV) with a length overall of 120.2 m, breadth of 25 m and a large cargo deck area of 1470 square meters. The environmentally friendly ship, especially fit

for rough weather conditions, features a new hull design (ULSTEIN X-BOW©) for increased comfort and safety, lower fuel consumption and increased speed.

The vessel has accommodations for up to 90 persons and is equipped with a moonpool, an active heave compensated offshore crane, ROV-hangar, diesel-electric machinery and a helicopter deck, among other innovations. The price tag? USD 106M.



The tremendous rise of ship values will continue to be a unique insurance challenge to the business of marine hull.



THE CHANGING PICTURE OF BUSINESS RISK

The economic pressure of adhering to tight schedules frequently results in the ship's command misjudging ocean or atmospheric conditions, putting vessels and cargoes at risk. February 2006 wasn't a good month for the container traffic trade. Losses in that month alone included 58 containers off the Dutch coast, 80 containers near Cape Finisterre, and 48 containers in the Bay of Biscay (30 containers damaged).

Even the largest and most modern container ships lose containers. And when the cargo comprises cigarettes, perfume, or electronic equipment, the

value of a single container can be in excess of USD two million.

Containers are a symbol of modern and efficient global trade, more than 95% of which is handled via sea routes. Today, it is not uncommon to see container ships with a capacity of more than 10,000 TEUs, or read about plans to build vessels capable of holding 15,000 TEUs.

Such mega-container ships represent accumulations that would have been inconceivable just a few years ago.



The changing picture of risk from a P&I perspective



Scandinavian P&I clubs have adapted to the changing picture of risk for over a century. In recent years, however, new risks from a broad range of different sources have emerged, resulting in a far more complex picture. Below we will describe the different risks and how we as an industry cope with them.

The International Group of P&I clubs, which includes the Scandinavian P&I clubs, insures over 95 % of all ocean going vessels. For this reason we are exposed to risk world-wide and to succeed, we must be willing to adapt to the various local aspects of managing risk.

The mutual P&I system is based on a collective approach to risk, meaning that all Group clubs share their risks within certain limits. The individual clubs have their own retention, which have increased from USD 5 million to USD 6 million in 2004 and will increase to USD 7 million by 20 February, 2007. Above the clubs' own retention, the Group collectively covers the risk up to USD 50 million. For risks over USD 50 million, the Group collectively purchases a reinsurance programme.

Increasing risks

During the last few years, many clubs have reported an increase in claims and in particular claims costs. This trend in increasing claims costs has now been confirmed by all clubs, and it is quite clear that the increase is quite dramatic. As an example, one Scandinavian club reports that over a period of the last 15 years, 99% of all claims are claims under USD 250,000 and that these claims stand for only 50% of all claims costs, meaning that 1% stands for the other half of the costs. The same club reports that the number of cases under USD 250,000 has decreased to 0.65 cases per vessel in 2004 from a peak of one case per vessel in 1998.

Unfortunately, this positive trend has turned, and once again, we are seeing an increase. If one looks

at average claims cost during the same period, the picture is quite different. In the year 2000, the average claims cost for this club was about USD 10,000 per case, which increased to a little under USD 16,000 per case in 2004. An increase of nearly 38 % in a four-year period clearly shows the shift, and risk increases, faced by the marine insurers.

Another indicator of the changing risk picture is the development of pool costs in recent years. As mentioned above, the pool is the cost of claims in the band between USD 7 million and USD 50 million that the International Group clubs share. Records indicate that in more than thirty years, 2004 was the most costly, with a combined total of over USD 350 million spread over about 16 cases. Unfortunately, 2006 may exceed this amount, with costs running as high as USD 450 million divided between more than 20 cases.

What is causing this sharp increase in claims costs, and how is the P&I industry coping with it? The complex picture makes it difficult to isolate one issue. In our view, the following factors contribute to the trend we now see:

- Social trend of increasing liabilities
- Implementation of new or adjustments of existing directives, conventions, laws and regulations
- Booming freight market
- Shifting technology
- Implementation of stricter liability, and
- The trend of curbing the right to limit.

Social trend of increasing liabilities

The world as a whole has adopted the "US approach" to viewing liabilities in recent years, causing a sharp increase in liability costs. Politicians are now taking a keen interest in casualties and in many instances, have abandoned established ways of handling liabilities. Instead, they push a "who is to blame culture", where the demand for higher rewards and harder penalties for ship-owners are key issues. The view that the polluter pays is now becoming more and more common.

Directives, conventions, laws and regulations

Revisions and implementation of new conventions, laws and regulations are also strong contributing factors to the increase in liability costs. Based on all the regulations that are in the pipeline, it is expected that these costs will be pushed even higher. It is important

to point out, however, that many of the existing conventions had not been adjusted for many years and are therefore not up to date with today's cost levels. But how many changes and increases should the industry be willing to accept?

Below you will find a summary of the recent changes to laws and regulations that have increased liability levels.

Legislative changes - oil pollution

- Delaware River Protection act (US). Introduced after the Athos 1 grounding, this Act is basically an inflation adjustment of the OPA 90 limit.
- TOPIA introduced, vastly increasing ship-owners' exposure.
- New regulations being implemented in the European Union:
 - Directive on Ship-Source Pollution and introduction of penalties
 - Introduction of a framework to strengthen criminal law against ship-source pollution
- Introduction of the Canadian Bill C-15
 - Introduction of strict liability, burden of proof now placed on the accused
 - Introduction of potential prison sentences and considerable fines

Hazardous and Noxious Substances

- This 1996 convention implies stricter liability for ship-owners
- Implementation of HNS fund for SDR 250 million beyond owners' limitation.
- Likely to be implemented in 2008/09

UNCITRAL Convention

- Draft Convention on the Carriage of Goods by Sea
- To replace Hague-Visby, Hamburg & US COGSA
- Implies loss of nautical fault defence

Athens Convention

- Compulsory insurance for ship passengers
- Revision of existing limit on death or personal injury
- New limit: SDR 250,000 per person, previous ca. SDR 47,000
- Negligence implies limit of SDR 400,000
- New limits are far beyond wishes of the P&I Clubs

Europe - Third Maritime Safety Package

(also known as Erika III Package)

Seven proposals are now under consideration by European Parliament - two concern the Clubs

1) Implementation of "Athens Plus"

- domestic traffic (not just international)
- inland waterways
- advance payments

2) Civil liability and financial security of ship-owners

- Implementation of LLMC 1996 throughout Europe
- Ships flying flags of states not party to LLMC 96 lose the right to limit where gross negligence
- Clubs required to provide certificates
- Guaranteeing liabilities
- Accepting direct action by third parties

Markets

Owners, operators and charterers work their ships harder in a booming freight market, which has caused an upsurge of navigation-related incidents such as groundings, collisions and strikings. Good freight markets mean generally higher cargo values, which serve to increase claim costs for loss of, damage to or delay in delivering cargo.

Technology

New technology has made it possible to construct vessels that can take as many as 14,000 containers and passenger vessels with a capacity of 6,000 passengers. The risk exposure for both these categories of vessels has increased dramatically due to the vast numbers involving individual risks. Due to the new limits set out in the Athens Convention, the clubs' structure will not be able to cover the whole risk involved with these mega-passenger vessels.

No right to limit

The right to limit liability is a well established practice within shipping. Many will go as far as claiming that this is one of the cornerstones of the carriage of goods by sea. We are now observing a clear trend among European politicians to limit this fundamental right and in some instances, challenging its whole existence. From a shipowner and insurance perspective, this trend is of great concern. Significant changes in this right can shift the balance in this industry and cause great difficulties in obtaining sufficient insurance cover.

Strict liability

Another trend we have observed is the implementation of strict liability in shipping incidents. In most jurisdictions, a well established legal safeguard is the institution that the accuser has the burden of proof. In many shipping related incidents, this burden of proof has shifted to the accused, thereby increasing the shipowners' liability. This trend is also a great concern for the industry going forward.

Conclusion

There is no doubt that the total risk picture for the shipowner is changing rapidly and that many of the changes represent significant challenges for marine insurers. Throughout its history, the P&I industry has demonstrated its ability to absorb and handle change, and we can expect marine insurers to continue to adapt to new market realities in future. However the shipping community will have to stand together to minimise the impact of these changes, which will have a significant influence on the cost of running their business.

FACT

THE CHANGING PICTURE OF CRIMINALIZATION

The maritime industry has witnessed a growing global trend toward criminal prosecution of seafarers involved in maritime accidents – many of which were not the result of human error. While politically popular, the criminalisation of seafarers is detrimental to recruiting and maintaining skilled personnel to man the world's merchant fleet – the backbone of the global economy. And

without quality seafarers, the risk of accidents related to human error will only increase.

The global trend toward the criminalization of seafarers for maritime accidents, especially those involved in pollution or loss of life, remain a major concern of shipowners, who are responsible for the fair treatment of their crews.



Tampa, 2001, Norwegian flag container/Ro-Ro-vessel. The vessel entered Australian waters 'illegally', with over 400 rescued refugees. The vessel was boarded and the master was threatened with criminal prosecution.

Safeguarding the engine of the global economy

Koji Sekimizu
Director, Maritime Safety Division, IMO.



While coping with emerging risks remains the responsibility of the shipping industry, it is in the interest of the global economy that these risks are managed responsibly.

Understanding the risks facing the maritime industry is not an issue confined to shipping companies, but the entire world. Indeed, the welfare of the global economy and the prosperity of human beings everywhere depend upon the provision of freely available, reliable and environmentally sustainable shipping services to every corner of the world. Therefore, anything that threatens the continuous flow of shipping services must be considered a fundamental risk.

Today's shipping industry is characterized by such important elements as the freedom of navigation, the recognition of sovereignty and jurisdiction over ships and territorial waters under UNCLOS, the free-trade system and the standardisation and harmonisation of rules at IMO, which have been designed to promote the safety and security of shipping and to protect the environment.

Emerging risks include the failure to maintain safe and environmentally sound shipping operations, based on the IMO's global standards, which could result in casualties and catastrophic accidents; unilateral actions to impose regional or national measures, or proliferation of regional control measures, which go beyond what is agreed at IMO; and acts of terrorism against shipping and the blocking of important sea lanes or straits. In addition, the failure to maintain a continuous provision of quality seafarers remains a major challenge to the shipping industry, now and in the future. We must make every effort to avoid all of these eventualities.

Looking ahead, the shipping industry must continue to play a role in the advancement of globalization and the need for sustainable development and more environmentally-friendly operations. The application of new technology is also a fundamental element which will affect the future operation of the shipping industry and will be a major determining factor in the way the industry will operate in the years to come.

Under the current free-trade system and with the growth of the world economy, it is expected that seaborne trade will continue to grow, so it is a challenge for everybody involved to maintain sound, safe, secure, efficient and environmentally-friendly shipping. In this context, the role of the shipping industry is of paramount importance and the industry itself has a primary responsibility to explore future possibilities within the concept of sustainable development.

Rather than being satisfied with pursuing business opportunities under the present regulations within a culture of compliance, the shipping industry should take more proactive, positive steps to lead the industry towards the future beyond compliance, under the principles of a safety and a more environmentally conscious culture. The shipping industry must invest in people and in technology in order to achieve sustainability to a level beyond that specified in the regulations.

As a leading global maritime authority, the IMO will continue to take a leadership role in these issues. Governments and industry will surely wish to maintain IMO's position as the global forum to discuss risk control options and to introduce necessary measures based on proper risk assessment, such as casualty investigation, the evaluation of new technologies and emerging social challenges. Co-operation among maritime authorities is vital, and maritime administrations should continuously act in collaboration, both in terms of information sharing and also burden sharing.

The mechanism of the IMO is crucial to ensure such collaboration among maritime administrations. The system for securing safety and environmental protection needs to be continuously reviewed with the aim to ensure quality improvements. In this context, IMO's current efforts to implement the Voluntary IMO Member State Audit Scheme should be strongly supported by maritime administrations.

“The welfare of the global economy and the prosperity of human beings everywhere depend upon the provision of freely available, reliable and environmentally sustainable shipping services to every corner of the world.”
Koji Sekimizu

The battle rages on

The CEFOR market

In 2006, gross premium income amounted to USD 120.3 million (NOK 772.5 million) compared to USD 102.7 million (NOK 661.9 million) in 2005. However, it should be noted that the 2006 figures include the Nordic hull account of TrygVesta and are thus not comparable with the 2005 figures.

Hull (and hull-related) covers amounted to USD 117.2 million (NOK 752.7 million). P&I amounted to USD 3.1 million (NOK 19.8 million). Premiums for coastal and fishing vessels are mostly paid in Nordic currencies.

The sector referred to as the "Coastal and Fishing Vessel" insurance market includes fishing vessels of all types and sizes, from small coastal fishing boats to large industrial trawlers operating worldwide. In addition, the market includes freighters, other coastal vessels and ferries serving Danish, Finnish and Swedish waters and the Norwegian coast and fjords, offshore supply vessels, tugs and lighters.

Insurance products

A majority of fishing vessels and small coastal vessels are covered according to the conditions of the Norwegian Marine Insurance Plan, especially Chapter 17 which has several covers designed for fishing vessels of all sizes. Danish, Finnish and Swedish conditions are also widely used. On the other hand, supply and offshore vessels, ferries and other special vessels enjoy full hull and machinery cover. The following covers are available for vessels categorized as coastal and fishing vessels:

- Hull and machinery insurance, including collision liability to third parties
- Loss of hire insurance
- Shipowner's insurance for third party liability (P&I),
- Liability for crews' wages and loss of personal effects
- Fishing insurance - covering catch, outfit, nets, gear, tools, instruments and dinghies
- War risk insurance.

Market conditions

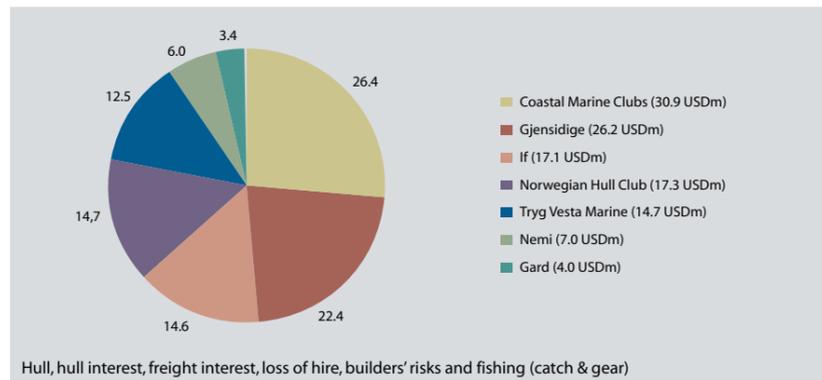
Strong competition in the coastal and fishing vessel market continues to hold premiums down in most segments, leaving margins insufficient to cope with large losses. This is especially evident in the supply and offshore vessel segment where insurance values are increasing steadily. Rating should be based on proper risk evaluation, not short-time considerations.

Competition in the Norwegian fishing vessel segment is fierce due to structural changes in the fishing fleet, including the liberalisation of the fishing licence scheme. The scheme allows for "merged" fishing licences shared among several boats, which has resulted in fewer but larger fishing vessels and a decreasing number of fishing vessels every year.

Competition continues to be fierce in the supply and offshore vessel segment, resulting in low premiums. This trend persists, despite the fact that there has been an increase in machinery damages which in some cases, has been the result of the machinery being driven too hard. There is a supply problem concerning large spare parts and yard capacity remains scarce.

Underwriters note that owners are having an increasingly difficult job recruiting quality crews. The problem is notable for owners of large fishing vessels in Norway, where the Norwegian net-salary scheme for offshore supply ships and ships in foreign trade results in skilled fishermen leaving the trade in favour of better paid jobs in the offshore supply sector.

Coastal and fishing %



THE CHANGING PICTURE OF GLOBAL WARMING

The Arctic sea ice has receded by about 40 percent since 1979. By the end of this century, some analysts believe some Arctic sea-lanes could be ice-free during the summer months. While representing disturbing trend global trend, the melting of the ice cap creates a broad range of complex issues for the shipping industry. For example, by taking advantage of these new sea-lanes, which cut transit distances by about 5,000 kilometres, shipowners can reduce costs, improve on delivery times – resulting in significant commercial benefits. On the other hand, the environmental impact on the fragile Arctic eco-system may be devastating. The issue is complicated by the global energy

picture. The high cost of oil, political instability in some oil producing regions, and a booming economy in China, have increased interest in developing energy resources in the region, which will result in more sea-going traffic – and more risk. The rising temperatures in the Arctic will impact everything from delicate eco-systems to global weather patterns. And with more vessels operating in the area, marine insurers will have to adapt, and adapt quickly to this new environment. More ships will bring more risk of accidents, and the nightmare of black oil spilled the pristine snow-fields of the Arctic.



Cargo under pressure

The premium income for the Norwegian cargo insurance market (excluding war risks) totalled USD 58.1 million (NOK 373.1 million) in 2006. Premium income in 2005 amounted to USD 63.1 million (NOK 406.7 million). Premiums for cargo insurance are mostly paid in Norwegian Kroner.

The 2006 figure is not comparable to previous years due to the fact that CEFOR member Industriforsikring no longer does business with the former Norsk Hydro company, Hydro Agri. In 2004, Hydro Agri was listed on the Oslo Stock Exchange as an independent company under the name Yara International ASA.

Vigorous competition in most market segments continued throughout 2006, both among CEFOR members and in international markets. The pressure on cargo premiums increased during 2006, when both new and established domestic companies, combined with international players, sought a larger share of a limited domestic market. In spite of fierce competition and sliding rates, Norwegian cargo business remains profitable.

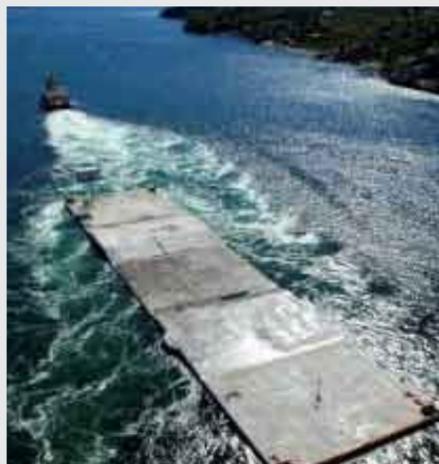
Throughout 2006, Norwegian underwriters have experienced a new kind of fraud. Evidence suggests that road haulers from the Baltic region offer cheap freight rates, receive the goods (mostly salmon), and then disappear with the cargo – never to be heard of again.

The largest claim in 2006 was due to containers lost overboard from a container feeder vessel during an October storm in the North Sea. The approximate claim is EUR 1,500,000.

The following issues will be monitored closely:

1. Road haulage of fish within Italy (robbery of whole trucks)
2. Chartered overage vessels causing disproportionate contributions from cargo owners in case of general average as well as total loss of vessels
3. The values of cargoes shipped seem to be constantly rising while the weight is decreasing, leaving Underwriters with little recourse.
4. Values accumulated on board container vessels.
5. The impact of climate change. (Cargoes in containers lost overboard, flooding, derailling of freight trains, etc.)

AN IF PROJECT: Bjørvika



The Bjørvika tow

A submersible tunnel will be constructed in Bjørvika, Oslo. Scheduled to be completed in 2010, the tunnel will manage motor traffic - estimated at 120,000 vehicles each day - that is now passing through central Oslo.

This complex construction project, which has been valued at 1 BNOK, has involved a lot of planning, development and production and requires a comprehensive insurance solution. If designed and offered a total package for the project and last spring, the company was chosen to insure the whole construction. Total value of the whole project is 4.6 BNOK.

The submersed part of the tunnel consists of 6 concrete-elements, with each section 110 metres long, 42 metres in width and 12 metres high and weighing 30,000 tons. These elementes represent

675 metres out of the total length of the tunnel, which will be 1100 metres in length.

The elements, each valued to NOK 80 mill., will be towed along the coast from the Hanøytangen Yard north of Bergen to Oslo and laid up in Oslo harbour until the construction of the tunnel begins in 2008. The contractor Skanska Norway AS will work in cooperation with two Dutch contractors as co-operating partners. The towage will be performed by Buksér & Berging AS. The estimated time for each tow is five days. The two first towages are already successfully completed. The remaining elements will be towed during summers 2007 and 2008.

The main elements in the insurance solution are Cargo and Marine Liability for the towage plus Construction All Risks (CAR) and Liability risk for the total project.



FACT

THE CHANGING PICTURE OF CARGO THEFT

While long an issue for the maritime industry, cargo theft has become increasingly organized, resulting in increased insurance premiums. And with more vessels now trading around the world, this trend has become a greater point of concern to shipowners and marine insurers alike.

Current market estimates place financial loss through cargo theft at between USD 50 -100 billion a year. Some 85% of all business security losses are attributed to the loss of product in

transit. And between 80% and 85% of cargo thefts involve inside information. The high profit potential of high-tech cargo thefts is attracting more sophisticated international criminals.

Cargo theft is a global problem, which lacks a coordinated response to become a global priority issue. And while accurate records on cargo theft are almost impossible to obtain, most analyst agree the problem will get worse before it gets better.



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A trusted resource in a changing industry

Established in 1911, CEFOR's primary function is to strengthen and develop the basic concepts of the Scandinavian marine insurance market and unite and coordinate its members around key issues for the marine insurance industry. Yet as the leading organization for marine insurance, CEFOR is also in a unique position to gather, organize and share valuable information not only to our members, but to other segments of the industry.

At present, the maritime industry is in a process of rapid change. Economic development has resulted in more and larger vessels trading in more parts of the world than ever before. At the same time, the development of new technologies and the introduction of new regulations have pushed the industry into uncharted waters. While many of these changes are positive, they have also led to the emergence of new risks which threaten to change how shipowners interact with marine insurance providers. This new market reality will have a long term impact on the marine insurance industry.

Perhaps now more than ever, CEFOR's expanding role as a provider of quality data and the organisations co-operation with other industry stakeholders, has become increasingly important not only to our members, but to the industry they serve. CEFOR will continue to leverage the knowledge, competence and experience of our organisation to remain a trusted resource in a rapidly changing industry.



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