REPUBLIC OF TURKEY

ANKARA UNIVERSITY

GRADUATE SCHOOL OF SOCIAL SCIENCES

DEPARTMENT OF MARITIME TRANSPORTATION LAW AND POLITICS

IMPACTS OF THE "PAY TO BE PAID" RULE ON P&I INSURANCE UNDER COMPULSORY INSURANCE AND DIRECT ACTION

LLM Program (conducted in English)
in the Sea & Maritime Law

KADİR DOLU

Ankara, 2023

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PROF. DR. XXX ADEMUNI-ODEKE

THESIS JURY MEMBERS

Name and Surname	**Signature**
1- Prof. Dr. Xxx Ademuni-Odeke	
2- Prof. Dr. İsmail Demir	
3- Prof. Dr. Nil Kula Değirmenci	

Thesis Defence Date
19 July 2023

REPUBLIC OF TURKEY
ANKARA UNIVERSITY
GRADUATE SCHOOL OF SOCIAL SCIENCES

I state that all the information in my master's thesis titled "IMPACTS OF THE "PAY TO BE PAID" RULE ON P&I INSURANCE UNDER COMPULSORY INSURANCE AND DIRECT ACTION" (2023, Ankara), which I prepared under the supervision of Prof. Dr. Xxx Ademuni-Odeke, was collected and presented in accordance with academic rules and ethical behaviour principles, I fully indicated the information I received from other sources in the text and in the bibliography, I declare that I have acted in accordance with the ethical rules, and I will accept any legal consequences in case the contrary arises.

Date: 21/07/2023

KADİR DOLU

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ABBREVIATIONS

BUNKERS 2001: International Convention on Civil Liability for Bunker Oil Pollution Damage, 2001

CLC 1992 : International Convention on Civil Liability for Oil Pollution Damage (CLC 1992 refers to the consolidated text of the International Convention on Civil Liability for Oil Pollution Damage, 1969)

CRTPA 1999 : Contracts (Rights of Third Parties) Act 1999

EU : European Union

ed. : Edition

FUND 1992 : International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage (FUND 1992 refers to the consolidated text of the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1971)

H&M : Hull & Machinery

HNS 1996 : International Convention on Liability and Compensation for Damage in Connection with the Carriage of Hazardous and Noxious Substances by Sea, 1996

HNS 2010 : International Convention on Liability and Compensation for Damage in Connection with the Carriage of Hazardous and Noxious Substances by Sea (HNS 2010 refers to the consolidated text of the Convention of 1996)

ICA 1989 : Insurance Contracts Act of 1989

ICC : Institute Cargo Clauses

IG P&I : International Group of Protection & Indemnity

IHC : International Hull Clauses

IMO/ILO/WGLCCS : Joint IMO/ILO Ad Hoc Expert Working Group on Liability and Compensation Regarding Claims for Death, Personal Injury and Abandonment of Seafarers

ILO : International Labour Organization

IMO : International Maritime Organization

Iss. : Issue

ITCH : Institute Time Clauses, Hulls

LLMC 1976 : Convention on Limitation of Liability for Maritime Claims, 1976

LLMC 1996 : Convention on Limitation of Liability for Maritime Claims (LLMC 1996 refers to the consolidated text of the convention)

MIA 1906 : Marine Insurance Act 1906

MLC 2006 : Maritime Labour Convention, 2006

MSA 1995 : Merchant Shipping Act 1995

NMIP : Norwegian Marine Insurance Plan

OPA 90 : Oil Pollution Act of 1990

p. : Page

PAL 2002 : Athens Convention relating to the Carriage of Passengers and their Luggage by Sea (PAL 2002 refers to the consolidated text of the Athens Convention relating to the Carriage of Passengers and their Luggage by Sea, 1974)

P&I : Protection & Indemnity

s. (sec.) : Section

SDR : Special Drawing Right

STOPIA : Small Tanker Oil Pollution Indemnification Agreement

TCC : Turkish Commercial Code

TOPIA : Tanker Oil Pollution Indemnification Agreement

TPA 1930 : Third Parties (Rights against Insurers) Act 1930

TPA 2010 : Third Parties (Rights against Insurers) Act 2010

UK : United Kingdom

UNCTAD : United Nations Conference on Trade and Development

US : United States

USA : United States of America

USD (US$): United States Dollar

Vol. : Volume

WRC 2007 : Nairobi International Convention on the Removal of Wrecks, 2007

I. INTRODUCTION

A) SUBJECT MATTER, AIM AND QUESTIONS

1- Role of Insurance

From the dawn of civilisation onwards, humanity has struggled against various human, transport, and commercial risks resulting in material damages or losses. Although the risks were not diverse at the start, they caused catastrophic consequences due to, *inter alia,* technological, statistical, and scientific lack of development. Thus, our ancestors endeavoured to eliminate or mitigate risks in many ways, among which the concept of insurance has been the most effective one so far.

Insurance, of which marine insurance is a considerable part throughout its history and currently, is a contract whereby the insurer is obligated to indemnify the insured against particular losses derived from certain risks. Not to mention the fact that there is no hurdle for individual merchants to bear any risk themselves. It is, however, to their detriment and also to the detriment of the public benefiting from their trade. Insurance, on the other hand, is more advantageous in many ways. First, it spreads out the economic burden of risks and distributes the losses in return for relatively fewer contributions by increasing the number of people bearing damages, *i.e.*, it is a transfer of risk of loss from individuals to a group of people. Second, it provides solidarity among, and certainty, predictability, and security for individuals. Third, merchants might, *inter alia,* receive credits for their businesses easier. Fourth, it provides the optimal utilisation of capital. Last of all, it lightens the burden of social insurance.[1] It protects individuals from a significant and uncertain financial loss, which they cannot otherwise afford, in return for specific and small consideration, *i.e.*, the "premium", or *ad rem*, "call" within the context of Protection & Indemnity insurance ("P&I insurance" or "P&I").

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[1] Vaughan, E. J. / Vaughan, T. M.: Fundamentals of Risk and Insurance, 10th ed., John Wiley & Sons, Inc., USA 2008, p. 34-35, 42; *Kayıhan*, Ş. / Günergök, Ö.: Türk Özel Sigorta Hukuku Dersleri, 5th ed., Umuttepe Yayınları, İstanbul 2020, p. 2-7, 15-18.

2- Role of Marine Insurance

Marine insurance, from which insurance was historically derived, is a contract whereby the insurer is obligated to indemnify the insured against losses stemming from specific risks incidental to marine adventure. It goes without saying that shipping has always been a marine adventure since maritime-based commerce and marine-based activities include numerous and considerably high risks. That being so, maritime-based commerce and marine-based activities are lucrative businesses, with approximately 80-90% of the world trade being conducted at seas, covering a vast area, that is, three-fourths of the earth's surface.[2] For that very reason, shipping seems to be indispensable in terms of world trade.

Moreover, maritime commerce and transportation have gradually evolved and become more complicated over recent years, particularly following the stimulation of steamships. Needless to say, no reasonable or prudent, *inter alios*, shipowner, cargo owner, charterer, ship operator, or terminal operator can bear such risks on their own by trading without insurance. Insurance, therefore, emerged and evolved mainly in maritime commerce and transportation in order to protect and foster such merchants, investing in a hazardous area, by relieving them of the financial burdens therein. Hence, it would not be wrong to suggest that marine insurance is deemed to be indispensable and prominent in overseas trade in the ordinary course of business. So much so that, it was tied up with shipping and banking, all of which were once one in the early history. However, the subject matter of this thesis is related to P&I insurance in particular, an aspect of marine insurance, to which the rest of this thesis will be devoted.

3- P&I Insurance and the Subject Matter and Aim

P&I insurance, as a type of marine insurance, is mainly provided by Protection & Indemnity Clubs ("P&I clubs" or "clubs") rather than the traditional insurance companies

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[2] Yorulmaz, M.: "Deniz Taşımacılığı ve Deniz Sigortaları", Master's Thesis, Marmara University, 2009, p. 7; United Nations Conference on Trade and Development ("UNCTAD"): "Review of maritime transport", ***https://unctad.org/topic/transport-and-trade-logistics/review-of-maritime-transport*** ***(accessed 17/05/2023)***; Organisation for Economic Co-Operation and Development: "Ocean shipping and shipbuilding", ***https://www.oecd.org/ocean/topics/ocean-shipping/#:~:text=The%20main%20transport%20mode%20for,are%20carried%20over%20the%20waves***. ***(accessed 17/05/2023)***.

and is, therefore, also commonly known as Club Insurance.[3] It provides a broad range of cover for the discharge of liability against the third-party claims as well as costs and expenses incurred by the insured, that is, the club member, usually the shipowner, in conjunction with the use or operation of his ship in return for non-fixed calls, in lieu of premiums, owing to mutuality. In other words, it primarily aims to cover the payments actually made by the member in practice, not the potential nor the exposed liability thereof on the ground that clubs do not want to become liability guarantors.

This is the corollary effect of the "pay to be paid" rule, which is peculiar to P&I insurance and underpinned by the notion of reimbursement, in accordance with which the insured club member shall make the necessary payments he is liable for in advance in order to entitle him the right to recover from the insurer, that is, the club. Only then, will the club indemnify its insured member. Traditional insurance companies, on the other hand, shall indemnify the insured as he is exposed to liability and claims for indemnification. The notable impact of this in the eyes of third-party claimants, who might sue the insurers by means of direct action, is that clubs can rely on the defence of "pay to be paid" in those actions, whereas traditional insurers cannot do so since there is no such policy defence in favour of them to be relied on. This rule, however, seems to satisfy everyone but third parties who suffer damage upon the act of the insured and might come up against a brick wall, so to speak, as to whether or not they will be compensated.

A person who suffers damage might, on the condition that there is an insurance cover, want to proceed primarily against the insurer, rather than the insured, which is expected to be financially stronger by its very nature, having regard to the fact that states enact binding and strict legislation for insurers, including clubs, to have and maintain a sustainable financial capability in terms of satisfying any claims. Thanks to the principle of mutuality, clubs are much stronger than any ordinary insurance company because they do not aim to profit, and thus, incomes and outcomes are usually equal. Over and above this, they act for the common interest of all where their members have mutual duties,

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[3] The terms P&I insurance and club insurance are interchangeably used throughout this thesis.

share the risks of each other, and have an interest as to whom should be accepted to the club for the sake thereof.

That being the case, it does not seem possible for third parties to proceed against clubs as a rule because of the principle of *inter partes*, that is, the privity of contract, indicating that a contract is legally binding and enforceable only between the parties thereto. Even if they could do so by means of direct action prescribed by law, clubs still would be able to invoke the defence of “pay to be paid” against them. More clearly, clubs might rely on this rule as a policy defence against third-party claimants, which could have relied on the member according to their contractual relationship, in direct actions wherein the third party “steps into the shoes” of, that is, subrogates to and becomes the successor of, the insured by means of law. In the end, however, third parties cannot be compensated by clubs because of this rule. Either way, they would have been forced to proceed against the member, and unfortunately, in a colloquial manner, they would have been at the mercy of the solvency of the member.

From the foregoing issues, it can be deduced that it is rare for a club to become insolvent, and therefore, bringing a direct action where clubs cannot rely on the defence of “pay to be paid” would definitely be in favour of third parties. For that very reason, this unique rule has been waived recently in the specific fields of marine insurance law in order to overcome this problem. From a *contrario* aspect, it is concluded that it is still retained in some other fields where the third-party claimants still have to proceed against the insured, the outcome of which depends on the solvency of the insured. Hence, the extent to which the third-party claims can be protected, by waiving this policy defence, to lay the groundwork for claimants to proceed against clubs, becomes an additional issue.

4- Questions Raised

The questions raised and answered throughout this thesis are as follows:

- What were the origins and what are the types of marine insurance? Which cover do these types provide basically? In this context, how is P&I defined, what is the legal framework thereof, and which claims does it provide and exclude basically?

- How, when, and where did P&I insurance emerge and evolve? What is the underlying rationale for such emergence and evolution, and what is the role of hull clubs and increasing liabilities of shipowners in that regard?

- What are the legal and organisational structure and status of P&I clubs as of today? How do they basically differ from traditional insurance companies?

- What is the role and function of the "pay to be paid" rule in the policy? How and why is it unique to P&I insurance, or more exactly, P&I clubs?

- What is the indemnity principle, and what is its relation with the doctrine of subrogation in general insurance law? What is the role of the "pay to be paid" rule in that regard? How do third-party claimants are affected by it?

- What are the ensuing problems of the application of the "pay to be paid" rule? Is it still strictly applied, or has the harshness of it been ameliorated from its origins and onwards?

- What is the principle of mutuality? Why is it significant on the part of third-party claimants in consideration of their right to choose to proceed against either the club or the member? What are the other distinctive features of P&I insurance?

- What are the roles and functions of compulsory insurance and direct action in maritime law? Will third parties be unprotected if the insured member is insolvent, or will those systems by themselves be adequate to solve the ensuing third-party problems arising out of the "pay to be paid"? If not, is there any solution to overcome the problem?

- Which international, supranational, and national regulations have been adopted or enacted so far governing compulsory insurance, direct action, and defence of "pay to be paid"? How and to what extent do these protect third-party claimants? Which claims fall within the scope of that protection, and which claims are excluded therefrom?

- Last of all, what is the perspective of clubs regarding compulsory insurance and direct action? Are they satisfied with their current position, or are they ready to be liability guarantors from today to tomorrow?

Eventually, this thesis is dedicated to seeking an ultimate answer as to whether the scope of compulsory insurance, together with direct action and the impacts of the “pay to be paid” rule on them in terms of unprotected, or even inadequately protected if any, third-party claims, should be broadened or not. If so, which ones and how?

B) SCOPE AND STRUCTURE

(1) In the first and introductive part of this thesis, the subject matter will be set forth in a deductive method by addressing the role of insurance, marine insurance, and P&I insurance consecutively. Subsequently, the aim of the thesis and the questions raised and answered thereunder will be determined. The first part will end upon setting out the scope and structure of the thesis, as well as approach and methodology used throughout.

(2) In the second part, an overview of marine insurance from ancient times to the medieval era and onwards plus the types of marine insurance will briefly be set out for the readers to perceive the location of P&I insurance in the grand scheme of insurance. In this sense, P&I will also be defined, claims covered within its scope and its legal framework will briefly be set forth.

(3) In the subsequent third part, the history of P&I insurance, its evolutionary stage from the late 17th century, will be set out by evaluating the ground on which the hull clubs (the predecessors of P&I clubs of today) emerged and declined, the scope of liabilities of shipowners simultaneously increased, the “protection” and “indemnity” classes amalgamated, reinsurance and the pooling system popped out in terms of P&I, and the clubs moved to offshore countries. Afterwards in this part, current status of P&I insurance, legal and organisational structure of clubs, and their differences from traditional insurance companies will briefly be set forth.

(4) In the fourth and pivotal part, the role and function of the “pay to be paid” will be analysed, under which its uniqueness, history, application, problems, and erosion will be discussed. Over and above this, the indemnity principle and the doctrine of subrogation as well as the effects of the “pay to be paid” rule in that regard will be analysed. Besides that, the way how third-party claimants are affected by it will be evaluated, and the problems of “pay to be paid” will be set forth. In addition, the role, function, and

significance of the principle of mutuality, having regard to the right of third-party claimants to choose to proceed against either the club or the member, will be analysed. Lastly, other distinctive features, that is, non-profit-making base and claims handling will briefly be evaluated.

(5) In the fifth part of this thesis, the roles and functions of compulsory insurance and direct action and the impacts of the "pay to be paid" rule on them will be analysed in accordance with international, supranational, and national laws. Finally, in this part, the perspective of clubs to that effect will be set forth.

(6) Last, but not least, in the sixth part, an evaluation will be set out as to whether the scope of the three-tiered protection – compulsory insurance, direct action, and the waiver of "pay to be paid" – in the field of maritime law should be broadened or not. If so, it will be determined for which claims and how it should be done.

C) APPROACH AND METHODOLOGY

This thesis mainly focuses on international and English law and practices in terms of legal framework. It focuses on English law and practice because P&I insurance originated in the 19th century and evolved in England, the most effective P&I clubs have located therein, and those clubs are still playing a pivotal and dominant role in the business. In other words, due to the historical influence of the English market, English law remarkably prevails today. It focuses on international practice due to the international characteristic of marine insurance, of which P&I is a part. Even though there is no uniform international convention specifically dealing with P&I or even marine insurance, there are relevant provisions of a few international conventions governing compulsory insurance and direct action in particular in this field. Over and above these, International Maritime Organization ("IMO") Guidelines, *European Union* ("EU") *Directive of 2009/20*, and the relevant provisions of some acts under prevailing national laws and the law of the author's country will be analysed.

The theoretical analysis will be supported by club rules that commonly refer to English law and jurisdiction. In this regard, the member clubs of International Group of Protection & Indemnity ("IG P&I" or "IG") will be preferred because they provide most of the P&I

cover, amounting to 90% of the oceangoing tonnage, in the world.[4] Besides, it is worth noting that rules of each club are nearly the same. In addition, judicial decisions will be referred to when the occasion arises because disputes are mainly resolved via the board of directors or arbitral proceedings prior to litigation.

The analysis throughout the thesis will be based mainly on the law of contracts and insurance law, and when the occasion arises, company law. It is noteworthy that this thesis will primarily focus on marine insurance, and as the occasion arises, insurance in general.

This thesis will also be based on a combined deductive, critical, and comparative method. Besides, examples and statistics will be given to support the research as the occasion arises. For the purpose of this thesis, the term "P&I insurance" will be used to indicate the cover provided by clubs because it is rarely provided by traditional companies. Also, the term "insured" will be preferred in lieu of the terms assured and policyholder.

II. AN OVERVIEW OF MARINE INSURANCE

A) BRIEF HISTORY

The origins of insurance, but not as we know it today, dates back to ancient times when the overseas trade was mostly carried out via shipping. Unlike today, seas were more dangerous with notably numerous and high risks, and the ships of then were rudimentary. Therefore, ancient communities sought solutions similar to insurance,[5] remarkable ones of which were the concepts of general average and bottomry.[6] Putting these aside, it was not until the 13th century that insurance contracts in the modern sense popped out.

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[4] IG P&I: "About the International Group", ***https://www.igpandi.org/about*** ***(accessed 02/03/2023)***.

[5] For China, *see* Vaughan / Vaughan, 74. For the Babylonian Empire, *see* Vance, W. R.: "The Early History of Insurance Law", ***Columbia Law Review***, 1908, Vol. 8, Iss. 1, p. 1, 5-6; Kayıhan / Günergök, 7; The Code of Hammurabi, sections 23 and 24. For general average and Rhodian and Roman laws, *see* UNCTAD: General Average: A Preliminary Review, Report by the UNCTAD Secretariat, TD/B/C.4/ISL/58, August 1991, p. 4 § 13-14, ***https://unctad.org/system/files/official-document/c4isl58_en.pdf*** ***(accessed 13/02/2023)***; Sözer, B.: Deniz Ticareti Hukuku, Vol. II, 1th ed., Vedat Kitapçılık, İstanbul 2016, p. 3, 49-52; Kayıhan / Günergök, 8. *See also* Kingston, C.: "Governance and Institutional Change in Marine Insurance, 1350 – 1850", ***European Review of Economic History***, 2013, p. 1, 2.

[6] Vance, 6; Holdsworth, W. S.: "The Early History of the Contract of Insurance", ***Columbia Law Review***, 1917, Vol. 17, Iss. 2, p. 85, 89; Yorulmaz, 82; Kayıhan / Günergök, 8-9.

Modern insurance, which was led by marine insurance, emerged to cover marine risks in Italy. The oldest policy in the modern sense, or *polizza* standing for an undertaking or promise at those times from which the term policy derived, was drafted on 23 October, 1347, to insure the ship, namely *The Santa Clara* and the cargo thereon.[7] Latterly, marine insurance spread from Italy by the Lombards, rich merchants emigrating therefrom to England, *circa* the 15th century.

In the 17th century of England, the most remarkable development in marine insurance was the laying the foundations for Lloyd's of London in 1688.[8] Demanding policies from various insurers was onerous then, so each individual used to underwrite the rate he would indemnify, and the paper was circulated from hand to hand until the risk was fully insured. For that very reason, they were called "the underwriters".[9] Another notable development in marine insurance was the enactment of the *Marine Insurance Act 1745* (19 Geo. 2 c. 37), under which insurance contracts without an insurable interest were forbidden in order to preclude the insureds from gaining profit.

That aside, the true cornerstone in respect of the law of marine insurance, which had progressed over centuries, was the enactment of a very well-known piece of legislation, namely the *Marine Insurance Act 1906* ("the MIA 1906"). It was a codification rather than a reform, *i.e.*, it encapsulated the existing case law theretofore.[10] Since then, it has had a widespread application, and it would not be wrong to say that England has been dominating the marine insurance market where its practice and law are still used or referred to on a global scale.

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[7] Vance, 7; Holdsworth, 88; Hayden, R. P. / Balick, S. E.: "Marine Insurance: Varieties, Combinations, and Coverages", ***Tulane Law Review***, 1991-1992, Vol. 66, Iss. 2 & 3, p. 311, 314; Yorulmaz, 83; Gürses, Ö.: Marine Insurance Law, 2nd ed., Routledge, Abingdon 2017, p. 74; Kayıhan / Günergök, 9.

[8] Lloyd's: "Pocket Guide", ***https://assets.lloyds.com/media/15f6b225-1095-4a16-8204-9c9bc2515f50/Lloyd's_pocket_guide_2022_digital.pdf*** ***(accessed 15/02/2023)***.

[9] Rose, F. D.: Marine Insurance: Law and Practice, Informa Law, London 2004, p. 1; Birds, J.: Birds' Modern Insurance Law, 7th ed., Sweet & Maxwell, London 2007, p. 2; Vaughan / Vaughan, 74-75; Yorulmaz, 84-85; Kayıhan / Günergök, 10.

[10] *Marine Insurance Act 1906* (c. 41), Introductory Text and section 91(2) ("MIA 1906"); Staring, G. S. / Waddell, G. L.: "Marine Insurance", ***Tulane Law Review***, 1999, Vol. 73, Iss. 5 & 6, p. 1619, 1622; Rose, 2; Gürses, 81.

B) TYPES OF MARINE INSURANCE OF WHICH P&I IS A PART

1- Marine Cargo Insurance

Marine cargo insurance is basically a contract of property insurance whereby the insurer indemnifies the cargo interests, *e.g.*, a consignee or shipper, having an insurable interest with respect to the loss of or damage to the cargo on board the ship. It provides cover for an extensive range of risks, even those not specified under the policy,[11] whereas P&I covers the specified risks. Nevertheless, P&I too provides cover for a vast range of risks.

In this branch of marine insurance, the outdated Ships and Goods Form was once used as the main policy form. It was superseded by the up-to-date and contemporary Lloyd's Marine Policy introduced in 1982, in addition to which Institute of London Underwriters drew up standard clauses recently revised in 2009 for cargo insurance.[12] Nowadays, these clauses are called Institute Cargo Clauses ("ICC") A, B, and C, *i.e.*, ICC All Risks, ICC with Particular Average, ICC Free of Particular Average, respectively. The cover can even be expanded to war and strike risks by Institute War Clauses (Cargo) and Institute Strikes Clauses (Cargo) because ICC A, B, and C do not cover these types of risks.[13]

2- Hull and Machinery Insurance (H&M)

H&M insurance is also a contract of property insurance whereby the insurer indemnifies, *inter alios*, the shipowner or ship operator in case of a loss of or damage to the ship itself and the machinery thereof, that is, the integral parts and accessories of the ship, *e.g.*, the machinery related to the propulsion of the ship, navigational equipment, or lifeboats.[14]

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[11] Lemon, R. T. II.: "Allocation of Marine Risks: An Overview of the Marine Insurance Package", ***Tulane Law Review***, 2007, Vol. 81, Iss. 5 & 6, p. 1467, 1478.

[12] UNCTAD: Legal Documentary Aspects of the Marine Insurance Contract, Report by the UNCTAD Secretariat, TD/B/C.4/ISL/27/Rev.1, 1982, p. 35-36 § 191(4), ***https://unctad.org/system/files/official-document/tdbc4ISL27Rev.1_en.pdf*** ***(accessed 17/02/2023)*** (hereinafter "Legal Documentary Aspects of the Marine Insurance Contract"); Rose, 103-104; Dunt, J.: Marine Cargo Insurance, 2nd ed., Informa Law from Routledge, Abingdon 2016, p. 3-7; Gürses, 79, 81.

[13] ICC (A) 09, clauses 6 and 7; ICC (B) 09, clauses 6 and 7; ICC (C) 09, clauses 6 and 7.

[14] Hayden / Balick, 315; Lemon, 1468; Lin, M. T.: "A Selective Appraisal of the P&I Insurance System with Special Reference to Claims for Personal Injury, Illness and Loss of Life", MSc Thesis, World Maritime University, 2009, p. 8.

Following the introduction of Lloyd’s Marine Policy and ICC, Institute Time Clauses, Hulls (“ITCH”) was drafted in 1983, revised in 1995, and International Hull Clauses (“IHC”) was drafted in 2002, revised in 2003.[15] The cover can even be expanded by the Institute War and Strikes Clauses, Hulls–Time 1/11/95 to war and strikes risks.[16] Furthermore, there are also institute clauses for yachts, fishing vessels, and port risks.[17]

The cover might, in case of a collision and unless another fraction is stipulated,[18] be expanded up to 3/4ths of the sums paid to the other ship if and in which the policy includes the “running down clause”.[19] It has crucial importance for determining the scope and percentage of P&I in terms of collision liability. It would not be wrong to say that the correlation of H&M with P&I is not overlapping but supplementary, or more clearly, P&I fills the gaps, so to speak. Other clauses in hull policies are beyond the scope of this thesis.

3- Protection and Indemnity Insurance (P&I)

a) P&I Defined

P&I insurance might be deemed to be the liability insurance of shipowners *stricto sensu*. Such definition, however, is not completely accurate, nor is it enough regarding the scope of P&I. As if that were not enough, P&I insurance was not defined under the MIA 1906.

First and above all, technically speaking, P&I is not traditional liability insurance despite the fact that indemnity provides indirect liability coverage in the end. The insurer (club) indemnifies the discharge of the liability of the member against third-party claims in connection with the use or operation of the ship. Moreover, it is not only limited to the liability of shipowners *per se*, but it also consists of the costs and expenses they incur.

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[15] Hudson, N. G. / Madge, T. / Sturges, K.: Marine Insurance Clauses, 5th ed., Informa Law from Routledge, Abingdon 2012, p. 85-90; Gürses, 81.

[16] ITCH 1/10/83, clauses 23 and 24; ITCH 1/11/95, clauses 24 and 25; IHC 1/11/02, clauses 29 and 30; IHC 1/11/03, clause 29.

[17] *See* to that effect, Institute Yacht Clauses, 1/11/85; Institute Fishing Clauses, 20/7/87; Institute Time Clauses Hulls – Port Risks, 20/7/87.

[18] Liability cover provided by H&M insurance for collision might be expanded to 4/4ths of the sums paid to the other ship. *See* to that effect, IHC 02, clause 40; IHC 03, clause 38.

[19] ITCH 83, clause 8; ITCH 95, clause 8; IHC 02, clause 6 IHC 03, clause 6; Hayden / Balick, 316-318; Lemon, 1473-1474; Lin, 8. For the historical background of the clause, *see infra,* Part III.A.2.

These liabilities, costs, and expenses have widely increased even in themselves over the recent years, during which P&I has empirically evolved piece by piece, and now, it has a very wide range of cover. Furthermore, although P&I insurance is basically provided for shipowners, it might be expanded in which the variety of others might, but limitedly, participate, so far as they have an insurable interest on their parts.

In light of these issues, accurately defining P&I is not easy because of its piecemeal and empirical evolution, and numerous risks included and the variety of persons involved therein. Nonetheless, it can be defined by setting out the following criteria that (*nota bene*, the last of which corresponds to the pivotal point of this thesis analysed hereunder):

(i) there shall be a shipowner or others[20] conducting business in, or related to, shipping;
(ii) these persons shall be exposed to liability or shall incur costs or expenses;
(iii) liability, costs, or expenses shall be arisen out of the use or operation of the ship;[21]
(iv) such ship shall be entered into a club; and
(v) the liability shall be established and discharged in order to be reimbursed.

b) Claims Covered

(1) Clubs cover collision claims which are, technically and within the meaning of marine insurance law, derived from the crash of at least two ships. Collision liability was not included in hull policies earlier, to which the insurance practice responded by inserting a "running down clause" in order to cover such liability up to 3/4ths of the sums paid to the other ship. It is still used, *mutatis mutandis*, at the present time to basically cover the

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[20] It must be noted that if a person is a shipowner and has any other status other than shipowner, the club will solely provide cover in respect of his status as a shipowner. For detail, *see* Hazelwood, S. J. / Semark, D.: P&I Clubs: Law and Practice, 4th ed., Informa, London 2010, p. 218.

[21] *Merchant Shipping Act 1995* (c. 21), s. 313 ("MSA 1995"). Crafts constantly used for non-navigational purposes such as oil rigs, docks, dredgers are not considered to be ships. *See* to that effect, Britannia P&I, Protection & Indemnity Rule Book, Class 3, 23/24, Rule 2 ("Britannia"); The Shipowners' Club, Club Rules 2023, Rule 67 ("Shipowners"); North of England, P&I Rules 2023-24, Rule 2(1) ("North"); The London P&I Club, The Protecting and Indemnity Rules, Class 5, 2023/2024, Rule 1(1) ("London"); UK P&I, Rules 2023, Rule 44 ("UK"); West of England, Rules of Classes 1 & 2, 2023, Rule 58 ("West" for the Class 1); Standard Club, P&I Rules, Rule Book, 2023/24, Rule 26 ("Standard"); Steamship Mutual, Rules 2023/24, Rule 2 ("Steamship"); Skuld, 2023 P&I Rules, Appendix 1 definitions ("Skuld"); The American Club, By-Laws & Rules, 2023/2024, Rule 1, section 2 ("American").

collision liability against the other ship.[22] Nonetheless, the liability of hull insurers cannot exceed the insured value of the ship in any case.[23] In response to this, P&I has been filling the gaps of H&M insurance for over a century, that is, the remaining 1/4ths of collision liability and the excess liability over the insured value.[24] Besides, their liability depends on to whom, that is, to which insured party in a collision, the fault is attributed. So much so that, the rights of subrogation of those insurers will accordingly be determined.

(2) Apart from collision, clubs also cover the claims arising out of other types of crashes, which are not collisions in the strict sense, and thus, not covered under the umbrella of hull policies' aforementioned clause. In this regard, non-contact damages (damages to vessels without collision) as well as damage to fixed or floating objects, *e.g.*, harbours, wharves, piers, underwater pipelines and cables, and docks, or *e.g.*, buoys are covered.[25]

(3) Clubs cover the claims regarding death and illness of, and personal injury to, seafarers, passengers, and others. Given the fact that these claims are related to fundamental rights, it would not be wrong to say that clubs have been covering them without applying their unique "pay to be paid" rule even before the adoption of the related conventions. So much so that, passenger claims arising out of cases that occurred outside the ship or in the course of air transportation, included in package tours together with a sea voyage, are covered only if such claims are related to death, injury, or illness.[26] Those aside, clubs cover the losses of and damages to the properties of seafarers and the luggage of passengers.[27]

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[22] ITCH 83, clause 8; ITCH 95, clause 8; IHC 02, clause 6; IHC 03, clause 6.

[23] ITCH 83, clause 8.2.2; ITCH 95, clause 8.2.2; IHC 02, clause 6.2.2; IHC 03, clause 6.2.2.

[24] Coghlin, T. G.: "Protection & Indemnity Insurance: The P & I Clubs", ***Journal of World Trade Law***, 1971, Vol. 5, Iss. 6, p. 591, 592; Acar, S.: "Çatmadan Doğan Sorumluluğa Verilen Sigorta Teminatı", ***İstanbul Barosu Dergisi***, 2006, p. 639, 640-641, 647-648; Hazelwood / Semark, 127; Algantürk Light, D.: Denizde Çatma Hukuku, On İki Levha Yayıncılık, İstanbul 2011, p. 85. For instance, *see* Britannia, Rule 19(9) (A, B); Shipowners, Rule 2, section 7(A, C); North, Rule 19(10); London, Rule 9.13; UK, Rule 2, section 10; West, Rule 2, section 9; Skuld, Rule 12; Gard, Rules 2023, Rule 36 ("Gard"); Japan P&I Club, Rules 2023, Rule 23 ("Japan"). *Nota bene*, provided that the ship is underinsured pursuant to the hull policy, the liability of clubs will increase accordingly. Clubs, therefore, reserve their right to determine the proper value of the ship, that is, the market value at the time of the collision, in accordance with which the excess liability will be determined in that case.

[25] Coghlin, 607; Lemon, 1483; Hazelwood / Semark, 139-140; Algantürk Light, 95.

[26] Acar, S.: "Kulüp Sigortası (P&I)", DPhil Thesis, İstanbul University, 2007, p. 122-125 (hereinafter "Kulüp Sigortası (P&I)"); Hazelwood / Semark, 165, 167-168.

[27] Acar, Kulüp Sigortası (P&I), 113-115, 117; Hazelwood / Semark, 165-167. For instance, *see* Britannia, Rule 19(1)(C) and Rule 19(2)(B). *Nota bene,* cash or precious and valuable objects are excluded.

(4) Not to mention the fact that members pay a sum to seafarers who will be repatriated or substituted. Clubs also cover the claims regarding such cases, in so far as those derive from serious situations, *e.g.*, death, injury, or illness. P&I insurance does not, however, cover the expenses of ordinary repatriation such as the expiration of the labour contract.[28] In addition, when there is a wreck or loss of the ship, and seafarers become unemployed, an equitable salary or unemployment compensation, which is paid to them, is covered.[29]

(5) Clubs cover losses and damages due to pollution, which is the contamination of oil or other similar hazardous substances leaking from the ship and spilling out the environment, and they cover costs thereby incurred for prevention or mitigation. H&M insurance covers pollution damages or their threat in case of a collision, but it is limited to the other ship or property thereon, whereas the cover under P&I for pollution is wider.[30] Besides, state authorities might give orders or directions, which could lead to the ship suffering loss or damage, to prevent or mitigate the pollution or its threat. This is also covered under hull policies, so far as the orders or directions are not the results of the lack of due diligence of the member, wherefrom the functional area of P&I starts.[31] Besides, clubs do not cover the escape of substances, even if previously carried on board, from land-based facilities.[32]

(6) As to salvage, which is an operation to assist a ship and any other property in danger, the principle of "no cure, no pay" is the fundamental basis of the operations under the *Salvage Convention, 1910*, and it is preserved under the *Salvage Convention, 1989*, whereby the salvors are remunerated or rewarded if their operations end up with a useful result.[33] However, the principle has started to be questioned since *The Amoco Cadiz* incident in 1978.[34] Hence, the harsh rule of "no cure, no pay" was gradually ameliorated

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[28] Acar, Kulüp Sigortası (P&I), 116; Hazelwood / Semark, 166. *E.g.*, *see* Britannia, Rule 19(1) (D, G).

[29] Acar, Kulüp Sigortası (P&I), 117; Hazelwood / Semark, 166. *E.g.*, *see* Britannia, Rule 19(1)(B).

[30] ITCH 83, clause 8.4.5; ITCH 95, clause 8.4.5; IHC 02, clause 6.4.5; IHC 03, clause 6.4.5.

[31] ITCH 83, clause 7; ITCH 95, clause 7; IHC 02, clause 5; IHC 03, clause 5; Hazelwood / Semark, 183. *See also* Britannia, Rule 19(12)(D); Shipowners, Rule 2, section 9(E); North, Rule 19(13)(d); London, Rule 9.15.1.3; UK, Rule 2, section 12(E); West, Rule 2, section 11(E); Standard, Rule 3.8.4; Steamship, Rule 25(vi)(d); Skuld, Rule 14.1.3.

[32] For instance, *see* Britannia, Rule 19(12)(iv).

[33] *Convention for the Unification of Certain Rules of Law with Respect to Assistance and Salvage at Sea*, Brussels, 23.09.1910, article 2 ("Salvage Convention, 1910"); *International Convention on Salvage*, London, 28.04.1989, 1953 UNTS 165, articles 12(1) and 12(2) ("Salvage Convention, 1989").

[34] Salvors did not carry out salvage operations considering the risk of non-payment in the absence of a useful result. It revealed that the non-payment to salvors minimising or preventing environmental

by, *inter alia*, introducing the concept of "special compensation" in 1989, which is a payment granted to salvors minimising or preventing environmental damage despite their failure.[35] As to the role of P&I insurance in this context, special compensation paid to salvors is covered by clubs, whereas the salvage reward itself is not.[36] As to the saving of human life, it has long been considered moral and humanitarian, and therefore, it has been accepted that no remuneration should be paid to salvors – save that they participate in the rescue of others, who salve the ship or property or minimise or prevent environmental damage and earn a salvage reward, from which the saviours of life are also granted a fair share.[37] In this regard, such share as a part of the salvage reward is under the cover of H&M. If there is only saving of life, P&I will step in to pick up the slack, so to speak.[38]

(7) Clubs cover the liability, costs, and expenses arising out of the loss or damage suffered by cargo interests. As to the property other than cargo, the loss thereof or damage thereto is also covered unless it is covered under another insurance or head of cover of P&I.[39]

(8) Clubs cover the towage claims if they approve the terms and conditions of the towage contract. The cover consists of either customary towage, denoting the entry or departure of the ship or the manoeuvres thereof in ports, or non-customary (ocean) towage in case the club particularly accepts it and, if required, an additional premium or call is paid.[40]

(9) Clubs cover the costs incurred by the member for locating, marking, and removing of wrecks when these activities are legally compulsory. The liability arising out of an

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damages but not being able to salve the ship or the property thereon was unequitable. For detail, *see* Bozkurt Bozabalı, B.: "Kurtarma Faaliyetinde Deniz Kirlenmesini Engelleyen Kurtaranın Ücret Hakkı", ***Süleyman Demirel Üniversitesi Hukuk Fakültesi Dergisi***, 2011, Vol.1, Iss.1, p. 169, 170-174.

[35] Salvage Convention, 1989, article 14. *See also* Hazelwood / Semark, 184-186; Demir, İ.: "Özel Tazminat Koruma ve Tazmin Klozu (SCOPIC)", ***Banka ve Ticaret Hukuku Dergisi***, 2011, Vol. 27, Iss. 4, p. 89, 91-96; Bozkurt Bozabalı, 180-181; Lloyd's Standard Form of Salvage Agreement 2020.

[36] For the exclusion of special compensation from H&M insurance, *see* ITCH 95, clause 10.5; IHC 02, clause 8.5; IHC 03, clause 8.5. For the inclusion of salvage charges in H&M, *see* ITCH 83, clause 11.1; ITCH 95, clause 10.1; IHC 02, clause 8.1, and IHC 03, clause 8.1. *See also* Acar, S.: "Çatmadan Doğan Sorumluluğa Verilen Sigorta Teminatı", ***İstanbul Barosu Dergisi***, 2006, p. 639, 644; Britannia, Rule 19(12)(E); North, Rule 19(13)(e); West, Rule 2, section 20; Skuld, Rule 22; Gard, Rule 42.

[37] Salvage Convention, 1910, article 9; Salvage Convention, 1989, article 16.

[38] Britannia, Rule 19(8); Shipowners, Rule 2, section 6; North, Rule 19(7); London, Rule 9.10; UK, Rule 2, section 9; West, Rule 2, section 7; Skuld, Rule 22, Gard, Rule 33.

[39] Acar, Kulüp Sigortası (P&I), 161-176; Hazelwood / Semark, 140-164.

[40] Acar, Kulüp Sigortası (P&I), 157-160; Hazelwood / Semark, 190-191.

inadvertent relocating of the wreck or escape of substances therefrom, due to the failure of the member trying to carry out the above-mentioned activities, is also covered.[41]

(10) In terms of general average, according to adjustment reports, damages suffered and expenses incurred are apportioned. Pro-rata shares of the ship and cargo are recoverable under hull and cargo policies, respectively. However, in case of a breach of the contract of carriage by the member or any justifiable reason exposing the member to liability, cargo interests might abstain from contributing to loss or damage. Besides, adjusters may have assessed the value of the ship in excess of its insurance value, to the extent for which the H&M insurers are liable in any case. P&I steps in and fills these unrecoverable gaps.[42]

(11) Clubs cover fines and impositions on the member such as customs fines, migrant fines, pollution fines, fines related to false documentation or short delivery of cargo, or fines related to the non-observance of the safety regulations.[43]

(12) Seafarers, who stay together without frequently going ashore during voyages, might come up against the outbreak of contagious diseases that they might easily carry and transmit. Precautions shall be taken to ensure public health. Members, therefore, incur additional expenses related to quarantine and the disinfection of the ship, and the expenses incurred during then, *e.g.*, loss of fuel, provisions and salaries of crew, port charges since the ship is segregated from the port. These quarantine expenses are covered as well.[44]

(13) Diversion expenses, *inter alia*, the loss of fuel, provisions and salaries of seafarers, or port charges, are also covered on the condition that the ship deviates from her route with the aim of carrying an ill or injured person, or landing refugees or stowaways.[45]

(14) Naturally, the scope of cover varies according to each claim and member. Omnibus cover, which is peculiar to P&I insurance, stands for the discretionary reimbursement by the club where the claim is not under club cover. In other words, it is an *ex gratia* payment

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[41] Hazelwood / Semark, 178. *E.g.*, *see* Britannia, Rule 19(13).
[42] Acar, Kulüp Sigortası (P&I), 178-181; Hazelwood / Semark, 176-177. *E.g.*, *see* Britannia, Rule 19(18).
[43] Acar, Kulüp Sigortası (P&I), 232-240; Hazelwood / Semark, 169-175. *E.g.*, *see* Britannia, Rule 19(19).
[44] Acar, Kulüp Sigortası (P&I), 240-242; Hazelwood / Semark, 175. *E.g.*, *see* Britannia, Rule 19(16).
[45] Hazelwood / Semark, 176. *E.g.*, *see* Britannia, Rule 19(6).

based on the sole discretion of the club, and in parallel therewith, the member has no right to claim its enforcement. On the plus side, it enables the cover to be dynamic and flexible to satisfy the changing needs. Besides, clubs cover the expenses reasonably incurred when the member is carrying out an instruction given by the club due to its absolute discretion.[46]

(15) Paying less to claimants is both in favour of the member and club, and thus, members are obliged to take necessary and reasonable steps to mitigate or avert the expenses upon the incident. These expenses as well as the "costs of defence" in the actions brought against the member are covered under the head of sue and labour cover.[47] Apart from all of those claims explained in this section, there are also general exceptions to P&I cover.[48]

c) Legal Framework

i. Statutory Framework

In spite of its highly international character and efforts by the United Nations Conference on Trade and Development ("UNCTAD") towards the end of the 20th century, marine insurance is still one of the few which has not been regulated in the form of a convention so far. Its uniformity has been ensured *de facto* by means of English law and practice, in conformity with which standard clauses and forms have been drafted, because it took its roots in England.[49] It also applies, *mutatis mutandis*, to P&I insurance, the practice of which is mainly based on standard and similar club rules.

Putting aside the fact that it is not statutorily and directly regulated under national laws, it might be subject to certain statutes thereunder. First and foremost, the MIA 1906 shall

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[46] Coghlin, 605; Ronneberg, N. J.: "An Introduction to the Protection &(and) Indemnity Clubs and the Marine Insurance They Provide", ***University of San Francisco Maritime Law Journal***, 1990, Vol. 3, Iss. 1, p. 1, 11-12; Acar, Kulüp Sigortası (P&I), 242-243; Hazelwood / Semark, 191-193.

[47] MIA 1906, section 78; Hodges, S.: Law of Marine Insurance, Cavendish Publishing, London 1996, p. 319-320; Acar, Kulüp Sigortası (P&I), 242, 273-274; Hazelwood / Semark, 319-327. *Nota bene*, Freight, Demurrage & Defence cover, on the contrary, indemnifies the costs and expenses incurred by the member, that is to say, the costs of attack, in the actions brought by the member. It does not cover the freight nor the demurrage fees not earned, though. For detail, *see* Hazelwood / Semark, 381-385.

[48] Wilful misconduct of the member, sailing of the ship in an unseaworthy condition with the insured's privity, loss of or damage to member's property, claims recoverable elsewhere, claims arising out of dredging, drilling, or other activities conducted in offshore operations, claims deriving from unlawful, hazardous, or improper adventure and trade like nuclear or bio-chemical risks, and war and strike risks.

[49] UNCTAD, Legal Documentary Aspects of the Marine Insurance Contract, 38-41; Lin, 39-40.

apply to P&I pursuant to section 85(4), except for its provisions related to premium (s.85(2)), and unless modifications are made to the contrary under club rules (s.85(3)).

Each act, however, inherently reflects the needs and circumstances of its respective era. Albeit the MIA 1906 has been a remarkable success, it has become outdated due to the fact that the concept of consumer has developed. The diversity between the MIA 1906 and consumer insurance has become intense.[50] After the stimulation of the concept of consumer and the ever-increasing clamours for reform to overhaul the antiquated MIA 1906, the distinction between consumer and non-consumer insurance has become clearer. At long last, three statutes were enacted, the foremost is the *Third Parties (Rights against Insurers) Act 2010* ("the TPA 2010"), updating its previous version of 1930. It reforms the statutory subrogation regime by excluding the defence of "pay to be paid" in terms of not all but specific claims.[51] The other two acts are the *Insurance Act 2015* and the *Consumer Insurance (Disclosure and Representations) Act 2012*. All of which are neither codifying nor repealing acts but only reforming ones. In practice, club rules both incorporate the MIA 1906 and the aforesaid Act of 2015. That being the case, they exclude the particular sections of the latter one.[52]

Apart from those *ut supra*, there are also relevant acts, or at least provisions thereunder, applicable to P&I insurance, some of which are the *Contracts (Rights of Third Parties) Act 1999* ("the CRTPA 1999"), the *Merchant Shipping Act 1995* ("the MSA 1995"), the *Companies Act 2006*, the *Arbitration Act 1996*.

ii. Contractual Framework

aa) In Terms of Insurance Law

Marine insurance is a contract providing cover against "losses incident to marine adventure" pursuant to section 1 of the MIA 1906. Going a step further, there is said to

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[50] Hertzell, D.: The Insurance Act 2015: Background and Philosophy, Clarke, M. / Soyer, B. (editors): The Insurance Act 2015: A New Regime for Commercial and Marine Insurance Law, Informa Law from Routledge, Abingdon 2017, p. 2-5.

[51] For detail concerning the rule, *see infra,* Part IV.A. For detail concerning the Act, *see infra,* Part V.B.3.a.

[52] For detail, *see infra,* Part II.B.3.c.ii.bb.

be a marine adventure in certain situations pursuant to section 3(2) of the MIA 1906, under which subsection (c) addresses the essence of P&I. Additionally, it was discussed that P&I is not only a time policy *per se*, but it is also marine insurance within the meaning of sections 1 and 3 of the MIA 1906.[53] It can, thus, be considered to be marine insurance.

That aside, P&I is liability insurance, but different from traditional liability insurance, the underlying rationale of which will be analysed elsewhere in this thesis in conformity with the effects of the "pay to be paid" rule in that regard, thereby refraining from giving more detail herein.[54] It is also mutual insurance based on non-fixed calls. Its purpose is to ensure the mutual benefits of members. Related details can be found elsewhere *infra*.[55]

With the exception of the evolution of compulsory insurance over the recent decades in particular fields of maritime law in view of the public interest and protecting third-party claimants, this distinction is nothing more than an abstract legal standpoint and is not notable in terms of practical reality where every prudent shipowner purchases a P&I cover. That being the case, it is still based on voluntariness from a legal perspective. Details and the effects of the "pay to be paid" in this regard will be analysed later on.[56]

Finally, it is non-consumer (business or commercial) insurance because it covers the risks arising out of the use or operation of the ship in maritime-based commerce, and it is also private insurance – not social insurance originating from public law, protecting persons against such as unemployment or old age, and carried out by state authorities – because the insured has the freedom to choose with whom he has his risks insured.[57]

bb) In Terms of Law of Obligations

Needless to mention, P&I insurance is in the form of a contract.[58] Doubts in that respect were dispelled later on in cases where courts held that it was a contract while they were

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53 *Compania Maritima San Basilio S.A. v The Oceanus Mutual Underwriting Association (Bermuda) Ltd (The "Eurysthenes")* [1976] 2 Lloyd's Rep 171; Hazelwood / Semark, 46-47.
54 *See infra,* Parts III.B.2. and IV.A.
55 *See infra,* Part IV.B.
56 *See infra,* Parts V.A. and V.B.
57 Vaughan / Vaughan, 45, 48; Kayıhan / Günergök, 24-25.
58 MIA 1906, sections 1, 3(1), and 3(2)(c).

discussing whether the agreement between a club and its member would fall within the scope of the *Third Parties (Rights against Insurers) Act 1930* ("the TPA 1930").[59]

The P&I policy year commences on 20 February, and ends thereon of the next year with the exception of mid-year entries where the calls are paid pro rata. It helps for records, calculations, and contributions to be evaluated simultaneously. At the end of the period, it is renewed automatically unless one party notifies the other regarding termination.[60]

Contractual documents used in the practice are *ut infra:* "Certificate of entry" corresponds to policy together with club rules, the Memorandum of Association, and the Articles of Association.[61] However, it does not always reflect the current status of cover because "endorsement slips" might be issued to vary the scope.[62] "Club rules", to which the certificate of entry refers, *in extenso*, include provisions concerning the details of the contract, that is, the scope of cover, exclusions, and obligations. Rules of different clubs are almost identical. Clubs might also issue "bye-laws" as the appendices to club rules.[63] "Memorandum of Association" and "Articles of Association", to which the club rules refer, govern the foundation and management.[64] Lastly, "circulars" is the communication network for clubs to notify their members in terms of any situation concerning them.[65]

Over and above these, there are contractual obligations imposed on parties:

(1) Provided that the club accepts an application made, it will be under obligation to issue a certificate of entry and deliver it to the member.[66]

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[59] *Wooding v Monmouthshire & South Wales Mutual Indemnity Society Ltd Etc* [1939] 4 All ER 570; *Allobrogia Steamship Corporation (The "Allobrogia")* [1979] 1 Lloyd's Rep 190. *See also* Tilley, M.: "Protection and Indemnity Club Rules and Direct Actions by Third Parties", ***Journal of Maritime Law and Commerce***, 1986, Vol. 17, Iss. 3, p. 427, 431-436; Acar, Kulüp Sigortası (P&I), 539; Hazelwood / Semark, 45-46, 293-294.

[60] Hazelwood / Semark, 349-350.

[61] *British Marine Mutual Insurance Company v Jenkins and Others* [1900] 1 QB 299; *The United Kingdom Mutual Steamship Assurance Association Limited v Nevill* (1887) 19 QBD 110; Hazelwood / Semark,60.

[62] Hazelwood / Semark, 39-42.

[63] Hazelwood / Semark, 58-59.

[64] Hazelwood / Semark, 10. *See also* the *Companies Act 2006* (c. 46), section 8 and sections 18 *et seq.*

[65] Acar, Kulüp Sigortası (P&I), 93.

[66] Britannia, Rule 6(3); Shipowners, Rule 38(1); North, Rule 7(3); London, Rule 6(1); UK, Rule 12(A); West, Rule 33(1); Steamship, Rule 7(i); Skuld, Rule 1.1.3; Gard, Rule 5(1); American, Rule 1, section 4.6; Japan, Rule 1(4).

(2) The characteristic obligation on the part of the club is to assume the risks regardless of the fact that they will occur or not, and if so, undertake to indemnify the member.

(3) The characteristic obligation on the part of the member is, in return for the club's assuming of risk, to undertake to pay non-fixed calls, which are classified as follows:

(i) "Advance or estimated total calls" are levied as an up-front fee in the course of entry or as instalments during the policy year by evaluating the records of retrospective five years;[67]

(ii) "Supplementary or additional calls" are levied when the number of claims exceeds the advance calls;

(iii) "Overspill calls" are levied if there are unexpected catastrophic claims exceeding reinsurance limits;
As for supplementary and overspill calls, they might be collected during and, because of the delay of claims, until two years after the end of, the policy year.[68] Policy years are, therefore, kept open for additional two years afterwards for the clubs to be able to collect such calls; and

(iv) Lastly, "release calls" are levied, for relieving the member of his prospective duties regarding his period in the club, when the membership is ceased.[69]

(4) With respect to the duty of fair presentation (or duty of utmost good faith), comprising of "duty of disclosure" and "duty to abstain from misrepresentation", the insurer wants to know in respect with whom he will assume the risk and for whom he will provide cover. The insurer is bound by the disclosures and representations of the insured, and it naturally affects the judgment of the insurer relying on the information given as to whether or not

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[67] The rationale is that the settlement of claims takes time, and thus, the emergence of useful claims records occurs in, at least, four or five years. *See* to that effect, Hazelwood / Semark, 102. *See also* Britannia, Rules 11 and 14; Shipowners, Rule 51; North, Rule 13(1); UK, Rule 20; West, Rules 43 and 44; Standard, Rules 18.1 to 18.6; The Swedish Club, Rules for P&I Insurance, 2023/2024, Rule 22 ("Swedish"); Skuld, Rule 4.2; Gard, Rules 10 to 12; Japan, Rule 6(1)(1).

[68] Britannia, Rules 11(3) and 11(4); Shipowners, Rules 52 and 53; North, Rules 13(2) to 13(7); London, Rules 32 and 33; UK, Rules 21 and 22; West, Rules 45 and 45a; Standard, Rules 18.7, 21, and 22; Swedish, Rules 23 and 24; Skuld, Rules 4.3 and 4.4; Gard, Rules 13 and 18; Japan, Rules 6(1)(2 and 3).

[69] Britannia, Rule 14; Shipowners, Rule 55; North, Rule 16; London, Rule 36; UK, Rule 30; West, Rule 45b; Standard, Rules 19.1 to 19.8; Skuld, Rule 4.5; Gard, Rule 15; Japan, Rule 6(1)(4). *See also* Ronneberg, 29-30; Acar, Kulüp Sigortası (P&I), 284-288; Hazelwood / Semark, 98-101, 104-105, 119.

it will assume the risk or under which terms it will do so. So much so that, the contract is based on not "*bona fide* (good faith)" but "*uberrimæ fidei* (utmost good faith)". The matters pointed out above apply to P&I where, owing to mutuality, these duties are much more paramount, and therefore, the member shall disclose a wider range of circumstances.

Even though the harshness of the "draconian remedy" of retrospective avoidance of the contract in case of a breach of this duty has already been ameliorated by the *Insurance Act 2015*,[70] clubs were not avoiding the contract even before 2015. Instead, they were choosing alternative solutions, *e.g.*, rejecting to pay indemnity or deducting from indemnity.[71] As of now, clubs exclude the sections regarding remedies of the above-cited Act in any case.[72] On the part of the club, the duty is to disclose the financial status and annual reports. It shall also disclose the extent of special entries on fixed-premium bases considering that these entries might be risky and to the detriment of mutuality. Because the club, if needed, will not be able to collect supplementary or overspill calls from those entrants, who are only liable for fixed premiums, and this situation might, despite not quite possible, give rise to the insolvency of the club. Such disclosure is, therefore, crucial for members.[73]

(5) Lastly, members shall comply with the warranties,[74] which shall be strictly adhered to. It is worth noting that in that regard, the warranty to promptly notify, and submit documents to, the club is paramount in the event of a loss or claim for the club to take the

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[70] *Insurance Act 2015* (c. 4), sections 8 and 14(1). *Confer* MIA 1906, sections 17, 18(1), and 20(1) before the enactment of the Insurance Act 2015.

[71] Acar, Kulüp Sigortası (P&I), 337.

[72] Britannia, Rule 3(5); Shipowners, Rule 1(10)(A); North, Rule 6(1); London, Rule 43; UK, Rule 5(L); West, Rule 21; Standard, Rules 1.5.1 and 1.5.2.

[73] Hazelwood / Semark, 32-36.

[74] Warranties in P&I are, *inter alia*, the express (not implied) warranty of seaworthiness, navigational warranties, crew warranty, warranties in respect of the use or operation of the ship, warranty requiring the ship to be classed by a classification society at the time of entry and to maintain it during the policy, warranties of ISM and ISPS compliance, warranty of paying calls, warranty of not admitting the liability which otherwise will bind the club, warranty of notifying the club about losses and claims, warranty of paying the claim before seeking indemnity, warranty of taking necessary steps to mitigate or avert the liability. *See* Harter, S.: "Warranties and Exclusions in Protection & Indemnity Policies", ***Seminar*, *American Institute of Marine Underwriters***, New York 2003, p. 4-7; Hazelwood / Semark, 195-204.

necessary steps, for its right of subrogation not to be prejudiced, for the member to assist its club, and for the club to realistically assess calls and manage its funds accordingly.[75]

4- Other Types of Marine Insurance

War and strike insurance covers the losses arising out of, *inter alia*, state interventions, invasions, riots, strikes, insurrections, and revolutions that occurred during the voyage or at the ports.[76] As discussed, these risks are generally excluded from any type of insurance, by inserting a "free of capture and seizure" clause, by the reason of their unpredictability in many aspects. Nevertheless, it is possible to expand the cover in order to include such risks in return for an additional premium or a call. Other types of marine insurance are:

(1) Freight insurance covering the freight fees that cannot be earned;[77]

(2) Loss of hire insurance under which the owner is insured against the loss of income under a charterparty during the repair period of the damaged vessel;[78]

(3) Builder's risk and ship repairer's liability insurance covering the loss under construction and during repair, respectively;[79]

(4) Charterers' liability insurance covering the liability under a charterparty;[80]

(5) Liability insurance covering the legal liabilities of wharfingers, terminal operators, and stevedores;[81]

(6) Kidnap and ransom insurance; and

(7) Tower's liability insurance.[82]

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[75] Hazelwood / Semark, 307-318; Li, L.: "Marine Insurance Law – General Conditions in Hull, Cargo and P&I Covers", ***Asian Business Law.***, 2014, Vol. 13, p. 129, 141-142.
[76] Lemon, 1495-1497; Lin, 10-11.
[77] Institute Time Clauses, Freight, 1/11/95; Institute Voyage Clauses, Freight, 1/11/95; Institute General Average – Pollution Expenditure Clause, Freight, 1/1/96.
[78] Lemon, 1476-1478; Lin, 9.
[79] Lemon, 1494-1495.
[80] Lemon, 1488.
[81] Lemon, 1492-1493; Hayden / Balick, 332-333.
[82] Hayden / Balick, 332-333.

III. HISTORY OF P&I INSURANCE

A) EVOLUTIONARY BACKGROUND

1- Impacts of the Bubble Act 1720 and the Period Theretofore

England participated in the Nine Years' War between 1688 and 1697, during which 100 ships of the Smyrna convoy with a cargo valued at £1,000,000 were captured in 1693. It led to the underwriters having difficulties in fulfilling their obligations. The second period of wars began with the War of the Spanish Succession (1701-1714) in which England participated again. Wars, however, were expensive inherently. So much so that, Great Britain was left with a debt of £5,000,000. The difficulties which the underwriters incurred resulted in the insolvency thereof.[83]

During that period, insurance companies, which were initially founded *circa* 1680s and onwards following the Great Fire of London in 1666, were in high demand.[84] A very well-known marine insurance company then, namely The South Sea, was founded at the turn of the 18th century and made an extreme profit, thereby also undertook the debts of the government. Nevertheless, such financial growth brought fraudulent transactions which were followed by other companies. Eventually, financial collapses occurred among which the South Sea Bubble was the most remarkable one.[85] In the wake of this, the government enacted the *Bubble Act 1720* with the intention of controlling such companies and restoring the damages suffered theretofore.

Despite the fact that the Act of 1720 solely chartered the London Assurance and the Royal Exchange Assurance to provide insurance, it prohibited other companies, partnerships, and societies from being established to that end;[86] therein lies the problem that led to monopolisation thenceforwards. On the bright side, the underwriters of Lloyd's and

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[83] Reynardson, W. R. A. B.: "The History and Development of P&I Insurance: The British Scene", ***Tulane Law Review***, 1969, Vol. 43, Iss. 3, p. 457, 458-459.

[84] James, P. S.: "Nicholas Barbon--Founder of Modern Fire Insurance", ***The Review of Insurance Studies***, 1954, Vol. 1, Iss. 2, p. 44, 45-47; Swiss Re: A History of Insurance, p.10, ***https://www.swissre.com/dam/jcr:638f00a0-71b9-4d8e-a960-dddaf9ba57cb/150_history_of_insurance.pdf*** ***(accessed 16/02/2023)***.

[85] Reynardson, 459; Lin, 11.

[86] Reynardson, 460; Gürses, 74.

mutual associations, the latter of which the P&I clubs would derive from later on, were not within the scope of application of the Act, and therefore, their development became easy. At that time, the total amount of business in marine insurance was mostly carried out between Lloyd's underwriters (9/10ths) and the two chartered companies (1/10ths).[87]

Over and above this, there were also criticisms directed at marine underwriting of that time. First of all, and owing to the outbreak of wars yet again, British merchant ships were destroyed or seized by enemy forces during the war. Thus, the size and numbers of losses, and accordingly the claims, were so significant that some of the underwriters became bankrupted or became reluctant to provide insurance, and the insureds, including shipowners, did not get paid. Underwriters were, therefore, cautious and covering a limited range of risks in exchange for high premiums. Moreover, the monopoly deprived the market of competition, and therefore, the premiums and inflexibility in accepting risks increased. Furthermore, the underwriters became more litigious resulting in delays in providing recoveries. Lastly, the shipowners, residing away from London which was the centre of the insurance market, either had no opinion or were narrow-minded regarding the solvency and faithfulness of the underwriters conducting their businesses in a big city.

In the light of these concerns, shipowners were neither satisfied with the monopoly companies, nor with the individual underwriters. From the mid-18th century towards the end of the century, such dissatisfaction led individual shipowners at outlying ports to associate and insure the hull risks between themselves based on mutuality. Thus, an insured shipowner was also a member of the association in which all the shipowners were considered to be the insurers of each shipowner collectively. They, therefore, overcame the prohibition resulting from the aforesaid Act of 1720 since the association had no legal personality. Moreover, shipowners were not doing insurance for profit, thus the insurance became cheaper than before. Besides, the consideration was mutual "calls" collected by shipowners in lieu of premiums. Consequently, the hull clubs, that is, the predecessors of P&I clubs of today, emerged. They were, however, solely insuring hull risks back then.[88]

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[87] Lin, 12; Gürses, 74, 76.
[88] Reynardson, 460-463; Ronneberg, 3; Acar, Kulüp Sigortası (P&I), p. 11; Hazelwood / Semark, 1-3.

2- Decline of the Hull Clubs and Increasing Liabilities of Shipowners

The charter previously granted to two companies was withdrawn in 1824, and thereafter, the number of companies as well as the competition between Lloyd's underwriters and new companies increased, which ended up with the decline of hull clubs and gradual closure of many of them due to their inability to compete in the market. As if that were not enough, after the Industrial Revolution that resulted in the building of steamships, the issue of third-party liability of shipowners popped out and gradually increased, which had not been regarded as a problem theretofore, by the reason of the increase in the value and size as well as the complexification of ships and cargoes thereon.[89]

First and foremost, the *locus classicus* of increasing third-party liabilities of shipowners was the case of *de Vaux v. Salvador* in 1836.[90] It was held that the liability arising out of collision damages was not included in the scope of the hull policy owing to the fact that the collision was not a "peril of the sea" and not recoverable pursuant to the policy.[91] Besides that, the *Marine Insurance Act 1745* had already forbidden insurance cover in excess of the value of the ship.[92] In response, the insurance cover expanded in practice in the manner that it would consist of the liability for collision damages suffered by the other ship and cargo thereon on the condition that the policy included the "running down clause" enabling to cover such damages up to 3/4ths. The remaining 1/4ths, as well as the excessive damages, were excluded from hull cover since the due diligence of the shipowner was expected, *i.e.*, the underlying rationale was to urge them to be careful.[93]

Between the 1820s and 1880s, tens of thousands of people, particularly following the exploration of gold in America and Australia, emigrated from the United Kingdom ("UK") to those countries with the intention of obtaining a more prosperous life. Those

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[89] Reynardson, 464; Tilley, M.: "The Origin and Development of the Mutual Shipowners' Protection & Indemnity Associations", ***Journal of Maritime Law and Commerce***, 1986, Vol. 17, Iss. 2, p. 261, 266-267 (hereinafter "The Origin and Development"); Acar, Kulüp Sigortası (P&I), 11; Lin, 13-14.

[90] *de Vaux v. Salvador* (1836) 4 Ad & E 420.

[91] Reynardson, 466; Tilley, The Origin and Development, 262; Hodges, S.: Cases and Materials on Marine Insurance Law, Cavendish Publishing, London 1999, p. 535; Rose, 301.

[92] Lin, 14; Hazelwood / Semark, 5.

[93] Reynardson, 467; Rose, 302; Lin, 15; Hazelwood / Semark, 5; Pekşen, 7. The "Running Down Clause" was introduced in 1861; however, it was not until 1888 it incorporated into the Institute Time Clauses Hulls dated 1888. For detail, *see* Reynardson, 467; Algantürk Light, 84.

sea voyages were exactly a marine adventure due to tough conditions, and no act was protecting them until the enactment of the *Fatal Accidents Act of 1846* (9 & 10 Vict. c. 93) governing the liability of shipowners who negligently caused injury to or death of others. Hence, dependants of the deceased started to file suits against shipowners on the ground of their wrongful acts.[94] Latterly, shipowners were exposed to a broader liability, to which the wrongful acts of the crew were also added, *i.e.*, the vicarious liability of shipowners was established. The liability was, however, unlimited, and neither the standard Lloyd's policy nor the hull policy was covering third-party liabilities back then. A corollary effect of this, following the insistence of shipowners, was the enactment of the *Merchant Shipping Act 1854* (17 & 18 Vict. c. 104) which limited their liability to the sum of the ship and freight. That being the case, the value of ships had to be at least £15 per ton as a condition precedent for the limitation; however, many were less than that. As a result of which, the shipowners were still vulnerable.[95]

Furthermore, the *Harbours, Docks and Piers Clauses Act 1847* authorised the harbour authorities to recover damages to port structures, including from shipowners.[96] In addition, the *Employers' Liability Act 1880* governed a payment by employers, including shipowners, to employees injured during employment.[97]

From the foregoing events, it is possible to conclude that, *inter alia*, any claims regarding personal injury and loss of life were not covered, and claims regarding the 1/4ths collision liability were still a tremendous burden. Besides, the excess liability was also a significant concern for sure. Shipowners had to pay regard to the ever-present dangers at seas. Hence, as the liability of shipowners accordingly increased, obtaining protection against these dangers became a significant need.

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[94] Reynardson, 465-466; Tilley, The Origin and Development, 263; Nolan, D.: The Fatal Accidents Act 1846, TT Arvind / Steele, J. (editors): Tort Law and the Legislature, Hart Publishing, 2012, p. 135-140; Sözer, B.: Deniz Ticareti Hukuku, Vol. I, 5th ed., Vedat Kitapçılık, İstanbul 2019, p. 242-243.

[95] Reynardson, 466; Tilley, The Origin and Development, 263-264; Hazelwood / Semark, 6.

[96] *Harbours, Docks and Piers Clauses Act 1847* (10 & 11 Vict. c. 27), s. 74; Hazelwood / Semark, 6, 140.

[97] *Employers' Liability Act 1880* (43 & 44 Vict. c. 42); Hazelwood / Semark, 6.

3- From Protection Plus Indemnity Onwards

While shipowners were dwelling on how to obtain protection in the middle of the 19th century, they realised that the solution was in front of their eyes. Hull clubs of the not-so-distant past, therefore, converted into protection clubs by which shipowners could protect themselves against third-party claims.[98] In this sense, the Shipowners' Mutual Protection Society was the first protection club in the world, founded in 1855, currently known as Britannia P&I.[99] Foundation of other clubs continued thenceforth.

At the beginning, clubs were solely providing protection. In 1870, *The Westernhope*, proceeding to Cape Town, deviated from the agreed route and sank. Thereafter, the cargo interests claimed for the damages from the owner. Nonetheless, the protection club, to which the shipowner was insured, did not indemnify such claims because the club rules did not cover such losses and there was also a deviation. It was held by the court that he was liable for the loss of the cargo. Therefore, despite the fact that the club made a few *ex gratia* payments, the shipowner bore the loss himself. Likewise, *The Emily* stranded, and the shipowner had to compensate the cargo interests on the ground that such stranding was not because of a peril but navigational negligence. The bill of lading issued in that event did not, however, protect the shipowner against such negligence. In short, they were not relieved of liabilities in both events. The increase in cargo claims, which did not completely lay a burden on shipowners until the end of the 19th century, disconcerted them, and thus, a new class was proposed to be added by a club to indemnify the owners. Others followed this, and P&I clubs were established by the end of the 19th century.[100]

Following the amalgamation of the "protection" and "indemnity" classes, the distinction between them lost its significance. It is now regarded as a historical distinction stuck in the dusty pages of history, and it has no importance at present having regard to the fact that their basic functions are similar. In addition, the scope of cover has been broadened gradually, and clubs were later reorganised as companies.

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[98] Lin, 17; Hazelwood / Semark, 6.

[99] Britannia P&I: "History", ***https://britanniapandi.com/about/history/*** ***(accessed 20/02/2023)***.

[100] Reynardson, 467-468; Tilley, The Origin and Development, 264-265; Lin,18-20; Hazelwood/Semark,7.

4- Reinsurance and the Pooling System

Losses occurring at the same time might put much strain on insurers. When viewed from this aspect, they might face enormous risks and claims exceeding their capacities. As a matter of fact, they might become insolvent. To refrain from such danger, spreading and transferring the risk becomes pivotal in the context of insurance once again, but in the eyes of insurers this time. As a consequence, they might reinsure themselves for the risks that they would not, or could not, otherwise accept, for the contracts they wish to conclude, and therefore, they might undertake more significant risks in the market. In brief, there is said to be a contract of reinsurance where the reinsured, insurer of an already existing contract of insurance, purchases insurance to obtain cover from the reinsurer, that is to say, another insurer who undertakes to indemnify the loss of the reinsured.

In the wake of the development of shipping and technology, *inter alia*, tonnages of ships, and thus, the amounts of cargoes carried thereon has increased. Third-party claims have broadened, and as a consequence of which, so have the liabilities of shipowners. Due to the mutual system operating in the clubs, shipowners were paying advance calls in the course of their entry to the club. Furthermore, it was possible for clubs to collect whip-rounds, or more exactly, supplementary or overspill calls in case of an emergency. Conversely, these calls were unexpected and could reach a high amount. Thus, this solution was somewhat less satisfactory in the eyes of club members, and clubs remained at risk. They, therefore, overcame this problem, not only by increasing the advance calls to refrain from the problems of default or non-payment of shipowners in the event of urgency *per se*, but also by reinsuring themselves. In 1899, a pooling agreement was, to that end, concluded for the first time between six British clubs, namely the London Group,[101] in which the others participated later on.[102]

As of now, it is known as the International Group, in accordance with the reinsurance programme of which a club retains a portion of its own risk, up to a limit called the "club retention" and the others proportionately and collectively bear the exceeding remainder

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[101] These six clubs are: Britannia, the UK, London, Standard, Sunderland, and Newcastle. For detail, *see* Watson, N.: 150 Years of the London P&I Club: 1866-2016, St. Matthew's Press, Leyburn 2016, p. 30.

[102] Acar, Kulüp Sigortası (P&I), 435; Hazelwood / Semark, 365.

up to another limit called the “lower pool”. The excess of it, the “upper pool”, is reinsured via Hydra Insurance Company Limited, which was founded by the clubs. For potential catastrophes over the pool, reinsurance is purchased from the market and Hydra.[103] Apart from that, there is no hurdle for each club to purchase reinsurance for its own retention.

5- Moving to Offshore Countries

Another milestone against the backdrop of the evolutions of clubs was the devaluation of the pound sterling in 1967 that led to, *inter alios*, the clubs falling into an economic crisis. They, therefore, collected supplementary calls reaching high amounts, ending up with the displeasure of their members. On the opposite, the non-collection of such calls could have caused worse problems, including bankruptcy.[104]

When the clubs could not solve their problem in the UK, from the 1970s, they considered moving their headquarters to offshore countries,[105] in which the financial status was better. They, however, jumped out of the frying pan into the fire, so to speak, *i.e.*, they escaped from economic to legal uncertainty on the ground that no law and jurisdiction accurately perceived P&I insurance other than English law and jurisdiction. As a result, clubs incorporated the positive aspects of this dilemma, not only by moving their administration and headquarters to offshore countries *per se*, but also by preserving their places in the UK. In fact, nothing changed. Claims handling and underwriting functions of clubs continued to be conducted in the UK as if they were the agencies of the registered overseas companies, and English law and jurisdiction continued to be applied under club rules.[106] Only the management was being carried out in offshore countries.[107]

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[103] IG P&I: “2023/24 Pool and GXL Reinsurance contract structure”, ***https://www.igpandi.org/reinsurance/*** ***(accessed 01/03/2023)***.

[104] Acar, Kulüp Sigortası (P&I), 48; The National Archives: “The 1967 Devaluation of the Pound”, ***https://webarchive.nationalarchives.gov.uk/ukgwa/+/https://www.nationalarchives.gov.uk/cabinet-office-100/the-1967-devaluation-of-the-pound/*** ***(accessed 02/03/2023)***.

[105] For instance, *see* Shipowners’ Club: “History of the Club”, ***https://www.shipownersclub.com/160-years/#1976/1*** ***(accessed 28/02/2023)***; West: “History of the Club”, ***https://www.westpandi.com/about-us/150th-anniversary/*** ***(accessed 28/02/2023)***.

[106] Britannia, Rule 46; Shipowners, Rule 1(10)(A); North, Rule 51; London, Rule 43; UK, Rule 42; West, Rule 57; Standard, Rule 25; Steamship, Rule 48. *Confer* Swedish, Rule 2, paragraph 6; Skuld, Rule 47; Gard, Rule 90; American, Rule 1, section 4.52; Japan, Rule 48.

[107] Acar, Kulüp Sigortası (P&I), 47-50; Hazelwood / Semark, 12-13.

B) PROVIDERS AS OF TODAY

1- P&I Clubs

a) Legal Structure

P&I insurance is mainly provided by P&I clubs among which the English ones have overwhelming supremacy. First and above all, they were established on the exact basis of mutuality. Because the years during which the clubs were established were the monopoly years, they were organised as unincorporated associations of which the shipowners were the members. At those times, membership was signifying a dual role where a member was not only the insured via the association *per se*, but also the insurer together with all members.[108] Section 85 of the MIA 1906 was exactly fitting for the purpose of the clubs of earliest times. Following the enactment of the *Companies Act 1862*,[109] clubs were gradually incorporated, thereby having legal personalities. As of today, they are still incorporated companies, that is to say, private companies limited by guarantee with no shareholders and share capital on a non-profit-making base pursuant to the *Companies Act 2006*.[110] As regards the members, they solely have the status of an insured now.

b) Constitution and Management

Clubs are founded upon two documents, the Memorandum and Articles of Association, in compliance with which the General Meeting is placed at the top of the club. This body is formed by members and held once a year except for, if necessary, interim meetings.[111]

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[108] Tilley, The Origin and Development, 267-268; Acar, Kulüp Sigortası (P&I), 40; Lin, 21.

[109] Companies Act 1862 (25 & 26 Vict. c. 89), sections 6, 9 and 14; Pulbrook, A.: The Companies Act 1862 with Analytical References and Copious Index, Effingham Wilson, London 1865, p. 3-7.

[110] *Companies Act 2006* (c. 46), section 3(3); Lin, 21; Hazelwood / Semark, 9; Pekşen, 33; Burucuoğlu, G.: "Kulüp Sigortası (P&I) Çerçevesinde Eşyanın Zıyaı veya Hasarı Halinde Teminatın Kapsamı", Master's Thesis, Ankara University, 2019, p. 33. For instance, *see* Companies House: "Britannia Steam Ship Insurance Association Limited (The)", ***https://find-and-update.company-information.service.gov.uk/company/00010340*** ***(accessed 24/02/2023)***; Companies House: "North of England Protecting and Indemnity Association Limited (The)", ***https://find-and-update.company-information.service.gov.uk/company/00505456*** ***(accessed 28/02/2023)***; Companies House: "The United Kingdom Mutual Steam Ship Assurance Association Limited", ***https://find-and-update.company-information.service.gov.uk/company/00022215*** ***(accessed 28/02/2023)***.

[111] The powers and duties of the General Meeting are, *inter alia*, (1) drawing up and amending the club rules, (2) deciding in respect of the accounts and annual reports, (3) electing the Board of Directors and

In the hierarchy, the second organ is the Board of Directors conducting the business. Any member might become a director or be nominated to become one. As compared to General Meeting, voting rights are not in parallel with the entered gross tonnages but entered ships. It has wide-ranging powers and duties.[112] Apart from those specific duties peculiar to clubs, directors are subject to the *Companies Act 2006* and the general duties thereunder by which they shall abide.[113] Furthermore, they exercise their powers, duties, and discretion *bona fide*.[114] Club rules might also grant absolute discretion in particular situations to directors or contain the "omnibus rule", both of which enable them to decide without explaining the reasons. Discretion is exercised without prejudice to the principle of *bona fide* howsoever, pursuant to which the directors consider the benefits of the club.

As regards the managers, they are responsible for the daily management of the club and the services rendered for claims handling, both of which otherwise will not rapidly be accomplished if the directors are late to meet due to busyness or absence, thereby affecting the required periodic meetings. Managers might bind the club via contracts and settlements to the extent set out under the Articles of Association. They might also admit members; however, it must be absolutely borne in mind that special entries based on fixed premiums are usually exercised by directors for the sake of the club, the rationale of which will be set forth below.[115]

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determining the remuneration thereof, (4) electing the auditor, (5) amending the Articles of Association, (6) deciding in respect of the matters brought before it by the directors, (7) determining the dissolution or amalgamation of the club with others. For detail, *see* Hazelwood / Semark, 10-11; Lin, 22.

[112] The powers and duties of the Board of Directors are, *inter alia*, (1) administering the club in conformance with the requests of the members, (2) settling disputes between the club and the members before proceeding to arbitration, (3) approving claims if required, (4) fixing the amount of and levying the calls, and deciding the frequency thereof; however, such determination will be without prejudice to the Board's right to levy supplementary calls to the tune of greater amounts, (5) deciding upon the interest in respect of due but not paid calls, the rate of which is at the Board's absolute discretion, (6) approving reinsurance, (7) settling claims and financial issues, (8) deciding the opening and closing of policy years, (9) administering the club funds and how to use reserves or surpluses, (10) initiating the amendments with respect to the club rules, (11) employing and dismissing the staff, and deciding the remunerations thereof, (12) issuing bye-laws. The powers, duties, and discretions of the Board might be assigned and fulfilled by sub-committees or managers delegated by the Board. For detail, *see* Hazelwood / Semark, 11-12, 24, 58, 104, 108, 112, 119-120, 229-230.

[113] *Companies Act 2006* (c. 46), sections 171 to 177.

[114] *Re Smith & Fawcett Ltd* [1942] Ch 304. The duty is now embodied under the *Companies Act 2006* (c. 46), section 172.

[115] *See infra,* Parts III.B.1.d. and IV.B. The powers and duties of managers are, *inter alia*, (1) appointing correspondents, (2) claims handling, (3) underwriting, (4) issuing certificate of entries, (5) admitting

c) Correspondents and Brokers

Claims are extensive and complicated, but they also need rapidity. Thus, there must be an efficient "claims handling" process for them to be promptly and adequately handled when they arise. That aside, know-how is needed with regard to the measures to minimise the damage or loss, evidence gathering, suits to be filed, and any other technical or legal support to those ends. That being the case, directors and managers are far away, and they, together with the shipowner and crew, know neither the language nor the current law, customs fines, or competent domestic authorities of the country wherein the incident takes place. Overcoming the hurdles above is merely possible by constituting a global network via correspondents as the "eyes and ears" of clubs worldwide. They are obliged to promptly notify the club regarding the incidents, out of which the claims have arisen, and conflict of interests where the correspondents work with more than one club.[116]

It is often accepted that the correspondents are not the agents of clubs, thereby having neither the power to settle claims, nor the authorisation in terms of legal proceedings and acceptance of the notification of claims on behalf of the club *ex officio*.[117] On the other hand, it is possible for a club to appoint its respective correspondents, *e.g.*, attorneys-at-law in the cases brought by or against them. Correspondents might also act as an insurance broker on behalf of the member during contractual negotiations. From the preceding discussion, it is possible to make the following observation that although correspondents might act as an agent of the club in some cases, such situations are exceptional, and the club shall authorise them and give instructions to that effect. Otherwise, this leads to the empowerment of the correspondents with respect to settling claims or standing to sue or be sued, both of which are costly and highly significant so that the handling of those by

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members, (6) deciding upon as to whether or not to provide a guarantee, (7) maintaining records, (8) paying claims and submitting reports to the Board of Directors, (9) assigning the contract of membership or rejecting an assignment, and in the case of assignment, issuing an endorsement slip, (10) if empowered, concluding the contracts of reinsurance, (11) executing the basic policies and decisions of the Board of Directors, (12) issuing circulars and sending them to members. For detail, *see* Ronneberg, 25; Acar, Kulüp Sigortası, 93; Hazelwood / Semark, 12-15, 69, 70-71, 91, 230, 256.

[116] *International Group Guidelines for Correspondents, September 2022*, Guidelines 3, 4, and 11, ***https://static.igpandi.org/igpi_website/media/article_attachments/Correspondents_Guidelines_-_2022.pdf*** ***(accessed 03/03/2023)*** ("IG Guidelines"); Acar, Kulüp Sigortası (P&I), 64-65; Hazelwood / Semark, 16-17.

[117] IG Guidelines, Guideline 1; Hazelwood/Semark, 15-16, 230.

clubs is more appropriate. To summarise, they carry out activities limited to consultancy as they are not agents of the clubs as a rule; however, it might change from case to case.

As to brokers,[118] they act on behalf of the members during the entry or renewal of the membership with the club, or even in respect of changing it. What is important in terms of P&I, as opposed to marine insurance in general, is that clubs can solely recover calls from shipowners, not from brokers, and members, not clubs, shall pay the brokerage fee regardless of the membership is effected via a brokerage or not.[119]

d) Club Membership

Entry to the club is twofold. First, membership is established between the club and the member. Secondly, insurance cover is provided as it is between an insurer and an insured. An event depriving the member of cover does not terminate the membership *ex officio*. Even the club can refuse the application for membership, it might still provide insurance. Besides, it has the freedom to reject the application without any reason. For those reasons, providing insurance and admittance is totally within its discretion.[120] In terms of insurable interest, the member should be exposed to potential liabilities for which he seeks cover.[121]

Nowadays, members are generally shipowners. They might also enter with a part tonnage, thereby contributing to calls and bearing losses, but acquiring fewer votes pro rata.[122] In contradistinction thereto, if they have a fleet of ships, they might, of course, enter them in the same club or various clubs. In case of the former, there is said to be a fleet entry where he will have a voice in the constitution and management on a pro-rata basis.[123]

In addition, there might be joint entries where the entrants are jointly and severally having rights and being exposed to liabilities. First of all, only one certificate of entry is issued

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[118] Brokers and agents are insurance intermediaries representing the insured and the insurer, respectively. Brokers are not authorised to bind the insurer, whereas agents are to do so via insurance contracts in the name and for the account of the insurer. For detail, *see* Rose, 5 § 1.17-1.18; Vaughan / Vaughan, 83.

[119] Hazelwood / Semark, 17-18. *Confer* MIA 1906, section 53.

[120] Acar, Kulüp Sigortası (P&I), 82; Hazelwood / Semark, 67.

[121] Hazelwood / Semark, 64. *See also* MIA 1906, section 5.

[122] Hazelwood / Semark, 64-66, 74. For instance, *see* Britannia, Rule 6(4); Gard, Rule 3(2).

[123] Hazelwood / Semark, 75-76, 109. For instance, *see* Britannia, Rule 16; North, Rule 10; London, Rule 25; Swedish, Rule, 31; Japan, Rule 14.

for them. Secondly, any notification or equal thereto directed to (or by) any one of them by (or to) the club shall be deemed to be directed to (or by) all of them. Thirdly, the failure of any one of them at fulfilling the obligations, *e.g.*, the non-disclosure of a material fact, shall be regarded as a failure of all. Fourthly, each and every one of them is jointly and severally liable in respect of the payments, *e.g.*, calls.[124]

As to group affiliate or the co-assured's cover, shipowners might be in relation to other companies which they totally or partly own, operate, or manage the ship. Claimants have the option to choose against whom they will file an application in consideration of financial capacities and easiness regarding the jurisdiction. The related companies will, of course, need cover on the assumption that they could be the ones sued although the shipowner should have been sued. The scope of co-assured's cover is limited to the extent for which the shipowner would have been responsible if the claims had been directed to him. Furthermore, the co-assured will lose his cover if the shipowner loses his right to recover. Most of all, the co-assured is not responsible for the payment of calls.[125]

Last but not least, members are responsible for non-fixed calls by virtue of the mutuality. There might, but limitedly, be special entries on a fixed-premium base howsoever, *e.g.*, time and voyage charterers or state-owned ships. Bareboat charterers, on the other hand, might avail of the standard cover, since they are also liable, like shipowners.[126] Ignoring that, it was held by the House of Lords *In Re Corfield* v *Buchanan*[127] that the special entrants, which were covered on a fixed-premium base, were not real members. The crucial point is to what extent the clubs admit these entries since all claims will, regardless of being transferred from advance calls or fixed premiums, be settled by the same pool. As recalled, clubs might collect supplementary or overspill calls from members, but not from those special entrants who are only liable for fixed and periodical premiums. From which it can be concluded that such entries should be balanced out delicately by clubs.

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[124] Hazelwood / Semark, 74-75. For instance, *see* Britannia, Rule 8(1); Shipowners, Rule 41; North, Rule 9; West, Rule 36; Swedish, Rule, 30; Japan, Rule 15.

[125] Hazelwood / Semark, 76-78. For instance, *see* Britannia, Rule 8(2); Shipowners, Rule 41; North, Rule 9; London, Rule 23; West, Rule 36; Swedish, Rule, 30.

[126] Hazelwood / Semark, 68, 79-81, 373.

[127] *Corfield* v *Buchanan* (1913) 29 TLR 258.

2- Traditional Insurance Companies

P&I insurance might also be provided by insurance companies using ordinary insurance technics. The main differences between such insurers and clubs are as follows:

(1) Foremost among these, traditional insurance companies do not operate on the basis of mutuality in contrast to clubs, *i.e.*, their relationship with the insured is not based on a membership. Hence, they collect fixed and periodical premiums, unlike clubs collecting non-fixed advance calls at the beginning of, or sometimes during, the policy year and non-assessable supplementary or overspill calls for additional two years following the end of the policy year.

(2) Traditional insurance companies carry out their activities with the aim of profiting, *e.g.*, they provide financial securities to that end. They are, thus, based on a shareholding system with shareholders and share capital compared to clubs, which conduct their businesses for the mutual benefit of their respective members and are also companies functioning on a non-profit-making base with neither shareholders nor share capital.

(3) So much so that, traditional companies wish to know their incomes and outcomes, which are in contradistinction to the basis of clubs where there might be unpredictable and unexpected supplementary or overspill calls.

(4) Furthermore, they do not have a network of correspondents handling claims on a global scale. As for clubs, on the contrary side, correspondents play a crucial role in the business when claims arise.

(5) They provide cover for short ranges, small ships, and not high amounts as compared to clubs providing cover for long ranges and big ships and providing almost unlimited cover.

(6) Last but not least, they indemnify the insured whether the third party is paid or not. Clubs, on the other hand, assert that its member shall pay the third party to be reimbursed by the club, which is the corollary effect of the so-called “pay to be paid” rule.

The market share of traditional insurance companies is incomparably less than the market share of P&I clubs.[128] There is a relationship of supplementation or cooperation between clubs and traditional insurers rather than competition because both of them conduct their activities in a manner that they will not overlap. For that very reason, traditional insurers provide cover for short ranges (not oceangoing) and smaller ships with less gross tons, whereas clubs provide cover for the contrariwise.[129] That being the case, some fixed premium insurers might provide cover as clubs do; however, they are reluctant in the business and face the danger of withdrawal to that effect, and it is a high risk since their capacity is inadequate.[130] As a result, they provide fixed premium cover generally up to United States dollar ("USD" or "US$") 500m,[131] which is obviously less than the limits of cover provided by clubs and reinsured by IG P&I.

It must be taken into consideration that the insured who pays is the weaker party of the contract *vis-à-vis* the insurer who only gives a promise of indemnity, and therefore, it is the one supposed to have a sustainable financial capability. In this sense, states enact binding and strict legislation in respect of insurers to have and maintain such capability.[132]

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[128] P&I clubs, particularly the members of IG P&I, insure the 90% of the oceangoing tonnage of the world. *See* IG P&I: "About the International Group", ***https://www.igpandi.org/about*** ***(accessed 02/03/2023)***.

[129] Acar, Kulüp Sigortası (P&I), 46; Pekşen, 39-40. However, clubs might also provide cover for smaller and short-range ships based on fixed premiums. For instance, *see* Shipowners' Club: "Club insurance cover", ***https://www.shipownersclub.com/insurance/*** ***(accessed 28/02/2023)***; North of England: "Sunderland Marine", ***https://www.nepia.com/about-us/who-we-are/sunderland-marine/*** ***(accessed 28/02/2023)***; The London P&I: "Owners' Fixed Premium Cover", ***https://www.londonpandi.com/our-services/owners-fixed-premium-cover/*** ***(accessed 28/02/2023)***; West: "Fixed cover", ***https://www.westpandi.com/products/standard-covers/fixed/*** ***(accessed 28/02/2023)***; Gard: "Nordic small craft", ***https://www.gard.no/web/products/nordic-small-craft*** ***(accessed 02/03/2023)***.

[130] For instance, AXA, a French insurer, who once carried out the business of providing P&I insurance withdrew from the business in 2005. For detail, *see* Acar, Kulüp Sigortası (P&I), 47.

[131] Røsæg, E.: "Compulsory Maritime Insurance", ***Scandinavian Institute of Maritime Law***, 2000, No. 258, p. 1, 4, ***https://rosaeg.no/erikro/WWW/corrgr/insurance/simply.pdf*** ***(accessed 02/03/2023)***. For example, *see* Eagle Ocean Marine: "About Us", ***https://www.eagleoceanmarine.com/about.php*** ***(accessed 02/03/2023)***.

[132] As recalled, clubs moved to offshore countries from the 1970s, and were thereafter authorised to conduct business in the UK by meeting the requirements under the *Insurance Companies Act 1974* (c. 49) and *Insurance Companies Act 1982* (c. 50). Afterwards, the *Financial Services and Markets Act 2000* (c. 8) with a broader scope, including insurance industry, was enacted, and the Insurance Companies Act 1982 was superseded in 2001 by the *Financial Services and Markets Act 2000 (Consequential Amendments and Repeals) Order 2001 (No. 3649)*, section 3(1)(b). Besides, the authorisation of insurance companies is similarly governed pursuant to the *Companies Act 2006* (c. 46), section 1165. Moreover, fundamental amendments were made by the *Financial Services Act 2012* (c. 21) and the *Financial Services Act 2021* (c. 22), the latter of which was a post-Brexit reform prepared to recalibrate the framework in the UK.

IV. ROLE AND FUNCTION OF THE “PAY TO BE PAID” RULE WITHIN THE CONTEXT OF THE DISTINCTIVE FEATURES OF P&I INSURANCE

A) THE “PAY TO BE PAID” RULE

1- The Condition Precedent

Private insurance, in terms of general insurance law, is basically classified into life and non-life insurance. The main, but not the sole, difference between the former and the latter is based upon the applicability of the indemnity principle to them. As to non-life insurance, it might cover, *inter alia*, the risks against the property, *e.g.*, vehicle, fire, marine cargo, or vessel, or the potential liabilities arising out of statutory or contractual obligations, *e.g.*, malpractice, automobile, or P&I insurance.

Generally speaking, in liability insurance, the insurer indemnifies the insured exposed to liability to a third party, thereupon the damaging act, regardless of the fact that the insured has previously compensated the third party who suffered damage or not. Likewise, provided that the third party is able to directly proceed against the insurer under law, then such party who suffered damages has the right to be indemnified by the insurer. In that case, the insurer cannot rely on the defence that the insured has not compensated the third party yet.

As regards the P&I insurance, on the contrary, there is this peculiar rule - the so-called “pay to be paid” or “payment first”, in accordance with which the member shall previously make the necessary payments he is, upon a judicial or arbitral decision or settlement, liable for in order to entitle to the right to recover. Only then, will the club indemnify its member. In other words, he will, only thereafter, be entitled to reimbursement from the club. It is the condition precedent for a member to entitle to be indemnified.[133] This rule is embodied under the provisions of the club rules similarly as follows:

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[133] Scowcroft, J. C.: “Protection and Indemnity Insurance - Pay to Be Paid Clauses - Third Party Claims - [British] Third Parties (Rights against Insurers) Act 1930”, ***Journal of Maritime Law and Commerce***,

"Unless the Directors in their discretion otherwise decide, it is a condition precedent of a Member's right to recover from the funds of the Association in respect of any liabilities, costs or expenses that he shall first have discharged or paid the same out of funds belonging to him unconditionally and not advanced expressly or impliedly for that purpose by way of loan or otherwise."[134]

Besides, one of the club rules explicitly state that the insurance is not provided with the aim of covering the liability of the member, but with the aim of indemnifying him only.[135]

From the above statements, a conclusion can be drawn that P&I might *prima facie* be considered to be traditional liability insurance in view of its shallow definition signifying the criterion of "the insurance covering the liabilities of shipowners". However, owing to this unique rule arising out of the notion of reimbursement, rather than liability guaranteeing, within the context of P&I, the "pay to be paid" rule is so peculiar in this field having regard to the fact that it characterises P&I and distinguishes it from ordinary liability policies in general insurance law.[136]

The unique "pay to be paid" rule might, however, give rise to notable difficulties in the eyes of third-party claimants who might remain out of pocket in the end. Details in this regard are set out below.

2- Conditions and Measure of Indemnity

It is also worth recalling that the indemnity principle is pivotal and applicable in terms of non-life insurance, *e.g.*, P&I insurance, which are the contracts of indemnity indicating that the person will be entitled to an indemnity in order to be reinstated if and only if, and

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1989, Vol. 20, Iss. 2, p. 205; Hodges, S.: Law of Marine Insurance, Cavendish Publishing, London 1996, p. 323; Acar, Kulüp Sigortası (P&I), 24; Hazelwood / Semark, 335, 341.

[134] Britannia, Rule 5(1); Shipowners, Rule 16; North, Rule 20(1); London, Rule 3; UK, Rule 5(A); Standard, Rule 6.15; Swedish, Rule 2, paragraph 3; Skuld, Rule 28.5.1; Gard, Rule 87; Japan, Rule 18.

[135] West, Rule 10.

[136] Scowcroft, 205; Ronneberg, 5, 14; Lemon, 1480; Tang, Y.: "A Study on the Principles of P&I Insurance", Master's Thesis, University of Oslo, 2007, p. 7, 35, 37; Hazelwood / Semark, 123-124, 335; Kimball, J. D.: "The Central Role of P&I Insurance in Maritime Law", ***Tulane Law Review***, 2013, Vol. 87, Iss. 5 & 6, p. 1147, 1149. *Confer* Pekşen, 20; Burucuoğlu, 28-29.

to the extent, he suffers loss. Provided that there is no loss, there will be no indemnity. This is the very basis of the indemnity principle.[137] Going a step further, the principle also indicates in itself that the insured "shall be fully indemnified, but shall never be more than fully indemnified",[138] *i.e.*, the person who suffers loss shall not profit therefrom.

Within the context of P&I insurance, for a member to entitle to indemnity, the following conditions must be satisfied:

(i) the ship shall be entered into the club;

(ii) the member shall be legally liable or shall made expenses because of the use or operation of the ship, which is the reflection of the indemnity principle;

(iii) the risks given rise to liability or expenses shall be within the scope of the club cover;

(iv) the events shall occur within the duration of the contract;

(v) the member must have fulfilled his duties theretofore; and

(vi) there shall not be any defence to be asserted by the club, foremost of which is the prominent "pay to be paid".[139]

That aside, there are limitations to the measure of indemnity. First of which is the "pay to be paid" rule where the club is only liable to the tune of the out-of-pocket payments made by the member, *i.e.*, the member will be able to be reimbursed to the extent of the payments he in fact made. The second limit is non-compliance with the instruction of clubs in case of handling claims where the club would be liable to the tune of the amount if the instructions were properly followed. Thirdly, in case the member lost his right to limit liability, the club would be liable as if he successfully limited his liability. Besides all these, there are aggregate amounts for some claims under international law.[140]

In addition, the duty to indemnify is due at the date of the payment made by the member to the claimant. Nevertheless, members are not entitled to any interest for the time

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[137] Hodges, S.: Law of Marine Insurance, Cavendish Publishing, London 1996, p. 1; Rose, 6-7; Birds, 4-5; Vaughan / Vaughan, 169.

[138] *Castellain v Preston* (1883) 11 QBD 380 at p. 386.

[139] Acar, Kulüp Sigortası (P&I), 398-404; Burucuoğlu, 42.

[140] Acar, Kulüp Sigortası (P&I), 413-418. For the limits under international law, *see infra*, Part V.B.1.

between the payment they made to the claimant and the indemnification by the club to them.[141] There is, of course, an interest acquired by the claimant which is attached to the principal credit in the relationship between the member and such claimant.

3- Doctrine of Subrogation in the Policy

a) Legal Doctrines Reinforcing the Indemnity Principle

The indemnity principle is reinforced by various legal doctrines. Otherwise, there is said to be an unjust enrichment on the part of the insured, occurrence of which is not desired, and it does not fit for the very purpose of such principle. These doctrines are *ut infra:*

(1) Insurable interest, in accordance with which the person who has a legal relation with the subject matter of insurance shall have interest in the subject matter not being damaged by marine risks. So much so that, the contracts without an insurable interest are void.[142]

(2) Prohibition of over insurance within the context of unvalued policies, in accordance with which the amount of the sum insured in excess of the insurance value is not paid.[143]

(3) Proportionate indemnification in case of under insurance, in accordance with which the ratio of the sum insured to insurance value, that is to say, the percentage underinsured, is multiplied by the partial damage, and the number payable is the product. It must be borne in mind that if there is total damage, the sum insured is directly paid then, *i.e.*, under insurance is important if there is partial damage.[144]

(4) Contribution in case of over insurance due to double insurance, where the insured suffering loss can choose against whom he will proceed, so the insurer making payment

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[141] Britannia, Rule 32(3); Shipowners, Rule 18(1); North, Rule 35(3); London, Rule 13.1.7; UK, Rule 5(T); West, Rule 13; Standard, Rule 6.14; Skuld, Rule 44; Gard, Rule 63(3); Japan, Rule 44.

[142] MIA 1906, sections 4 and 5.

[143] Over insurance is in question where the sum insured exceeds the insurance value, the exception of which is valued policies commonly used in marine insurance. In valued policies, *e.g.*, hull policies, the parties explicitly agree on a specific value at the time of the conclusion of the contract. In terms of P&I insurance, however, the measure of indemnity is the out-of-pocket payment of the insured. For detail, *see* MIA 1906, sections 27, 28, and 84(3)(e); Birds, 292-293; Vaughan / Vaughan 172, 591; Dunt, 365-369; Gürses, 83-84; Kayıhan / Günergök, 55-59.

[144] Under insurance is in question where the insurance value exceeds the sum insured. For detail, *see* MIA, section 81; Kayıhan / Günergök, 59-61.

will be entitled to demand a contribution from the other insurer or insurers since each one should make a payment proportionately. The aggregate number shall not exceed the loss itself in any respect.[145]

(5) Subrogation, a concept in question in trilateral legal transactions, in accordance with which the insurer indemnifies the insured pursuant to a legally valid insurance contract between them, and thereafter, the insurer, in a manner of speaking, “steps into the shoes” of the insured in terms of his rights against the third party but limited to the extent of the indemnification, which would otherwise have entitled the insured to indemnity twice.[146] The same logic is considered to be valid for third parties who “step into the shoes” of the insured against the insurer on the occasion of direct actions prescribed by law.

b) Subrogation in Terms of P&I Insurance

i. On the Part of Clubs

Subrogation within the context of P&I insurance is more limited because of the “pay to be paid” rule, and it is also twofold: The club’s or third parties’ right of subrogation. In terms of the former, theoretically, the club has to pay the insurance indemnity to its member in order to subrogate to his rights against the third party. That being the case, due to the “pay to be paid” rule in practice, the club is in a position that it does not need to indemnify its member unless the member himself compensates the third party before. Accordingly, there is no subrogation at all heretofore.

It is worth noting that the “pay to be paid” rule is not always strictly applied in practice. The club might discretionally choose to indemnify its member although its liability has not been established yet, but provided that there are indications of such liability to arise.

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[145] Double insurance is the insurance of the same subject matter against same risks during the same period for more than one time. For detail, *see* the MIA 1906, sections 32, 80, and 84(3)(f); Rose, 571, 579; Birds, 335-347; Dunt, 400-407; Kayıhan / Günergök, 68-70. *See also* Hazelwood / Semark, 222-226 for the double insurance in P&I. *Nota bene,* covers of P&I and H&M should not, but might, overlap.

[146] MIA 1906, section 79; Hodges, S.: Law of Marine Insurance, Cavendish Publishing, London 1996, p. 7-8; Rose, 519-520; Birds, 305; Gürses, 438-442; Kayıhan / Günergök, 70-80.

In such circumstance, the club will subrogate to the rights of its member against the third-party similar to insurance in general.

Other than that, where the member makes a payment in the amount of his liability, or the amount of his liability exceeds the payment he makes, the club will nevertheless be liable for the out-of-pocket payment made by the member. As a result, there is no subrogation from the point of the club yet again. If the liability, however, is under the payment that the member makes owing to the contributory fault of the third party or a miscalculation by the member, court, or arbitral tribunal, *i.e.*, if the member makes a payment more than he is liable for howsoever, then the club will be liable for the out-of-pocket payment again, but it will also subrogate to the rights of its member against the third party to the extent that the member is the creditor for the sum to whom the third party shall pay.[147]

From which it may be concluded that the club might entitle to subrogation where it discretionally or exceedingly indemnifies its member within the scope of P&I cover. Nonetheless, it is also worth adding that the discretionary payments which are not in the scope of P&I cover, that is to say, *ex gratia* payments under omnibus cover, do not grant the right of subrogation to the club on the ground that they are not legally enforceable.[148]

ii. On the Part of Third-Party Claimants

Before anything else, it must be noted that disputes in P&I insurance are threefold:

(i) disputes between the member and a third-party claimant on the basis of either contractual liability, *e.g.*, seafarers' claims, or tortious liability, *e.g.*, collision;
(ii) disputes between the club and its member based on the contractual relationship indicating the membership and insurance cover both; and
(iii) disputes between the club and a third-party claimant, that is to say, direct actions.

The last among these is the corollary to the right of subrogation of third parties as they "step into the shoes" of the insured, or more relevantly, the member of the club. Such

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[147] Hazelwood / Semark, 285-289, 341.
[148] Acar, Kulüp Sigortası (P&I), 434-435.

right of third-party claimants is pivotal, and therefore, will be focused on in this thesis. As a matter of fact, there is no contractual relationship between the club and a third party, *nota bene*, the law of contracts is based on the principle of privity of contract whereby the rights and duties are binding between the parties to a contract only. However, third-party claimants are able to directly sue clubs in terms of particular claims on the condition that the right of direct action is prescribed by law or arisen out of the contract.

The former, which was just cited above, or more exactly, the statutory subrogation, has been nothing more than a theoretical advantage until recently. As regards the latter, it is still not applied in practice due to the exclusion of the CRTPA 1999 under club rules. In sum, the situation from past to present, which is analysed just below, has given rise to problems on the part of third-party claimants.

4- Problems Arising out of Its Application

a) Establishment and the Ensuing Problems

At the dawn of P&I insurance, the notion behind the “pay to be paid” rule in the early mutual associations was the shipowners’ reliance on the financial statuses of each other and maintenance regarding the solvency for their payments and debts. In spite of the reorganisation of clubs as companies thenceforwards, the logical underpinning of the rule remained the same. Thus, clubs were in a situation where they were reimbursing their members, not guaranteeing their liability from which the members did not themselves exonerate in the first place.[149]

Afterwards, the TPA 1930 was enacted by which a statutory subrogation regime was introduced in favour of third parties, who were not a party to the contract of insurance, but suffered damage or loss by virtue of the damaging act of the insured. In other words, the TPA 1930, which was a remarkable change in support of the protection of the third-party claimants, applied to contracts of insurance where the insured was liable to third parties. In case the insured was insolvent, his rights under the insurance contract would

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[149] Hjalmarsson, J.: “Direct action against P&I clubs”, ***Insurance & Reinsurance Law Briefing***, 2008, Iss. 139, p. 1.

be transferred to the third party to whom the insured was liable, and the insurer would be liable to such third-party claimant. In a nutshell, it was accepted, by satisfying certain conditions, that third parties could directly sue the insurer.[150]

That being the case, this was not the major problem. As regards the practice of P&I back then, even though there was a subrogation regime under the TPA 1930, clubs were bringing the defence of non-payment forward to third parties on the ground of the "pay to be paid" rule. The rule was thereafter firmly established by a *locus classicus* verdict, *The "Fanti" and The "Padre Island"*,[151] in which it was held that the claimants did not have the right of direct action against the club because it would not be liable where the members did not make a payment first.[152]

In the following years, the reforming CRTPA 1999, a more general act compared to the TPA 1930, was enacted to grant third parties the right to enforce a term of a contract, to which they were non-parties, on the condition that the contract explicitly stated that they might do so, or unless the parties stipulate the otherwise, it implicitly conferred a benefit on them. Even then, however, contractual defences could be asserted against third parties. That aside, clubs have incorporated a provision under their rules and excluded its application since then. Therefore, the problems confronted continued to be unsolvable.[153]

In a nutshell, the "pay to be paid" rule precluded direct actions, which clubs did not wish to come up against, and it removed the statutory right of third parties, *i.e.*, as the third parties were granted the status of the member by statutory subrogation, clubs nevertheless

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[150] *Third Parties (Rights against Insurers) Act 1930* (c. 25), sections 1(1) and 1(4). *See also Third Parties (Rights against Insurers) Act 2010* (c. 10), section 1(3) ("TPA 2010"); Acar, Kulüp Sigortası (P&I), 490-502. Prior to filing a suit against the insurer directly, however, the third party had to make the insured become insolvent if the insured had not been insolvent by law yet, and then, the third party had to, regardless of before or after the insolvency, establish liability between him and the insured by the finalisation of a judgment or an arbitral award to that effect. Even then, third parties had only the right of subrogation, not compensation, *i.e.*, third parties could file a suit against the insurer to be compensated only then (multiple proceedings). This difficulty would later be dispelled by the TPA 2010 whereby the third party can file one suit for all of those steps (single proceeding).

[151] *The "Fanti" and The "Padre Island"* [1990] 2 Lloyd's Rep 191, HL.

[152] Hodges, S.: Cases and Materials on Marine Insurance Law, Cavendish Publishing, London 1999, p. 548-549; Acar, Kulüp Sigortası (P&I), 556-557; Hazelwood / Semark, 298-301.

[153] *Contracts (Rights of Third Parties) Act 1999* (c. 31), sections 1(1), 1(2), and 3. *See also* to that effect, Britannia, Rule 46(1); Shipowners, Rule 1(10)(C); North, Rule 3(2); UK, Rule (1)(8); West, Rule 10; Standard, Rule 1.6.

continued to rely on the contractual defence of non-payment which they could assert such defence to their members. From which it can be deduced that the theoretical advantages of the above-cited acts were inadequate, and they unfortunately failed to satisfy the needs.

b) Erosion Towards the 21th Century

The situation indicated above, however, was unfair. The ridiculousness was that in cases where the insured was insolvent, the third party wishing to be compensated had to make a payment to himself (!) in order to satisfy the condition of "pay to be paid", and achieve his ultimate purpose of being compensated.

That being the case, with the spark of compulsory insurance and direct action in the field of maritime law under some IMO conventions, there has accordingly been an erosion of the "pay to be paid" rule because this brand-new system has also prevented clubs from relying on that rule in direct actions. It might, thus, be remarked that the erosion of the rule over the recent decades has ameliorated its harshness with respect to not all, but specific claims. By means of this new system, third parties can directly sue the insurer, who cannot rely on the defence of "pay to be paid" or whatsoever, regardless of the insolvency of the insured member pursuant to the TPA 1930 and the TPA 2010. Which of the claims are falling within this scope will be analysed in detail later on.[154]

It is worth adding that the rule itself is not also strictly applied in practice where:

(i) the directors exercise their discretion otherwise, and the club indemnifies its member even though the liability thereof has not been established yet, but provided that there are indications of such liability to arise;
(ii) the club provides a letter of undertaking or equal thereto, if and in accordance with which the club puts itself into a position that it is liable to claimants, *nota bene* such guarantees are only acceptable to claimants;
(iii) the club settles with the claimants out of, not before, the court in case the verdict will be presumed to be to the detriment of its member;[155] or/and

[154] *See infra*, Part V.B.
[155] Hazelwood / Semark, 336.

(iv) the club compensates the third-party by the reason of a failure of its member in that respect, but only in terms of significant claims connected to public interest or fundamental rights such as death and injury. As a matter of fact, this is the club practice in terms of crew claims, the details of which will be set forth in the thesis below.[156]

c) The Current Situation

Third-party claimants, as a rule, cannot directly proceed against clubs by reason of the principle of *inter partes*, that is, the privity of contract prohibiting them to do so since they are non-parties to the contract of P&I insurance.

Despite the fact that the law might permit them in that regard, clubs still would be able to invoke the defence that its member was not discharged from his liabilities by making the payment himself yet. Therefore, third parties would have, in practice, been forced to sue the member, the outcome of which depends on the solvency thereof. On the other hand, clubs cannot easily become insolvent because of the strict conditions, under which they shall have and maintain financial capability, they found upon pursuant to the legislation of states and also because of the principle of mutuality which will be analysed in the part just hereinafter. Hence, clubs seem to be far better choices for claimants to proceed against.

From the foregoing dilemma, it is possible to observe that bringing a direct action where clubs cannot rely on the defence of "pay to be paid" will definitely be in favour of the claimants. In this regard, which of the claims are protected, and if so whether they are adequately protected or not, will be evaluated towards the end of this thesis after setting out their international, supranational, and national legal framework.[157]

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[156] *See infra*, Parts V.B.1.g and V.C.
[157] *See infra,* Parts V and VI.

B) PRINCIPLE OF MUTUALITY

1- Role and Function in the Policy

This principle is the basis of mutual insurance, denoting the cooperation of the members of an association, through which they recover the losses of each other for their mutual interests against common risks. Thus, the loss of any member is distributed among all.[158] Pursuant to section 85(1) of the MIA 1906:

> "Where two or more persons mutually agree to insure each other against marine losses there is said to be a mutual insurance."

As recalled, clubs once had a dual role where a member was an insured individual and an insurer together with all members. Section 85 reflected the prior status of clubs. Nevertheless, the mutual basis upon which the clubs were founded has slightly changed, and it brought discussions as to whether they are still operating based on mutuality or not. First of which were in terms of *locus standi*. Clubs lacked capacity, *i.e.*, they were not companies or equal thereto, which led them to sue and be sued by any member or person only altogether. Secondly, the increase in the number of members entailed difficulties in collecting calls, gathering the members, and suing all of them, but seeking reimbursement from each where all of whom were liable pro rata. In light of the foregoing problems, the principle of mutuality began to malfunction. Clubs, therefore, overcame the problem by incorporating themselves.[159] From the above discussion, it can summarily be drawn the conclusion that section 85 started to not exactly reflect the club practice anymore.

As of today, and as distinct from the situation in the past:

(i) the club provides indemnity, and it is the one exposed to liability, and therefore, it is the insurer, rather than members as a whole;
(ii) the members enter into transactions with the club, not with each other;
(iii) the plaintiff or defendant in cases heard is the club, not the members;

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[158] UNCTAD, Legal Documentary Aspects of the Marine Insurance Contract, 9 § 33; Ronneberg, 5.
[159] Acar, Kulüp Sigortası (P&I), 13, 29-30, 40-41.

(iv) the members exercise their rights via the club rather than exercising *inter se*, and also, they are liable to the club, not to each other; and

(v) there are separate insurance contracts on the part of each member instead of one contract between them.[160]

The above notwithstanding, clubs of today might still be considered to be functioning on the basis of mutuality although their structure is quite different from the one in the past. In this regard, they act for the benefit of the membership as a whole.[161] They do not aim to profit, and thus, members contribute to the claims for the common interest of all via non-fixed calls instead of commercial interest via fixed premiums.[162] Hence, incomes and outcomes should be equal, and in case of an imbalance, clubs might use surpluses in the following policy year, build up various funds from such surpluses, or collect supplementary calls. In addition, members have mutual duties, share the risks with each other, and have an interest as to whom should be accepted to the club and how they should conduct business. In short, the success of the club is crucial for all members. Furthermore, they might provide letters of undertaking in exchange for no charge. Most importantly, clubs themselves state that they are functioning based on mutuality,[163] and IG P&I considers its members as mutual organisations.[164] The discretion of clubs, including the omnibus rule by which they make *ex gratia* payments for the claims not within the scope of cover, is also a good indicator of the priority of clubs is to protect their members.

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[160] Acar, Kulüp Sigortası (P&I), 30; Hazelwood / Semark, 9, 63.

[161] Coghlin, 595; Tilley, The Origin and Development, 269; Hazelwood / Semark, 24.

[162] *See* MIA 1906, section 85(2).

[163] Britannia P&I: "Group Profile", https://britanniapandi.com/about/group-profile/ ***(accessed 28/02/2023)***; Shipowners' Club: "About us", https://www.shipownersclub.com/about-us/ ***(accessed 28/02/2023)***; The London P&I Club: "Mission Statement", https://www.londonpandi.com/about-us/mission-values/ ***(accessed 28/02/2023)***; UK P&I: "About us", https://www.ukpandi.com/about-us/ ***(accessed 28/02/2023)***; West: "Governance", https://www.westpandi.com/about-us/governance/ ***(accessed 28/02/2023)***; Standard: "About", https://www.standard-club.com/about/ ***(accessed 02/03/2023)***; The Swedish Club: "Our Core Values", https://www.swedishclub.com/about/our-background/our-core-values/ ***(accessed 02/03/2023)***; The American Club: "About the Club", https://www.american-club.com/page/about-the-club ***(accessed 02/03/2023)***; China P&I: "About Club", https://www.chinapandi.com/index.php/en/about-us/about-club-en ***(accessed 02/03/2023)***.

[164] International Group Agreement as amended on 10.03.2020, Introductory Text § 1, https://static.mycoracle.com/igpi_website/media/adminfiles/International_Group_Agreement_2020.pdf ***(accessed 03/03/2023)***; IG P&I: "About the International Group", https://www.igpandi.org/about ***(accessed 02/03/2023)***.

2- Significance on the Part of Third-Party Claimants

It is scarcely possible for a club to become insolvent having regard to the foregoing remarkable advantages of mutuality in itself except that all of the shipowners, or even a few of them in case of a fleet entry, run out of money. It is, however, practically difficult although most clubs virtually provide unlimited cover.

That being so, clubs not availing themselves of the pooling arrangement and reinsurance system of the IG P&I refrain from providing unlimited cover since they might fall into financial difficulties easier than the IG P&I members, particularly if they have problems with their reinsurers. Over and above this, the balance regarding to what extent the clubs admit special entries based on fixed premiums is crucial because, if needed, the clubs will not be able to collect supplementary or overspill calls from those fixed-premium based entrants. A good example of these problems was the bankruptcy of *The Oceanus*.[165] Furthermore, it is also easier for a club to encounter insolvency if it chooses most of its members from one-ship companies, the assets of which are limited to the ship itself at the sea and facing numerous risks. Members with limited assets might also lead to default in respect of payment of calls, or even worse, such calls might never be collected. Looking on the bright side, these are exceptions to the well-functioning system of mutuality.

From the foregoing advantages of mutuality, thanks to which it is practically impossible for a club to become insolvent, it is possible to observe that clubs are definitely more reliable choices for third parties to proceed against. Because, clubs found upon satisfying their sustainable financial capabilities, and they function on the basis of mutuality *vis-à-vis* the shipowners who are not insurers but usually just companies conducting business in shipping with commercial reasons, and thus, aim to profit unlike clubs. Therefore, in the ordinary course of business, shipowners might also lose money, or even worse, they might go bankrupt. As a result, proceeding against clubs seems to be a better choice for third parties.

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[165] Tilley, M.: "The Protection and Indemnity Clubs and Bankruptcy", ***Journal of Maritime Law and Commerce***, 1986, Vol. 17, Iss. 4, p. 531-538; Acar, Kulüp Sigortası (P&I), 45; Hazelwood / Semark, 69.

C) NON-PROFIT-MAKING BASE

As distinct from traditional insurance companies, clubs carry out activities for the mutual benefit of members, not for commercial profit, *i.e.*, they are companies limited by guarantee with neither shareholders nor share capital. Hence, incomes and outcomes, that is, the investment incomes plus calls should be equal to the expenses plus claims. If the incomes outweigh, there will be surpluses that will be used in the next policy year or to build up various funds. If the outcomes outweigh, there will be a deficit that will be closed by collecting supplementary calls or flowing of funds built up theretofore.[166] This feature of P&I is another reflection of the principle analysed above, the mutuality.

Given the fact that the ship is the most important, or in case of one-ship companies the only, capital of the member, the arrest of the ship causes a loss of earning each and every day. Clubs, therefore and particularly for the release of the arrested ships, provide financial security in exchange for no charge, but in accordance with strict conditions,[167] the aim behind of which is to prevent abuses of this service.

Clubs provide financial securities to their members, either in advance of the arising of a claim called the anticipatory guarantee (remarkable examples of which are the blue cards attesting that the financial security under IMO conventions is in place and the Maritime Labour Certificate attesting that the financial security for seafarers' claims is in place[168]), or subsequent to the arising of a claim in the shape of letters of undertaking in exchange for no charge, especially when their members' ships are arrested and members need financial security. The most common guarantee for the release of ships, in practice, is the

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[166] Acar, Kulüp Sigortası (P&I), 279-280; Hazelwood / Semark, 98, 101-102.

[167] The conditions are as follows: (1) The discretion of the club shall be exercised in that respect, *i.e.*, providing financial security is not a duty of the club (*See* to that effect, *Gregory Maritime, Ltd. v. Thomas Miller & Son, United Kingdom Mutual Steamship Assurance Association, Ltd., and United Kingdom Freight, Demurrage and Defence Associaion, Ltd.* [1966] 1 Llyod's Rep 299; *The Zuhal K and Selin* [1987] 1 Llyod's Rep 155). (2) The arrested ship must have entered into the club when the casualty occurs. (3) The arrest shall be within the scope and duration of the club cover. (4) The member must have fulfilled his duties properly and in time. (5) The member shall provide counter-security in case of a demand by the club in that regard. For detail, *see* Acar, Kulüp Sigortası (P&I), 376-380; Hazelwood / Semark, 255-259.

[168] Blue cards and Maritime Labour Certificate are the indicators of the requirements for compulsory insurance or financial security under related conventions being satisfied. For detail, *see infra*, Parts V.A.1 and V.B. *See also* Hazelwood / Semark, 254-255.

letters of undertaking since they are fast and free of charge. Banks or other insurers, on the contrary, do it for profit.[169] This type of security is prevalent in the shipping world.[170] Members shall comply with the terms of the letters of undertaking, a breach of which exonerates the club from liability.[171] That aside, there is no hurdle for members to utilise letters of guarantee issued by banks or bail bonds issued by other traditional companies, or the members themselves might store cash in the court.

What is particularly important is that there is no implied indication that a club is bound by any duty to pay indemnity ultimately even if it provides any type of security, which is also not a duty of the club.[172] It must therefore be underlined that the defence of "pay to be paid" is retained, or technically speaking, it is not waived. In other words, even though the club chooses to provide any security, it can still rely on the "pay to be paid" when faced with a claim, whether from its member or a claimant, unless such rule is not strictly applied in practice as indicated above in this thesis[173] or is waived with regard to certain claims under international or national laws, the details of which are set forth below.[174]

D) CLAIMS HANDLING

It is clear that claims handling is a highly significant service rendered by clubs. It is a process of crisis management as fast and as cheap as possible from the occurrence of an event resulting in the liability until the discharge therefrom, the good management of which is both in favour of the club and its members, without a doubt.

In this regard, clubs have a unique and global network of correspondents as the "eyes and ears" of them worldwide. It is worth recalling that, as a rule, settlement of claims is exercised by directors, whereas claims handling is exercised by managers via a global

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[169] Acar, Kulüp Sigortası (P&I), 380-383; Hazelwood / Semark, 247-248. For detail concerning the differences between letter of indemnity, letter of undertaking, and bank letter of guarantee *see* Gard: "LOI, LOU and BLG – Confused?", ***https://www.gard.no/Content/503153/No%2001-10%20LOI%20LOU%20and%20BLG%20-%20Confused.pdf*** ***(accessed 10/03/2023)***.

[170] Tetley, W.: "Arrest, Attachment, and Related Maritime Law Procedures", ***Tulane Law Review***, 1999, Vol. 73, Iss. 5 & 6, p. 1895, 1914, 1925, 1937, 1946; Hazelwood / Semark, 247-248.

[171] Acar, Kulüp Sigortası (P&I), 394.

[172] Hazelwood / Semark, 259, 336.

[173] *See supra,* Part IV.A.4.b.

[174] *See infra,* Part V.B.

network of correspondents. Neither managers nor correspondents have the authority to bind the club by approving or disapproving the settlements although their advice might be asked in that regard.[175]

Claims handling consists of taking measures to minimise the loss, gathering and preserving evidence, appointing surveyors and experts, acting as a law firm (*e.g.*, appointing attorneys, filing suits, informing and advising its members in respect of the latest updates in law and practice via circulars), supporting members by means of correspondents at every stage of the incident causing claims, and providing any other technical or legal support. It must not be forgotten that members are often strange to the language, law, or authorities of the country in which the incident takes place, whereas the claimants, in a manner of speaking, have the advantage of a host, *e.g.*, they can arrest the ship easier than members.[176] The club generally supervises its member in practice. In any case, members have to notify the club and follow the instructions thereof.

What is particularly important, and must be absolutely borne in mind, is that handling of claims by the club, which is not a duty thereof, does not implicitly mean that the club will be bound by any obligation to pay indemnity. Nonetheless, provided that the club renders such service, it will be bound by the duty of care to its members.[177] It can also be observed that “pay to be paid” is retained, or more technically, not waived herein as well. From which it can be concluded that even though the club carries out this process, there is no hurdle for it to rely on the “pay to be paid” when faced with a claim for indemnification with the same exceptions pointed out in the previous section.

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[175] Ronneberg, 27-28; Hazelwood / Semark, 229-230. *See also supra,* Parts III.B.1.b. and III.B.1.c.
[176] Acar, Kulüp Sigortası (P&I), 373-376; Hazelwood / Semark, 229, 231-232, 241.
[177] Hazelwood / Semark, 229-231.

V. SIGNIFICANCE OF COMPULSORY INSURANCE AND DIRECT ACTION AND THE IMPACTS OF THE "PAY TO BE PAID" RULE THEREON

A) THREE-TIERED PROTECTION

1- Compulsory Insurance

The very first step of the protection of third-party claimants is to oblige insurance cover in order to secure the pecuniary resources of insurers, or *ad rem*, clubs. In spite of the fact that insurance cover, in principle, is not compulsory for those who seek to avail of it, insurance, particularly marine insurance, is voluntarily purchased by prudent merchants in the ordinary course of their maritime businesses by virtue of high and numerous risks included and a significant amount of investment made therein.[178]

The spark in this regard was the very well-known incident of *The Torrey Canyon*, which was grounded on the coast of the UK in 1967. The contamination was so much worse than it had ever been seen before. The incident highlighted the requirement for a compensation regime. Thus, compulsory insurance made its debut[179] in maritime law with the adoption of the *International Convention on Civil Liability for Oil Pollution Damage* in 1969, which was followed by a series of others adopted by IMO.[180]

The compulsory insurance under these conventions is not only provided by P&I clubs, but also any type of security such as a guarantee by a bank is also sufficient in this regard, in so far as the conditions of the conventions are satisfied. Otherwise, any convention directly mentioning P&I insurance under its provisions would not be so different from the monopolisation era created by the *Bubble Act 1720*. Moreover, amending conventions will not be easy if clubs declare that they will not provide cover. Hence, in practice,

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[178] Røsæg, 2-4, 9.

[179] *Confer Convention on the Liability of Operators of Nuclear Ships,* Brussels, 25.05.1962, 57 AJIL 268, article III which was governing insurance to be compulsorily maintained by the operators of nuclear facilities, not by shipowners. Therefore, compulsory insurance in its true sense was deemed to be introduced in 1969. For detail, *see* Røsæg, 1.

[180] Hazelwood / Semark, 394; Zhu, L.: "Probing Compulsory Insurance For Maritime Liability", ***Journal of Maritime Law & Commerce***, 2014, Vol. 45, Iss. 1, p. 63, 66-70; International Maritime Organization (IMO): "Brief History of IMO", ***https://www.imo.org/en/About/HistoryOfIMO/Pages/Default.aspx*** ***(accessed 03/04/2023)***.

compulsory insurance is provided by clubs considering their unrivalled position in the business. In the enforcement of conventions, clubs issue blue cards to members for them to prove that they have insurance or any similar financial security in force, and thereafter, the members are able to receive insurance certificates issued by governmental authorities to submit, when necessary, *e.g.*, during port state controls. These certificates shall be carried on board. Otherwise, the ship may not be allowed to trade.[181]

That being the case, the notion of compulsory insurance has evolved in the last half-century, in particular, in the fields of maritime law. The underlying rationale of which is to satisfy public interest and protect third-party claimants for specific claims against the risk of non-compensation, especially if the insured is insolvent. As a reminder, due to mutuality and financial strength of clubs, proceeding against them is a far better choice than proceeding against the insured member.

Compulsory insurance will not be as functional as intended in the absence of a right of direct action granted to claimants enabling them to sue an insurer who is deemed to be financially strong. Thus, the problem might be overcome. Or is it indeed?

2- Direct Action

It is worth recalling that, as a rule, only the party privy to the contract can enforce its terms because of the doctrine of "privity of contract". In this regard, it must be stated that there is an absence of a contractual relationship between third-party claimants and clubs. For that very reason, the reliance on the solvency of clubs amounts to nothing, so to say, in practical reality unless third parties are somehow involved in the process.

The harshness of which, as already mentioned hereinbefore, was ameliorated by the CRTPA 1999. That being so, it did not have an application in the practice of P&I because of the exclusion of that Act by club rules. Third parties, who sought compensation, remained remediless again. Thus, it was considered that the second step in protecting those claimants was to grant them the right to directly proceed against the clubs by law.

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[181] Hazelwood / Semark, 255, 393-394; Zhu, 69-71.

As of now, in terms of particular claims, third parties are able to directly sue the clubs provided that such right is prescribed by law. From which it can be concluded that it is the enforcement of, but not a corollary nor adherence to, the regime of compulsory insurance, because third parties could have sued clubs in the absence of compulsory insurance as long as they had the right of direct action. Compulsory insurance is more of a security for third parties when taking into consideration that clubs are forced to maintain their funds accordingly.

3- Waiver of "Pay to Be Paid"

Generally, defence is a response pleaded by the defendant *vis-à-vis* the assertions of the plaintiff in a legal case with the aim of refuting such assertions. As to P&I insurance, clubs might rely on the policy defences, which could have been relied against the member according to their contractual relationship, against third-party claimants in direct actions wherein such claimants statutorily "step into the shoes", that is, subrogated to, and therefore becomes the successor of, the rights of such member.

The notable defences that can be asserted by clubs against third parties are, *inter alia*, the non-compliance with warranties including non-payment of calls and unseaworthiness, the application to arbitration before litigation,[182] non-liability or the limitation of liability of the insured,[183] the wilful misconduct thereof, the expiration of statute of limitation, and the non-fulfilment of discharge of liability in advance of seeking reimbursement, or more clearly, the one and only "pay to be paid".[184]

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[182] The member shall initially apply to the Board of Directors. Provided that the member is not satisfied with the decision, he might apply to arbitration which is also the condition precedent of litigation. This rule is known as the "*Scott v Avery* Clause". In this regard, clubs might allege the third party to apply to directors, arbitration, and court in that order. For detail, *see Scott v Avery* (1856) 10 ER 1121 - 5 HL Cas 811; *Arbitration Act 1996* (c. 23), section 9; Ronneberg, 13-14; Acar, Kulüp Sigortası (P&I), 453-456, 483-484, 549-551; Lin, 34-37; Hazelwood / Semark, 343-348; Burucuoğlu, 49-50.

[183] Pursuant to the regime under *Convention on Limitation of Liability for Maritime Claims* ("LLMC") or other conventional regimes, club might limit its liability to the extent that the shipowner would have limited his liability, or it might be liable to the extent that the shipowner would have been liable if he had successfully limited his liability. *See* to that effect, Britannia, Rule 27(1); Shipowners, Rule 22; North, Rule 22(1); UK, Rule 5(B)(i); West, Rule 8(1); Swedish, Rule 2, paragraph 5; Skuld, Rule 32.1; American, Rule 1, section 4.33 to 4.39; Japan, Rule 37(1).

[184] Acar, Kulüp Sigortası (P&I), 543-575; Hazelwood / Semark, 295-298.

As previously discussed, this cited rule has been the fundamental basis of P&I insurance, which it is peculiar to. What is also particularly important in terms of the subject matter is that, thanks to direct action, when the claimants statutorily subrogate the rights of the member, clubs might rely on the defence of "pay to be paid". As a result, direct action will not be functional and third parties will not be compensated in the absence of a solution in this regard.

The third step, and possibly the most important of all so far, is the exclusion of the reliance on the defence of "pay to be paid" against the claimants. Within the legal framework that will be analysed just below, the emergence and evolution of compulsory insurance and direct action which led the clubs to not be able to rely on the defence of "pay to be paid" against claimants anymore should be perceived as the ideal solution that hits the mark. In the absence of this step, however, all of the above-mentioned tiers will collapse to the detriment of third parties. In this regard, the critical question should be as follows: Which of the third-party claims can be protected in this way and to what extent?

B) LEGAL FRAMEWORK

1- Under International Law

a) CLC 1992, FUND 1992, and the Protocol of 2003

The Convention of 1969[185] was adopted to govern the liability of shipowners responsible for oil pollution damages causing significant environmental and costly problems. Following the adoption of two protocols thereto, it has become to be known as the *International Convention on Civil Liability for Oil Pollution Damage* today ("CLC 1992" for the consolidated text).[186]

CLC 1992 exclusively applies to pollution damages in the territory or in the exclusive economic zone or, in the absence thereof, in the waters 200 nautical miles adjacent to the

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[185] *International Convention on Civil Liability for Oil Pollution Damage, 1969*, Brussels, 29.11.1969, 973 UNTS 3.

[186] *Protocol of 1976 to the International Convention on Civil Liability for Oil Pollution Damage, 1969*, London, 19.11.1976; *Protocol of 1992 to amend the International Convention on Civil Liability for Oil Pollution Damage, 1969*, London, 27.11.1992, 1956 UNTS 255 ("CLC 1992" for the consolidated text).

territorial waters, of the coastal State Party, and preventive measures, regardless of the maritime area, for minimising or preventing pollution damage.[187]

The convention imposes, not fault-based, but strict liability on the shipowner if the ship causes pollution damage. From which it is concluded that, third-party claimants do not need to prove the fault of the owner.[188] Besides, the liability is joint and several where at least two ships are involved in an incident.[189] It enables the claimants to choose from one of those owners, or their clubs as will be addressed below, against whom to proceed for compensation. It would not be wrong to say that those provisions are in favour of third parties for sure; however, they are not sufficient by themselves.

More importantly, the convention, therefore, obliges the shipowner "carrying more than 2,000 tons of oil in bulk as cargo" to obtain insurance or any financial security for his liability under the convention up to the limits set out thereunder, and it enables the claimants to sue the insurer directly for the liability of the shipowner. *Nota bene*, if they choose to proceed against the club, it does not purport that they waive their right to bring the shipowner member into the legal proceedings. Last but not least, in order to protect them, the CLC 1992 also negates, among other defences save for wilful misconduct, the defence of "pay to be paid" to preclude clubs from relying on such defence.[190] From which it is possible to observe that provisions regarding the strict and joint liability are reinforced by this system, in accordance with which the unique rule of P&I is waived for such claims.

It is noteworthy that the shipowner, both in terms of liability and insurance perspective, stands for the registered owner or, in the absence thereof, the one owning the vessel.[191] What is important in terms of that is the claimants cannot directly sue clubs for the liability of persons other than owners even such persons are somehow covered under P&I.

187 CLC 1992, articles I/6, I/7, and II.
188 CLC 1992, article III.
189 CLC 1992, article IV.
190 CLC 1992, articles VII/1 and VII/8.
191 CLC 1992, article I/3.

The liability, however, is not unlimited. CLC 1992 enables the shipowner to limit his liability to a certain amount, but not exceeding Special Drawing Right ("SDR") 89.7m, to the tune of which such owner and its club will be liable.[192] Even if their members are liable since they lose their right to limit liability, clubs will in no case be liable, neither to their members nor to third parties, for a sum exceeding that limit.

In parallel with the evolution of the CLC 1992 regime, another convention was adopted to establish a fund with the aim of providing compensation for pollution damage suffered by persons who could not obtain adequate and full compensation from shipowners under the regime of the aforesaid Convention of 1969. Two protocols to that convention were mainly adopted in order to increase the limits in 1976 and 1992.[193] At last, the *International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage* ("FUND 1992" for the consolidated text) limited the compensation payable by the fund exceeding the limits for which the shipowner was liable.[194]

Upon the disasters of *The Nakhodka*, *The Erika*, and *The Prestige*, a third tier was added to the regime under the Supplementary Protocol of 2003 to the FUND 1992.[195] At long last, the limits have taken their final form as in the figure *ut infra:*

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[192] CLC 1992, article V.

[193] *International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1971*, Brussels, 18.12.1971, 1110 UNTS 57; *Protocol to the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1971*, London, 19.11.1976, 1862 UNTS 509; *Protocol of 1992 to amend the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1971*, London, 27.11.1992 ("FUND 1992" for the consolidated text). *See*, FUND 1992, articles 2 and 4/1.

[194] FUND 1992, article 4/4.

[195] *Protocol of 2003 to the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1992*, London, 16.05.2003, article 4 ("Supplementary Fund Protocol"); Hazelwood / Semark, 394-395.

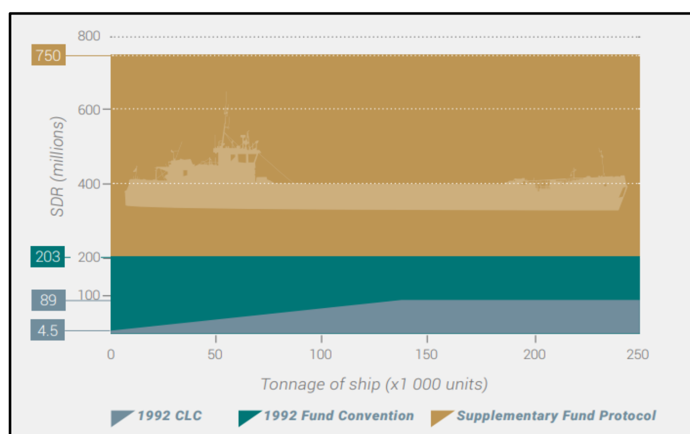

Figure 1: Upper limits under the regimes of CLC 1992, FUND 1992, and 2003 Protocol *Source:* IOPC: Claims Manual, 2019, p. 12-13, ***https://iopcfunds.org/wp-content/uploads/2018/12/2019-Claims-Manual_e-1.pdf*** ***(accessed 28/03/2023)***.

In order for this system to properly function – having regard to the fact that contributions to fund are made by cargo receivers, or more exactly, the oil industry – total quantities of oil and the list of physical receivers shall regularly be reported by State Parties.[196]

Furthermore, two voluntary agreements, namely the *Small Tanker Oil Pollution Indemnification Agreement* ("STOPIA") and the *Tanker Oil Pollution Indemnification Agreement* ("TOPIA"), were drafted in 2006 in order to lighten the burden laid on the petroleum industry imposed by the Protocol of 2003. STOPIA increases the compensation limits of small tanker owners. Besides, TOPIA prescribes tanker owners to make a payment for the half of compensation to share the burden of supplementary fund.[197] It is also worth bearing in mind that these agreements only apply where the FUND 1992 and the Protocol of 2003 are in force.

From the foregoing aspects and the provision governing insurance and direct action under the CLC 1992, it can be deduced that insurance and direct-action provisions apply only to the first tier of liability up to SDR 89.7m under the CLC 1992. However, they neither apply to second tier nor to the third one although the shipowners might make a payment

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[196] FUND 1992, articles 10 *et seq*; Supplementary Fund Protocol, articles 10 *et seq.*

[197] Hazelwood / Semark, 395. For STOPIA & TOPIA 2006 (as amended 2017), *see* IOPC: STOPIA and TOPIA, ***https://iopcfunds.org/about-us/legal-framework/stopia-and-topia/*** ***(accessed 04/04/2023)***.

from their pockets as they contribute to the supplementary fund by means of TOPIA. It must therefore be noted that, because of that third tier where shipowners might make a payment, clubs provide cover to them up to USD 1bn,[198] which is the current reinsurance limit of IG P&I,[199] for oil pollution claims. That being so, clubs can also rely on the "pay to be paid" even if third parties claim for a sum exceeding the first tier in direct actions.

b) BUNKERS 2001

Besides the success of CLC and FUND regimes, these conventions were drafted to apply to ships built or adapted with the aim of carrying oil in bulk as cargo, that is to say, oil tankers.[200] They were not, however, consisting of the spillage of bunker oil from a non-tanker ship, *e.g.*, container ships. The sinking of *The Treasure* in 2000 led the coasts of South Africa to be polluted by bunker oil and African penguins to be oiled. It revealed the need for a regulation in that regard.[201] The *International Convention on Civil Liability for Bunker Oil Pollution Damage, 2001* ("BUNKERS 2001") was adopted to govern the liability of shipowners regarding the leakage of, and pollution resulting from, bunker oil that is used to operate or propel the ship. It exclusively applies to pollution damages and preventive measures in the same maritime areas as it is under the CLC 1992.[202]

BUNKERS 2001 also imposes strict liability on the shipowner if the ship causes pollution damage due to any bunker oil.[203] The liability is also joint and several where at least two ships are involved in an incident.[204] The advantages but also the insufficiency of those provisions by themselves are identical to the ones mentioned for the CLC 1992 above.

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[198] Shipowners, Rule 21A; North, Rule 22(3); London, Rule 11.3; UK, Rule 5(B)(ii); West, Rule 7(3); Standard, Rule 6.5; Steamship, Rule 18(ii); Swedish, Rule 6, section 2; Skuld, Rule 14.3 and Appendix 5; Gard, Rule 53.1 and Appendix III; American, Rule 1, section 4.35; Japan, Special Clauses, Oil Pollution Liability Limitation Clause.

[199] IG P&I: "2023/24 Pool and GXL Reinsurance contract structure", ***https://www.igpandi.org/reinsurance/*** ***(accessed 01/03/2023)***.

[200] CLC 1992, articles I/1 and I/5; FUND 1992, article 1/2.

[201] Hazelwood / Semark, 401; International Bird Rescue: "2000 – Treasure Spill – South Africa", 30.06.2000, ***https://www.birdrescue.org/2000-treasure-spill-south-africa-2/*** ***(accessed 04/04/2023)***.

[202] *International Convention on Civil Liability for Bunker Oil Pollution Damage, 2001,* London, 23.03.2001, articles 1/7, 1/9, and 2 ("BUNKERS 2001").

[203] BUNKERS 2001, article 3.

[204] BUNKERS 2001, article 5.

What is therefore prescribed by this convention is that BUNKERS 2001 too obliges the registered owner to obtain insurance or any security for his liability under the convention if the ship is above 1000 gross tons, and it enables the claimants to sue the insurer directly. It is noteworthy that proceeding against the club does not purport that third parties waive their right to bring the shipowner member into the legal proceedings. Most of all, similar to the CLC 1992, it precludes clubs from relying on the defence of "pay to be paid" or any other but wilful misconduct.[205] Hence, strict and joint liability are reinforced.

Putting aside these similarities, the CLC 1992 is not subject to the limitation regime under the *Convention on Limitation of Liability for Maritime Claims* ("LLMC 1996" for the consolidated text, as amended in 2012),[206] *i.e.*, it has its own limitation regime; whereas the liability under the BUNKERS 2001 is limited according to the LLMC 1996,[207] and neither shipowners nor clubs will be liable for the excess of the limits set out thereunder against third-party claimants unless shipowners lose their right to limit liability. Even then, clubs would be liable only to the extent that shipowners successfully limit their liability. It is also noteworthy that, since there is no fund similar to the CLC/FUND regime, the liability under the BUNKERS 2001 is laid only on the shipowner.

It is also worth bearing in mind that, unlike the CLC 1992, "shipowner" has a broader meaning, including the manager, operator, and bareboat charterer, in terms of liability. However, the person, on who the obligation of compulsory insurance is imposed and with which the direct action is correlated, stands for the registered owner only.[208] From which it can be concluded again that the claimants can directly sue clubs for the liability of the registered owner even if the others are liable under the convention or covered under P&I.

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205 BUNKERS 2001, articles 7/1 and 7/10.

206 *Convention on Limitation of Liability for Maritime Claims, 1976*, London, 19.11.1976, 1456 UNTS 221; *Protocol of 1996 to amend the Convention on Limitation of Liability for Maritime Claims, 1976*, London, 02.05.1996 ("LLMC 1996" for the consolidated text). *See* LLMC 1996, articles 2 and 3. Limits were increased by IMO. *See* to that effect, *2012 Amendments to the Protocol of 1996 to Amend the Convention on Limitation of Liability for Maritime Claims, 1976*, IMO Resolution LEG.5(99), adopted on 12.04.2012, ***https://wwwcdn.imo.org/localresources/en/KnowledgeCentre/IndexofIMOResolutions/LEGDocuments/LEG.5(99).pdf*** ***(accessed 30/03/2023)***.

207 BUNKERS 2001, article 6.

208 BUNKERS 2001, articles 1/3, 3, and 7/1. *Confer* CLC 1992, article I/3; FUND 1992, article 1/2.

c) WRC 2007

What makes removal of wrecks crucial is because their presence might jeopardise, *inter alia*, navigational safety (*e.g.*, the manoeuvres of ships at the time of approaching and leaving ports), marine environment by negatively changing the habitats of marine animals and accordingly impeding the fishing and tourism sectors, diving or sports activities, or any other related coastal state interests. Besides that, it is a costly business to do because of the technical difficulties therein.[209]

The *Nairobi International Convention on the Removal of Wrecks, 2007* ("WRC 2007") was adopted to govern the liability of shipowners regarding the costs of marking, locating, and removing the wrecks, in so far as the liability under it is not in conflict with the CLC 1992, BUNKERS 2001, and HNS 2010.[210]

The remarkable difference between those conventions and the WRC 2007 is the scope of application. WRC 2007 only applies to wrecks in an exclusive economic zone or, in the absence thereof, in the waters 200 nautical miles adjacent to the territorial waters of a state. What is particularly important regarding this convention is that states might extend the area of application to their territories only by an "opt-in" clause pursuant to the convention.[211] From which it can be observed that the provisions in terms of liability and insurance as well as the direct action and waiver of policy defences shall apply to wreck claims within those opted-in maritime areas only then. Most of the wrecks occur in such narrow and crowded areas where there is too much maritime traffic, and therefore, opt-in will definitely be in favour of the claimants, by means of which they can directly proceed against the clubs without hitting the brick wall of "pay to be paid", so to speak.

The liability is not fault-based but strict liability herein as well. The shipowner might limit his liability under the LLMC 1996 with reference to the WRC 2007, because it does not

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[209] *Nairobi International Convention on the Removal of Wrecks, 2007*, Nairobi, 18.05.2007, 46 ILM 694, article 1/6 ("WRC 2007"); Demir, İ.: Nairobi Sözleşmesi Çerçevesinde Enkaz Kaldırma, Yetkin Yayınları, Ankara 2013, p. 26-30, 244.

[210] WRC 2007, articles 7, 8, 9, 10, and 11.

[211] WRC 2007, articles 1/1 and 3.

have its own limitation regime.[212] Clubs, again, will in no case be liable, neither to members nor to claimants, for a sum exceeding the liability limits set out under law.

More importantly, it obliges the shipowner to obtain insurance or any financial security for his liability under the convention provided that the ship is at least 300 gross tons. Besides that, it grants the right of direct action to claimants to sue the insurer directly. Similarly, such right does not purport that they waive their right to bring the shipowner into the legal proceedings, and clubs cannot avail themselves of the defence of "pay to be paid" or any other defence whatsoever except for, similar to other IMO conventions as you may appreciate, wilful misconduct.[213] Strict liability is reinforced by means of those provisions. Lastly, liability as well as insurance obligation and its correlation with direct action are channelled onto the registered or actual owner.

d) HNS 2010

The *International Convention on Liability and Compensation for Damage in Connection with the Carriage of Hazardous and Noxious Substances by Sea* ("HNS 2010" for the consolidated text), which was firstly adopted in 1996 and amended in 2010, governs the liability of shipowners regarding damages resulting from, *inter alia*, dangerous and noxious liquid substances or liquefied gases.[214]

It applies to damages in the same maritime areas as under the CLC 1992 examined above with a slight difference. If the damage is related to environmental pollution, there will be no difference; however, if the damage is related to any damage other than that such as death or injury resulting from a carriage under the HNS 2010, it will apply to any maritime area on the condition that the ship causing such damage is registered or, in the absence of registration, is entitled to fly any Contracting State's flag.[215]

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[212] WRC 2007, article 10.
[213] WRC 2007, articles 12/1 and 12/10.
[214] *International Convention on Liability and Compensation for Damage in Connection with the Carriage of Hazardous and Noxious Substances by Sea, 1996*, London, 03.05.1996, 35 ILM 1415; *Protocol of 2010 to the International Convention on Liability and Compensation for Damage in Connection with the Carriage of Hazardous and Noxious Substances by Sea, 1996*, London, 30.04.2010 ("HNS 2010" for the consolidated text). *See* HNS 2010, articles 1/5 and 1/6.
[215] HNS 2010, articles 1/6 and 3.

It imposes strict liability on the shipowner if there is damage by those substances above, and the liability is joint and several if at least two ships are involved.[216] In case of the former, third parties do not need to prove the shipowner's fault, and in case of the latter, they might choose the owner against whom they will proceed.

What is particularly important again is that the HNS 2010 obliges the shipowner to obtain insurance or any financial security for his liability; it also, enables the claimants to sue the insurer directly. Provided that the claimants choose to do so, they might nevertheless claim the shipowner as a defendant as well. Most of all, the HNS 2010 likewise precludes clubs from relying on the "pay to be paid" or any other defence; however, as it is under all IMO conventions examined so far, they can rely on the defence of wilful misconduct.[217] These provisions are, again, the reinforcement of the strict and joint liability.

With respect to limitation, it has its own limitation regime depending on whether the damage results from a packaged or a bulk substance, or both of them, or the situation is uncertain from which the damage is resulted. That being the case, as distinct from other IMO conventions mentioned here in this part, the HNS 2010 has not entered into force yet.[218] Since it is not still in force, the LLMC 1996 regime is expected to apply, at least for now. What must again be borne in mind is that clubs will in no case be liable, neither to their members nor to third-party claimants, for a sum exceeding the limits.

There is also a fund, similar to CLC/FUND regime, to cover claims exceeding the limits of liability on the shipowners.[219] Contrarily, this fund regime is a single instrument regime which indicates that the ratification of the HNS 1996 and the HNS 2010 means also the ratification of this fund regime. It enables this regime to easily apply in practice as

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[216] HNS 2010, articles 7 and 8.

[217] HNS 2010, articles 12/1 and 12/8. Note that the Contracting States might declare that the HNS 2010 not to apply to ships not exceeding 200 gross tons, carrying noxious and hazardous substances only in a packaged form, or engaging on voyages between facilities and ports of such state. *See* to that effect, HNS 2010, article 5/1.

[218] HNS 2010, article 9; International Maritime Organization: "Status of IMO Treaties", 10.02.2022, p. 508, ***https://wwwcdn.imo.org/localresources/en/About/Conventions/StatusOfConventions/Status%20-%202022.pdf (accessed 04/04/2023)*** (hereinafter "Status of IMO Treaties").

[219] HNS 2010, article 14(5).

compared to the CLC/FUND regime where the states need to ratify both of those conventions to give them effect.

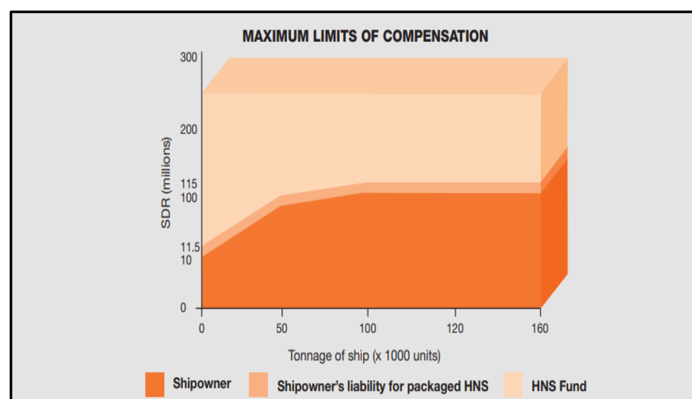

Figure 2: Upper limits under the HNS 2010

Source: International Maritime Organization: The HNS Convention-Why it is needed, ***https://wwwcdn.imo.org/localresources/en/MediaCentre/HotTopics/Documents/HNS%20ConventionWebE.pdf (accessed 04/04/2023)***.

e) PAL 2002

The carriage of passengers by sea has had an important place for a long time. That being so, it has brought deaths and personal injuries with it, resulting from disastrous accidents, among which the incidents of *The Titanic* (1912), *The SS Eastland* (1915), *The Herald of Free Enterprise* (1987), *The Estonia* (1994), and *The Costa Concordia* (2012) have been the remarkable ones so far.[220]

Ignoring the Brussels conventions that could not spread worldwide,[221] the year of 1974, in which a convention in that regard was adopted, was a true milestone for governing the

[220] Duda, D. / Wawruch, R.: "The Impact of Major Maritime Accidents on the Development of International Regulations Concerning Safety of Navigation and Protection of the Environment", ***Scientific Journal of PNA***, 2017, Vol. 211, p. 23, 29-32, 34-36, 37-38; Leighton Law: "10 Worst Cruise Ship Disasters in History", ***https://leightonlaw.com/10-worst-cruise-ship-disasters-in-history/ (accessed 04/04/2023)***.

[221] *International Convention for the Unification of Certain Rules Relating to the Carriage of Passengers by Sea*, Brussels, 29.04.1961, 1411 UNTS 87; *International Convention for the Unification of Certain Rules Relating to Passenger Luggage by Sea*, Brussels, 27.05.1967. Note that other conventions which were concluded and regulations which were made following the marine accidents in order to ensure the navigational safety are beyond the scope of this thesis.

carriage of passengers and the luggage thereof by sea. Later on, three protocols were adopted. Remarkable amendments were the change in the applicable unit of account as SDR in 1976, increase in the limits in 1990 that has never entered into force, and most of all, introduction of compulsory insurance, direct action, strict liability, and opt-out clause together with the increase in the limits in 2002. The consolidated text is known as the *Athens Convention relating to the Carriage of Passengers and their Luggage by Sea* ("PAL 2002").[222] It basically governs the liability of the carrier in the course of carriage of passengers and the luggage thereof. The convention applies to carriages conducted internationally.[223]

Different from other conventions, PAL 2002 imposes both strict and fault-based liability on the carrier. He is strictly liable for death and personal injury resulting from a shipping incident; however, he is liable only if he is at fault in terms of death and personal injury, not resulting from a shipping incident, and in terms of damage to or loss of the luggage.[224] Besides that, liability is joint and several for the performing carrier and the carrier if they are both liable on their parts.[225] It enables the passengers to choose from one of those carriers, or their clubs as indicated below, against whom to proceed for compensation.

With respect to limitations, strict and fault-based liability of the carrier, in terms of death and personal injury, shall not exceed SDR 250,000 and SDR 400,000 per passenger in each distinct case, respectively. These limits are above the limit of SDR 175,000 per passenger set out under LLMC 1996 (also note that the ceiling of SDR 25m under LLMC 1976 was repealed).[226] Over and above this, the liability is limited to SDR 2,250, 12,700, and 3,375 regarding cabin luggage, vehicles, and any other luggage, respectively.[227] That being the case, it must absolutely be borne in mind that clubs have been providing cover

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[222] *Athens Convention relating to the Carriage of Passengers and their Luggage by Sea, 1974*, Athens, 13.12.1974, 1463 UNTS 19; *Protocol of 2002 to the Athens Convention relating to the Carriage of Passengers and their Luggage by Sea, 1974*, London, 01.11.2002 ("PAL 2002" for the consolidated text). *See also* Ilgın, C. Ö.: "Deniz Yolu ile Yolcu Taşıma Sözleşmelerine İlişkin Bir Değerlendirme", ***İstanbul Ticaret Üniversitesi Sosyal Bilimler Dergisi***, 2007, p. 231, 248-252.

[223] PAL 2002, article 2.

[224] PAL 2002, article 3. For the definition of "shipping incident", *see* PAL 2002, article 3/5(a).

[225] PAL 2002, article 4. For the definition of "carrier" and "performing carrier", *see* PAL 2002, article 1/1.

[226] PAL 2002, articles 3/1, 3/2, and 7; LLMC 1976, article 7; LLMC 1996, article 7.

[227] PAL 2002, article 8.

up to the amount of USD 2bn and 3bn for passenger and passenger together with crew claims, respectively, under their rules since the adoption of the PAL 2002.[228]

Last but not least, the Protocol of 2002 obliges insurance for the ships authorised to carry at least thirteen passengers, and it prescribes direct action similar to its predecessors. It must be borne in mind that carriers are liable not only for death and injury of passengers *per se*, but also for their luggage and vehicles as indicated hereinabove; however, they shall purchase insurance only for the former group of claims. The insurance or security limit shall be at least SDR 250,000 at all events per passenger.[229] It is worth adding that the option of claimants to proceed against the club does not purport that they waive their right to claim against the carrier, regardless of performing or not, in the legal proceedings. Finally, clubs are precluded from relying on, among other defences but wilful misconduct, the "pay to be paid" under this convention too.[230]

It is worth noting that there is no prohibition for insurance cover to be purchased up to the amount of SDR 400,000, which is possible considering the fault-based liability by the way; however, clubs will not be responsible in direct actions for the exceeding amount of SDR 150,000, and they can, theoretically, very well avail of the defence that the member have not made the payment himself yet. That being so, this has never been the practical reality where clubs compensate the claimants for death and injury claims for the sum exceeding SDR 250,000. Because, as demonstrated, the liability regime under PAL 2002 is the heaviest one in view of the possible increase in compensation amounts if all, or the majority of, the passengers suffer loss or damage, or worst of all, decease.

f) IMO Guidelines

Other than the conventions stated above, the IMO issued three guidelines in this context. It must, first and foremost, be kept in mind that despite the importance of these guidelines

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[228] Britannia, Rule 27(2)(A); Shipowners, Rule 21D; North, Rule 22(4); London, Rule 11.4; UK, Rule 5(B)(iii); West, Rule 7(4); Standard, Rule 6.7; Steamship, Rule 18(iv)(b); Swedish, Rule 3, section 6 and Appendix II, Rule 1; Skuld, Rule 8.3 and Appendix 5a; Gard, Rule 53.2 and Appendix IV of the "Rules for ships"; American, Rule 1, section 4.37; Japan, Special Clauses, Passengers and Seamen Liability Limitation Clause.

[229] PAL 2002, articles 3 and 4bis/1.

[230] PAL 2002, article 4bis/10.

stated below, none of which are legally binding, *i.e.*, they are considered to be soft law[231] as compared to the conventions ratified by states.

The first guideline concerns the liabilities of shipowners in terms of maritime claims under the LLMC 1976/1996 regime. It urges shipowners, if the ship is 300 gross tons or more, to conform itself, under which they are urged to obtain insurance cover for the claims under LLMC 1976/1996, with the exception of cargo claims, and up to the limits, as amended in 2012. Shipowners are also encouraged to conform to the guideline even if the ships are less than 300 tons.[232] However, there is neither direct access to the insurer, or more relevantly, the club, nor any waiver of "pay to be paid" or whatsoever.

Claims of seafarers have always been a significant issue. The IMO, thereupon its joint work with the International Labour Organization ("ILO"),[233] issued two other guidelines:

(1) The first of which concerns the claims of abandonment of seafarers. In this context, insurance includes the expenses of and during repatriation like food or accommodation, any payment to seafarers like accrued salaries, and any other payment during the abandonment which is derived therefrom. It also urges the shipowners of all seagoing ships, save for the ones used for non-commercial purposes, to obtain financial security regardless of their tonnages. In consideration of the terms preferred under the IMO conventions above, it is evident that the term "financial security" corresponds to any security including insurance cover.[234] For abandonment, however, there is no provision regarding direct action, and there is no provision regarding the waiver of "pay to be paid" either.

(2) The other guideline concerns the claims of death and injury, under the provisions of which the shipowners of all seagoing ships, save for the ones aforementioned, are urged

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[231] *See* to that effect, *Statute of the International Court of Justice*, 26.06.1945, 33 UNTS 993, article 38.

[232] *Guidelines on Shipowners' Responsibilities in Respect of Maritime Claims*, IMO Resolution A.898(21), adopted on 25.11.1999, articles 1.1.5, 2.1, 2.2, 3.1, and 4.1.

[233] Demir, İ.: "Gemiadamlarının Ölüm, Cismani Zarar ve Terkedilmeleri Sebebiyle Doğan Taleplere Dair Hukuki Sorumluluk ve Tazminata İlişkin Uluslararası Denizcilik Örgütünce Yürütülen Çalışmalar", ***Sosyal Güvenlik Dünyası***, November - December 2011, Iss. 76, p. 68-75.

[234] *Guidelines on Provision of Financial Security in Case of Abandonment of Seafarers*, IMO Resolution A.930(22), adopted on 29.11.2001, articles 2, 3.1, 3.2, 4.1, 5, 6.1.

to obtain insurance cover, regardless of tonnage, pursuant to the guideline.[235] Nevertheless, right of action against the insurer and the waiver of "pay to be paid" seems to be not in question herein as well in respect of such claims.

g) MLC 2006 and the Amendments of 2014

Following the gradual increase in the importance of the claims of seafarers over the recent years, as well as considering the difficult conditions they have to work on since they are far away from their homelands and at sea for months, there was a need for a legal regulation to achieve an international standard for protecting their rights and establishing decent working conditions for them. As a result of this, the *Maritime Labour Convention, 2006* ("MLC 2006") was adopted to basically govern, *inter alia*, the minimum standards of working on board the ship, employment conditions, needs for food, accommodation, and social activities, and health protection and social security of seafarers.[236] It came into force on 20 August, 2013.

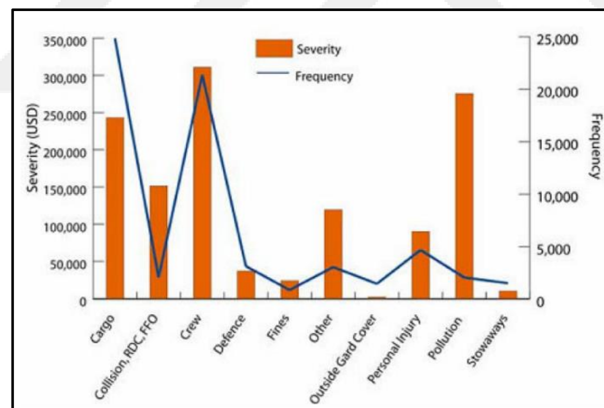

Figure 3: The statistics of claims exposed by Gard P&I

Source: Gard: "A crew claims statistical analysis", 2004**,**

https://www.gard.no/web/updates/content/51945/a-crew-claims-statistical-analysis

(accessed 26/03/2023).

[235] *Guidelines on Shipowners' Responsibilities in Respect of Contractual Claims for Personal Injury to or Death of Seafarers*, IMO Resolution A.931(22), adopted on 29.11.2001, articles 2, 3.1, 3.2, 4.1, and 6.

[236] *Maritime Labour Convention, 2006*, Geneva, 23.02.2006, 2952 UNTS 3 ("MLC 2006").

The convention, in its original text, prescribes that each Member State shall ensure under their respective laws that the ships flying their flags to have financial security, any security including insurance, for claims arising out of abandonment[237] and death, injury ending up with long term disability, and illness.[238] These are not direct impositions on shipowners, though. From this, it can be observed that the MLC 2006 addresses the concerns, but left the concrete steps to be taken to the implementation of national laws. As a result of that, unless States impose pecuniary sanctions or whatsoever on shipowners pursuant to their laws and regulations, and ensure the implementations thereof, shipowners might, theoretically, very well feel not obliged to purchase insurance. Nonetheless, this has never been the case in practical reality where every owner purchases insurance. It is, therefore, nothing more than a theoretical approach.

There are four amendments, adopted in the years of 2014, 2016, 2018, and 2022, to the MLC 2006, only the first of which is directly related to the subject of this thesis, and it entered into force on 18 January, 2017.[239] Clubs notified their members via circulars with regard to the amendments.[240] Amendments of 2014 primarily prescribed that each Member State shall require the shipowners to carry a certificate on board the ship, pointing out that the financial security was in force in terms of the two categories of claims

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[237] MLC 2006, Regulation 2.5, paragraph 2. At least the following shall be covered: Salaries and other entitlements up to four months, expenses reasonably incurred to that effect, and essential needs such as food and accommodation. *See* to that effect, Amendments of 2014 to the MLC 2006, Geneva, 11.06.2014, Standard A2.5.2, paragraph 9.

[238] MLC 2006, Standard A4.2.1, paragraph 1(b).

[239] International Labour Organization (ILO): "Ratifications of MLC, 2006", ***https://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:11300:0::NO::P11300_INSTRUMENT_ID:312331*** ***(accessed 04/04/2023)***. *See also* Chamber of Shipping: "Maritime Labour Convention (MLC 2006) 2014 Amendments", ***https://www.denizticaretodasi.org.tr/en/news/maritime-labour-convention-mlc-2006-2014-amendments-1124-1#:~:text=the%20changes%20means-,The%202014%20amendments%20to%20the%20Maritime%20Labour%20Convention%20(MLC)%2C,into%20force%20on%2018%20January*** ***(accessed 04/04/2023)***.

[240] For instance, *see* Shipowners' Club: "Circular: Maritime Labour Convention 2006 as amended (MLC) Financial Security Requirements", 10.10.2016, ***https://www.shipownersclub.com/publications/maritime-labour-convention-2006-as-amended-mlc-financial-security-requirements/*** ***(accessed 05/04/2023)***; The American Club, Circular No. 34/16, 06.10.2016, ***https://www.american-club.com/files/files/cir_34_16.pdf*** ***(accessed 05/04/2023)***.

mentioned hereinabove.[241] Despite the fact that these are not still direct impositions on shipowners in theory, it is not, as indicated above, important in terms of practical reality.

What is particularly important both in terms of the original text and the amendments thereto is that, although it was proposed,[242] there is not any provision governing the right of action against the security providers (mostly the insurers, or *ad rem*, the clubs), nor an exclusion of the defence of "pay to be paid" or whatsoever. This resulted from the pressure of clubs and the position they took during the discussions in terms of the financial security system. It must, nevertheless, be absolutely borne in mind that, even if their members could not pay first, clubs were already compensating seafarers only in respect of death, injury, and illness since they changed their rules accordingly even before the Amendments of 2014.[243] That being the case, third-party claimants, that is, seafarers, seem to be at the mercy of clubs, so to speak. More precisely, claimants might be compensated directly by the club; however, they cannot bring a direct action even if they themselves wish to under international law. Even if they could, they would come up against the brick wall of "pay to be paid", so to say, because the clubs would possibly change their existing rules accordingly once again. Putting aside the above-cited claims, abandonment cover under the MLC 2006 was separately placed in club rules after 2014.

To sum up briefly, compulsory insurance is left to the national implementations in theory; however, in practice, ships carry certificates on board attesting that such cover is in place. That aside, neither direct action nor waiver of "pay to be paid" is established by the MLC 2006 or the amendments thereto; however, again in practice, clubs ignore their unique rule and compensate seafarers only for the claims regarding death, injury, and illness. Although the way the protection of seafarers has come so far is praiseworthy in practice, it does not seem sufficient having regard to the fact that clubs still pull the strings, in a

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[241] Amendments of 2014 to MLC 2006, Geneva, 11.06.2014, Standard A2.5.2, paragraphs 3 and 6, Standard A4.2.2, Standard A4.2.1, paragraphs 8 and 11, Appendices A2-I and A4-I.

[242] IMO/ILO/WGLCCS 9/3: Examination of the issue of financial security for crew members/seafarers and their dependants with regard to compensation in cases of personal injury, death and abandonment., Geneva, March 2009, p. 4 § 3.

[243] IMO/ILO/WGLCCS: Final report, ILO/IMO/WGPS/8/2008/5, Geneva, 21-24 July 2008, page 7 § 55, page 11 § 89, page 12 § 93. For current club rules, *see* Britannia, Rule 19(1)(A); Shipowners, Rule 1(9); North, Rule 20(2); West, Rule 10, paragraph 7; Standard, Rule 6.16.1; Swedish, Rule 3(sec.4); Skuld, Rule 28.5.2; Gard, Rule 87.3; Japan, Rule 19(4).

manner of speaking. In other words, clubs might compensate seafarers, and they actually do so in practice, whereas seafarers cannot bring an action against clubs.

2- Under Supranational Law

In the EU, the *Directive 2009/20/EC* obliges ships of at least 300 gross tons, flying the flag of a Member State of the EU or flying the flag of another state but entering a port of a Member State of the EU, to have insurance cover for maritime claims under LLMC 1976/1996 regime and up to the limits set out thereunder. The non-compliance might be the issuance of an expulsion order or the detention of ships.[244] However, the period in advance of the aforesaid directive was problematical between the union and clubs. Therefore, it does not include any provision regarding direct action to support the enforcement of insurance, nor does it exclude the defence of "pay to be paid".

3- Under National Laws

a) English Law

As pointed out in the previous parts of this thesis, the TPA 1930 prescribed a subrogation regime, by which third parties "step into the shoes" of the insured and directly proceed against his insurer. However, the system thereunder was inadequate and, as to P&I insurance, clubs were invoking the defence of "pay to be paid", especially following the verdict rendered in the leading case of *The "Fanti" and The "Padre Island"*.[245] Because of this situation, third-party claimants were, so to speak, caught between a rock and a hard place, particularly if the insured member was insolvent. This unfairness was thereafter dispelled in marine insurance, regardless of the insolvency of the insured, only in respect of claims regarding death, injury, oil pollution, and wrecks pursuant to the addressed provisions of the TPA 2010 below together with the implemented IMO conventions. In short, clubs cannot invoke such defence, but limited to the claims just cited above and

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[244] *Directive 2009/20/EC*, articles 2(1), 4, and 5(2); Gauci, G.: "Compulsory Insurance Under EC Directive 2009/20/EC – An Adequate Solution for Victims, or is it also Time for the Abolition of Maritime Limitation of Liability and the Establishment of an International Fund as an Insurer of Last Resort?", ***Journal of Maritime Law and Commerce***, 2014, Vol. 45, Iss. 1, p. 77, 90-92.

[245] *The "Fanti" and The "Padre Island"* [1990] 2 Lloyd's Rep 191, HL.

deriving from marine insurance, in the actions brought by third parties against them as of now.

> "(5) The transferred rights are not subject to a condition requiring the prior discharge by the insured of the insured's liability to the third party."
>
> "(6) In the case of a contract of marine insurance, subsection (5) applies only to the extent that the liability of the insured is a liability in respect of death or personal injury."[246]

It must be noted that, in respect of oil and bunker pollution liabilities, the MSA 1995 enacted provisions in domestic law regarding compulsory insurance and direct action in support of the implementation of the related IMO conventions.[247] It similarly implements the WRC 2007 as for wreck liabilities.[248] That being so, the MSA 1995 explicitly excludes the application of the TPA 2010 for those three types of claims stated hereinabove.[249] Nevertheless, the "pay to be paid" is not retained for those claims since the relevant IMO conventions in that regard have already been implemented into the national law.

In addition to that, claims related to death and injury are also subject to the provisions of the TPA 2010, regarding the waiver of "pay to be paid" evaluated hereinabove, pursuant to which the insured shipowner shall be insolvent or the claimants shall make him insolvent if he has not been insolvent by law yet as a condition precedent. In terms of passenger claims, however, the MSA 1995 also implemented PAL 2002, and therefore, there is not any necessity of insolvency.[250] In terms of crew claims, on the other hand, the condition of insolvency for the claimants to "step into the shoes" of the insured is retained. It means that, although there is no reliance on "pay to be paid" for crew claims related to death and injury, claimants, that is to say, seafarers or their dependants, still need to satisfy the condition of insolvency under the TPA 2010 in order to be compensated in the end.

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[246] TPA 2010, sections 9(5) and 9(6).
[247] MSA 1995, sections 153, 153A, 163, 163A, 165(1), 165(1A). *See also* MSA 1995, Part VI, Chapters III&IV for the implementations of CLC/FUND.
[248] MSA 1995, sections 255J and 255P.
[249] MSA 1995, sections 165(5), 255P (4), and 255P (7).
[250] MSA 1995, sections 183 and 192A, and Schedule 6.

Besides all these, it must be noted that neither the HNS 1996 nor the HNS 2010 have been ratified or implemented by the UK yet,[251] as a consequence of which, the above-mentioned unique rule of P&I insurance is retained for HNS claims as well as the other types of claims.

It is worth adding that the illness and personal injuries of employees in the course of their employment, employers are obliged to obtain insurance. Nevertheless, shipowners were once exempted from insuring their employees, or *ad rem*, seafarers until MLC 2006.[252]

b) Scandinavian Law

Under Norwegian law, provisions regarding direct action were not mandatory pursuant to the *Insurance Contracts Act of 1930* erstwhile. The non-mandatory aspect was once posing a problem of contractual parties, particularly the insurer who was in a strong position *vis-à-vis* the insured, to stipulate to the contrary.

In the leading case of *The Skogholm*,[253] however, the provisions regarding direct action were held to be mandatory, *i.e.*, it could not be contracted out to the detriment of the third party anymore. The verdict was thereafter embodied under the *Insurance Contracts Act of 1989* ("ICA 1989") as a rule. As of now and opposed to the TPA 2010, Norwegian law entitles the third party to directly bring an action against any insurer, including clubs, wherein the insurer cannot rely on any defence.[254]

Considering the fact that P&I insurance offers liability coverage, bringing a direct action against clubs should be considered within the meaning of the mandatory aspect, the non-contracting-out aspect, of ICA 1989. Therefore, it can be observed that the Norwegian-based clubs, which are the members of IG, exclude the application of the ICA 1989 in

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[251] IMO, Status of IMO Treaties, 506, 510. *See also* MSA 1995, section 182B.

[252] *Employers' Liability (Compulsory Insurance) Act 1969* (c. 57), sections 1(1) and 2(2)(b); *Employers' Liability (Compulsory Insurance) Regulations 1998,* SI 1998, No.2573, Schedule 2, paragraph 12.

[253] *Skogholm,* ND 1954.445 (NH) (Rt. 1954, 1002).

[254] *The Insurance Contracts Act of 1989*, 16.06.1989, sections 1-2(a), 1-3, 7-6, 7-7, and 7-8. *See also* Bull, H. J.: "Insurance Law and Marine Insurance Law: The Unequal Twins", ***Stockholm Institute for Scandinavian Law***, 2010, p. 11, 33; Costas, E.G.: "P&I Cover in England and in Norway: A Comparative Analysis of Current Problematic Issues", Master's Thesis, University of Oslo, 2011, p. 26-28.

any case pursuant to their club rules[255] for abstaining from becoming liability guarantors unequivocally. As for the Swedish Club, it refers to the *General Swedish Marine Insurance Plan of 2006*, under the provisions of which the insurance contract does not apply to third parties unless otherwise agreed thereunder.[256] In sum, from the foregoing points, it can be deduced that the long-standing rule of clubs is retained save for the claims covered under international conventions to which these countries are party.

Those aside, it is also worth adding that the *Norwegian Marine Insurance Plan* ("NMIP") of 1996 (revised in 2010) governs the other sorts of marine insurance specifically. As to P&I insurance, although it was included in Part III of the NMIP of 1964,[257] it was excluded later on. As of now, there is not any part special to P&I insurance except for its common provisions applicable to all sorts of insurance.[258] NMIP has a significant role not only in Norway but also in the other Scandinavian countries. So much so that the *Nordic Marine Insurance Plan of 2013* (revised in 2019) was drafted on the basis of the NMIP of 1996 (revised in 2010).[259]

c) American Law

It must, in general, be borne in mind that, before direct action statutes were gradually enacted, the position under American law was identical to the one under English law. More exactly, third parties were not able to directly sue the insurer due to the privity of contract, which was also considered to be one of indemnity then.[260]

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[255] Skuld, Rule 47.3; Gard, Rule 90.

[256] Swedish, Rule 2, paragraph 6; *General Swedish Marine Insurance Plan of 2006*, 01.01.2006, article 14.1.

[257] *Norwegian Marine Insurance Plan of 1964*, ***https://www.nordicplan.org/archive/the-norwegian-marine-insurance-plan-of-1964/*** ***(accessed 04/04/2023)***.

[258] *Norwegian Marine Insurance Plan of 1996, Version 2010*, ***https://www.nordicplan.org/archive/the-norwegian-marine-insurance-plan-of-1996-version-2010/*** ***(accessed 04/04/2023)***; Judice, M. P.: "The Cover of Third Parties Under P&I Insurance", Master's Thesis, University of Oslo, 2008, p. 9-10.

[259] *Nordic Marine Insurance Plan of 2013, Version 2019* (based on the Norwegian Marine Insurance Plan of 1996, Version 2010), ***http://archive.nordicplan.org/The-Plan/*** ***(accessed 04/04/2023)***. It is an agreement between the Norwegian, Swedish, Finnish, and Danish associations of shipowners.

[260] Kierr, R. H.: "Effect of Direct Action Statutes on P and I Insurance, on Various Other Insurances of Maritime Liabilities, and on Limitation of Shipowners' Liability", ***Tulane Law Review***, 1968-1969, Vol. 43, Iss. 3, p. 638, 650.

Afterwards, the “no action” rule, standing for the “pay to be paid” rule, was negated in most jurisdictions in the United States of America (“USA” or “US”) on the ground that it was infringing on public policy and the right of direct action which had been granted to third parties under law. In other words, the underlying rationale of this negation is that the statutory right of third-party claimants should not be retrieved by a defence deriving from a contract to which they are not even parties. Therefore, the concept of direct action in the US is more developed than it is in the UK, and third parties are able to proceed against the insurers directly. By means of that, the indemnity basis has been converted into a liability basis where the “no action” rule is negated in certain states,[261] including the State of New York, to which the American Club refers, if the insured is insolvent. It is worth bearing in mind that it does not apply to club insurance.[262]

On the other hand, there is no federal statute concerning marine insurance and the right of direct action. Subsequent to the incident of *The Exxon Valdez* (1989), resulting in oil spillage in Alaska,[263] the US created its own pollution regime in 1990 with the *Oil Pollution Act of 1990* (“OPA 90”), pursuant to which no ship is allowed to navigate in a place subject to the US jurisdiction unless she is insured in accordance with that Act. However, ships might have insurance cover under strict conditions.[264] So much so that, the consequences of non-compliance are harsh.[265] In addition, it similarly enacts provisions regarding direct action in support of compulsory insurance. The OPA 90 also excludes the defence of “pay to be paid” in those actions.[266] Besides that, what must be borne in mind that the US has not ratified any of the above-mentioned IMO conventions so far, and it has not ratified the MLC 2006 either.

Furthermore, owners or charterers of the ships designed to carry at least 50 passengers, who embark on the ship at the ports of the US, shall provide insurance cover, which is

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[261] Acar, Kulüp Sigortası (P&I), 23-25, 401-404, 505-507, 559-561; Hazelwood / Semark, 303-305, 340. For instance, *see* Louisiana RS 22:1269. There are other conditions as well, *see* to that effect, Louisiana RS 22:1269, B. (1) (a-f). *See also* Kierr, 651-652.

[262] American, Rule 1, section 4.52; The Laws of New York, Chapter 28 (Insurance), Article 34 § 3420.

[263] Duda / Wawruch, 36-37.

[264] *Oil Pollution Act of 1990*, 33 U.S. Code § 2716(a).

[265] *Oil Pollution Act of 1990*, 33 U.S. Code § 2716(b); 33 U.S. Code § 2716a. *See also* 33 U.S.C. § 1321(7).

[266] *Oil Pollution Act of 1990*, 33 U.S. Code § 2716(f)(1).

evidenced by the Federal Maritime Commission Certificate, and ensure their potential liabilities regarding death and injury, pursuant to *Title 46, U.S. Code*.[267]

d) Turkish Law

Under Turkish law, no code directly regulates marine insurance, nor P&I insurance. Instead, with respect to insurance law in general, including marine insurance, there are relevant provisions under the Turkish Commercial Code ("TCC"). In accordance with the provisions of which governing liability insurance, a right of direct action is granted to those suffering damage to proceed against the insurer without subject to any condition of prior discharge or whatsoever.[268]

It is now possible to raise the question of whether the provision regarding direct action under the TCC applies to P&I insurance or not, especially in consideration of the "pay to be paid" clauses under the contracts of P&I insurance. First and above all, in so far as Turkish law applies to policies covering P&I liabilities, the direct-action provision under the TCC applies to such policies on the ground that contractual provisions cannot override the mandatory provisions of codes that intend to protect the weaker party, or *ad rem*, the injured third party to the contract of P&I insurance. Therefore, third-party claimants can proceed against P&I clubs in that case. That aside, there is no club, or more exactly, an association based on mutuality, conducting business in Türkiye. Actually, there is Turk P&I, but it is legally a joint-stock company, functioning on traditional insurance technics, rather than a club. Even if there was a club technically, it would probably exclude the application of the TCC similar to the Norwegian-based clubs evaluated above, or refer to English law or other laws depending on its choice. In case of the latter, it would probably be English law, pursuant to which the long-standing rule of "pay to be paid" is still mainly retained.

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[267] 46 U.S. Code § 44101, 44103. *See also* 46 C.F.R. § 540.20-27; U.S. Public Law 89-777, section 2; Acar, Kulüp Sigortası (P&I), 132-133; Hazelwood / Semark, 168.

[268] *Turkish Commercial Code* numbered 6102, dated 13.01.2011, article 1478 ("TCC").

In terms of oil pollution claims, the TCC refers to international conventions.[269] In addition thereto, there is also a particular code for, *inter alia*, insurance obligation imposed on the ships carrying oil or other harmful substances.[270] As to wrecks, however, Türkiye is not a party to the WRC 2007, nor did it adapt any provisions thereof. As for maritime claims, Turkish law not only refers to international conventions under the TCC, but it also prescribes compulsory insurance under a by-law in that regard.[271] Moreover, Türkiye has recently become a party to the PAL 2002, and it already adapted its provisions even before then, including compulsory insurance[272] but not direct action since the TCC, pursuant to article 1478, prescribes such right in terms of liability insurance in general as cited above.

C) PERSPECTIVE OF CLUBS

IG P&I, due to its strong position and supremacy in the business, represents the clubs and protects their benefits in the international field *vis-à-vis* intergovernmental organisations, states, legislators, maritime authorities, and marine insurance and shipping industries that will either regulate the policies, standards, or legal aspects of insurance and liability regimes. These bodies take heed of the IG P&I clubs' viewpoint on which it should be put an emphasis to perceive their perspective regarding compulsory marine insurance.

Clubs have never been satisfied entirely with the notion of compulsory insurance. Their main concern is that it might lay the groundwork for direct actions on which they cannot rely on the defence of "pay to be paid". Furthermore, such mandatory requirements might put them into a better bargaining position where it is known the members have to purchase the product no matter what, and thus, the number of calls might increase. In addition, club insurance is based on the "pay to be paid" rule, so the changes in this regard do not fit for the purpose of club insurance. Due to, *inter alia*, those concerns, clubs insist on not becoming liability guarantors who might face the risk of unlimited liability. Although, thanks to mutuality, the capacity is not a problem and insurance certificates issued by

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[269] TCC, articles 1336 to 1340.

[270] *Code on the Principles of Emergency Response and Compensation for Damages in Pollution of Marine Environment by Oil and Other Harmful Substances* numbered 5312, dated 03.03.2005, articles 1 and 8.

[271] TCC, articles 1328 to 1135; *By-Law on the Insurance and Inspection of the Ships Relating to Maritime Claims*, published on 14.11.2010 in the Official Gazette, article 5.

[272] TCC, article 1259.

state authorities mostly depend on the financial trust and an adequate inspection of clubs, it is not always certain whether they will become insolvent if claims with high amounts simultaneously arise.

The reflections of the perspective of clubs over the recent years can be seen in many legislative and conventional advances. First of all, they do not want to become liability guarantors and this is one of the reasons why they objected to the OPA 90, a federal act of the US, that much. Because, the limits of liability under that Act are high, the liability is harsh, and each state might enact its own law in terms of pollution. Thus, the Certificate of Financial Responsibility under the OPA 90 is not provided by clubs. It is only provided on the condition that additional premiums or calls are paid and periodic declarations with respect to voyages falling within the scope of the OPA 90 are given to clubs.[273]

Besides that, the period between the years of 2005 and 2009 was problematical between the EU and clubs following the proposal of the *Directive 2009/20/EC*. Clubs were mainly objecting to direct action system with similar reasons. Even though it was discussed during the negotiations, it did not take place in the final version.[274] The main concern was to not become a liability guarantor for the claims under LLCM 76/96 regime.

Over and above these, claims regarding death and personal injury might reach high amounts whether stemming from passengers or seafarers. So much so that, clubs objected that the limits under the PAL 2002 were high. Nevertheless, their attempts were futile. In consequence, IG P&I increased its reinsurance limits up to USD 2bn and 3bn for passenger and passenger together with crew claims, respectively. It is also worth noting that crew claims have gradually become a significant issue over the recent years, and it is continuing to be significant in the same manner.

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[273] Acar, Kulüp Sigortası (P&I), 196-198; 222-225; Hazelwood / Semark, 188-189; Gauci, 89; Zhu, 73.

[274] EUR-Lex: "COM/2005/0593 final - COD 2005/0242", ***https://eur-lex.europa.eu/legal-content/EN/HIS/?uri=celex:52005PC0593*** ***(accessed 05/04/2023)***; European Parliament legislative resolution of 29.03.2007 on the proposal, article 13, ***https://www.europarl.europa.eu/doceo/document/TA-6-2007-0094_EN.html?redirect*** ***(accessed 05/04/2023)***.

During the discussions of the provisions of financial security under the MLC 2006 and the Amendments of 2014 thereto, clubs objected to certain points with the aim of not becoming the guarantors of liabilities of their respective members. These claims were very well related to fundamental rights such as right to life or corporeal and spiritual integrity, but also therefore, the liability could reach to high amounts.[275] Clubs argued that they were already providing cover for the claims of death, injury, and illness even their members could not pay at first. They nevertheless embodied this practice of compensation under their rules regardless of any prior payment by its member. In addition to that, IG P&I rearranged, to be effective from the date of force of the Amendments of 2014, its reinsurance programme regarding abandonment cover to that end.[276]

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[275] IMO/ILO/WGLCCS: Final report, ILO/IMO/WGPS/8/2008/5, Geneva, 21-24 July 2008, page 7 § 55, page 11 § 89, page 12 § 93.

[276] IG P&I: "International Group reinsurance 2017/18 renewal update December 2016", 14.12.2016, ***https://www.igpandi.org/article/international-group-reinsurance-renewal-update-december-2016/*** ***(accessed 05/04/2023)***.

VI. CONCLUDING REMARKS

In the wake of globalisation, developing technology, the building of steamships, and increasing commercial relations brought a new dimension to marine risks. Accordingly, the liability of shipowners strikingly increased from the mid-19th century to the mid-20th century onwards, particularly following the remarkable marine disasters and casualties.

Law, thankfully, is empirical. Some of the liabilities which had not been previously regarded as a serious problem became crucial, and so did the necessity of change in terms of their legal framework. Thus, it was intended that clubs, unrivalled providers of P&I insurance, to maintain their funds, and it was also intended that third parties to be protected by making insurance compulsory over the recent decades, at least for specific claims related to public interest, *e.g.*, the protection of marine environment or safety of life and corporeal or spiritual integrity of persons. Nonetheless, it would not be wrong to say that insurance, or *ad rem*, P&I insurance is still theoretically based on voluntariness.

Over and above this, generally speaking, a contract is binding and enforceable only between the parties thereto owing to the principle of *inter partes*, or more clearly, privity of contract. Thus, the intention for securing the pecuniary resources of clubs and protecting the claimants, by making insurance compulsory, amounts to nothing if third parties are not somehow involved in the process. In order to overcome that problem, despite the absence of a contractual relationship, third parties were granted the right of direct action against clubs, by means of which they "step into the shoes" of the insured shipowner. Otherwise, compulsory insurance will not be as functional as intended in the absence of such direct connection.

It is highly significant because clubs, thanks to mutuality, are financially stronger than any other insurer or shipowner, and they cannot easily become insolvent unlike them. They have to also maintain sustainable financial capability pursuant to the regulations of states in which they carry out their activities. As can be seen, a club is a far better choice for claimants to proceed against. *Nota bene*, they can only file a suit against the club as long as they have such direct connection, and therefore, it is the enforcement of, but not a corollary nor adherence to, the regime of compulsory insurance.

Problems, however, never end. This time, third parties, so to speak, came up against the brick wall of "pay to be paid", due to which P&I insurance is different from traditional liability insurance and underpinned by the notion of reimbursement. In this regard, as the third parties were subrogated to the rights and became the successor of the shipowner, clubs started to rely on its unique rule as a policy defence, which could have been relied against the shipowner, that the third parties should have paid first. Hence, statutory subrogation seemed to be nothing more than a theoretical advantage. The situation was even worse when the owner was insolvent where the third-party claimants were put at the risk of remaining out of pocket. They were, in a manner of speaking, caught between a rock and a hard place. If they proceeded against the club, they would not be paid due to "pay to be paid". On the other hand, if they proceeded against the insolvent shipowner, they would not be paid again due to financial impossibility.

On the part of clubs, they are not completely satisfied with compulsory insurance because they are worried that it might pave the way for direct actions against them where they might not even rely on the defence of "pay to be paid" against claimants. In consideration of the extensity of claims, numerous risks in the business, and potential liabilities reaching to high amounts, clubs have always wanted to only reimburse the payments of their respective members instead of becoming liability insurers guaranteeing the liability to which such members are exposed. Due to their strong lobbies, they have been pretty much successful *vis-à-vis* the international bodies or states, a remarkable example of which is the position they took during the discussions concerning the financial security system under the MLC 2006 and the amendments thereto. That aside, clubs do not always apply its rule strictly, particularly when it comes to claims of death and injury.

Life should be in balance, and so should the scope of the protection of third parties. In principle, P&I insurance is not compulsory. As a matter of fact, there is no necessity that it should be totally compulsory or voluntary. The ideal solution striking the mark should be to establish a direct connection between third parties and clubs, where they cannot rely on the defence of "pay to be paid". The important point is to draw the line in respect of which claims and to what extent they should be protected thus and so. In this regard, its harshness has gradually been ameliorated, but can we consider it adequate?

(1) First and foremost, it goes without saying that the IMO has achieved a significant success by adopting the CLC 1992, BUNKERS 2001, HNS 2010, WRC 2007, and PAL 2002, under the provisions of all of which compulsory insurance and direct action were also prescribed in terms of claims related to marine environment as well as death and injury. More importantly, the aforesaid conventions negate, among other defences save for the wilful misconduct, the defence of "pay to be paid", on which clubs cannot rely, in the actions brought by the claimants against them. As for wreck claims, however, they mostly occur in internal and territorial waters, which are relatively narrow and crowded areas compared to vastly open seas, where there is too much maritime traffic. When viewed from this aspect, although internal and territorial waters of states might be included under the scope of the WRC 2007 by the "opt-in" clause enabling states to do so, the decision should not be left to states and the scope of the convention should be extended to those areas. As a result, insurance obligation, direct action against clubs, and waiver of defences will be extended accordingly.

(2) As regards seafarers' claims, although there is a financial security system for those related to abandonment together with death, injury, and illness, the right of direct action and the exclusion of "pay to be paid" therefrom have not been established yet. However, such claims are highly significant having regard to, *inter alia*, the aspects below.

It must be borne in mind that use or operation of each ship might give rise to a different claim, but every ship has a crew by which the navigation and overseas trade are carried out. Needless to say, the public also benefits from such trade. Furthermore, they work under difficult conditions. They have to work without shifts since it is uncertain what will happen and when it will happen. In addition, they are not only far away from their homelands *per se*, but they are also at sea for months. Even when a serious problem occurs, it is not quite possible for them to go ashore instantly. Over and above these, some claims might take a long time to show up, *e.g.*, mesothelioma, an occupational disease, resulting from asbestos exposure which may emerge even after decades of the event itself. Clubs might be liable even after the closing of the policy year, in so far as the event, which is occurred during employment, is the proximate cause of the loss. Last but not least, death or illness of or injury to seafarers are directly related to fundamental rights,

that is, the right to life or corporeal and spiritual integrity. In brief, the protection of seafarers is significant considering such protection also indirectly ensures public interest.

The ILO, with its joint work with IMO, took remarkable steps and prescribed a quasi-compulsory insurance system under the MLC 2006 for the claims arising out of death, injury, illness, and abandonment. Theoretically speaking, it prescribes that each Member State shall require the shipowners to have financial security, including insurance, and carry a certificate on board in that regard; however, it does not directly impose an obligation on shipowners. That being the case, it is not important in practical reality where every prudent shipowner purchases the product in the ordinary course of business. What must particularly be borne in mind that there is neither direct connection between seafarers and security providers, or *ad rem*, clubs, nor any waiver of "pay to be paid" or whatsoever. The way it has come so far is, therefore, praiseworthy but not adequate. It is possible from the foregoing issues to conclude that seafarers' claims, at least the ones related to death, injury, and illness, are highly significant. Prescribing only quasi-compulsory security system for such claims, however, does not solve the problems on the ground that compulsory insurance will not be functional in the absence of direct action, and direct action will not be functional in the absence of the waiver of "pay to be paid".

Practically speaking, clubs, provided that their members cannot not pay first, already provide cover for claims of death, injury, and illness by ignoring their two-centuries-old unique rule. That being the case, it does not signify that third-party claimant, that is to say, the seafarers, can proceed against clubs even if they very wish to. They are, therefore, at the mercy of the choice of clubs. In sum, clubs might compensate seafarers, and they actually do so in practice; however, seafarers cannot bring an action against them. That aside, granting the right of direct action will not be sufficient on its own because clubs will possibly change their existing and solution-oriented rules accordingly.

In light of these issues, there is a need for a detailed regulation, or at least an amendment to the MLC 2006 once again, whereby the right of direct action is prescribed and defence of "pay to be paid" is excluded therefrom. In consideration of the concerns of clubs throughout the adoption or enactment of legal instruments, it would not be wrong to say that abandonment of seafarers should not necessarily be protected in this way; however,

their death, injury, and illness should be. In this regard, it is worth bearing in mind that the MLC 2006 prescribes compulsory insurance for injury claims ending up with long term disability. However, seafarers' all injury claims should be protected on the ground that these claims are related to corporeal and spiritual integrity even if they end up with short term disability or no disability at all.

Besides, statutory regulations should be enacted under national laws in support of this process, especially in consideration of the existing condition of insolvency under English law for death and injury claims of seafarers. If the future will be patterned on the not-so-distant past, the system of compulsory insurance and direct action, directly or at least similarly modelling the IMO conventions, can be successful as it should be thus and so.

(3) As to other claims, the IMO and EU issued a guideline and a directive, respectively, for maritime claims under LLMC. Although there are not any provisions concerning direct action or waiver of "pay to be paid" under those instruments, it is not necessary in fact because it might seriously broaden the scope of actions, and convert the clubs into liability guarantors. The same rationale should be considered in terms of other claims not related to public interest but monetary interest, *e.g.*, collision, fines, or cargo claims.

To sum up, in the light of the above considerations, not to mention that P&I insurance is already compulsory in the ordinary course of business of a prudent shipowner, but not only on a legal basis. So much so that, no insurer will provide any type of insurance unless the shipowner has P&I cover, and *vice versa.* Similarly, no cargo will be loaded in the absence of such a cover. Besides, a ship not having P&I cover might face difficulties in the course of a port state control. Moreover, banks or other financiers might not provide any credit. These occasions impede the commercial life. Nevertheless, making P&I insurance compulsory on a legal base is not the solution on its own.

As a matter of fact, right of direct action should be granted, and the "pay to be paid" should be waived in order to properly protect the third-party claimants as it has done under certain IMO conventions so far. However, in terms of claims of death, injury, and illness of seafarers, there is no such protection but compulsory insurance. Instead, there should be a legal regulation for such claims which includes a direct connection between

them and clubs, where clubs cannot rely on the “pay to be paid”. Otherwise, the financial security regime under the MLC 2006 seems to be meaningless. Putting aside those claims, the scope of the WRC 2007 should be extended to territories of states without leaving the decision to them in that regard by the opt-in. A progress for those will, hopefully, be made someday in the not-so-distant future for the sake of claimants, the weaker ones *vis-à-vis* the strong clubs and shipowners.

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ÖZET

Uygarlığın doğuşundan bu yana ve özellikle deniz felaketlerini izleyen süreçte, deniz rizikoları ve gemi maliklerinin üçüncü kişilere karşı artan sorumlulukları giderek karmaşık bir hâl almıştır. Bu yüzden, P&I sigorta ilişkisinin üçüncü kişisi konumundaki ve gemi malikleri ile kulüpler karşısında görece güçsüz olan kişileri koruyabilmek adına, bu hususta hukuki bir düzenlemeye ihtiyaç olduğu fark edilmiş ve sonucunda uluslararası sözleşmeler akdedilerek bu sözleşmeler iç hukuklara entegre edilmiştir.

İlk olarak, gemi maliklerine bu uluslararası sözleşmelerden doğan sorumlulukları için finansal güvence sağlama yükümlülüğü getirilmiştir ki bu uygulamada çoğunlukla P&I kulüpleri tarafından sigorta sözleşmesi şeklinde sağlanmaktadır. Bunun yanı sıra, gemi maliklerinin ödemede acze düşmesi hâlinde üçüncü kişiler ödemesiz kalabilecektir. Dahası, kulüpler ve üçüncü kişiler arasında sözleşmenin nispiliği prensibi gereği bir sözleşme ilişkisi yoktur. Diğer bir deyişle, üçüncü kişiler kulüpleri dava edememektedir. Dolayısıyla zorunlu sigortaya ilaveten, üçüncü kişilerin finansal yönden gemi maliklerine ve (hatta karşılıklılık ilkesi uyarınca) diğer sigortacılara nazaran daha güçlü konumdaki kulüplere dava açabilmesinin temini amacıyla onlara doğrudan dava hakkı tanınmıştır.

Ne sigortayı zorunlu kılmak ne de doğrudan dava hakkı tanımak bu sorunu gereği gibi çözmeyecektir zira kulüpler, üyelerinin önce ödemekle yükümlü oldukları ödemeleri yaptıktan sonra ancak kulüpler tarafından masraflarının karşılanacağına ilişkin olan "önce ödeme" kuralını doğrudan davalarda üçüncü kişilere karşı bir def'i olarak ileri sürebileceklerdir. Bu yüzden "önce ödeme" kuralından deniz hukukunun bazı alanlarında vazgeçilmiştir. Ancak bunun mefhum-u muhalifinden çıkan sonuç, bu kuralın hâlen diğer bazı alanlarda geçerliliğini koruduğudur. İdeal çözüm kulüpler ve üçüncü kişiler arasında kulüplerin bu savunmayı ileri süremeyecekleri doğrudan bir bağlantı kurmaktır. Ancak o zaman bile, hangi taleplerin ne ölçüde bu şekilde korunması gerektiği tespit edilmelidir. Özetle, P&I sigortasınca teminat altına alınan talepler bu doğrultuda analiz edilmiştir.

Anahtar Kelimeler: P&I Sigortası, Koruma & Tazmin Sigortası, P&I Kulüpleri, Zorunlu Sigorta, Doğrudan Dava, "Önce Ödeme" Kuralı, Uluslararası Denizcilik Örgütü Sözleşmeleri, Sigorta Hukuku, Deniz Sigortaları, Karşılıklı Sigorta

ABSTRACT

Since the dawn of civilisation onwards, and especially following marine disasters, marine risks have become more complicated, and so has the issue of increasing third-party liabilities of shipowners. It was, therefore, noticed that there was a need for a legal regulation in that regard, which resulted in the adoption of international conventions and the implementation thereof into national laws, in order to protect third parties to the contract of P&I insurance, weaker ones *vis-à-vis* the strong clubs and shipowners.

First and foremost, providing financial security, which is usually provided by P&I clubs in the form of an insurance contract in practice, for the liability of shipowners under those conventions was imposed on them. That being the case, third parties might remain out of pocket provided that shipowners are insolvent. Furthermore, there is an absence of a contractual relationship between clubs and third parties due to the principle of *inter partes*, or more precisely, privity of contract, *i.e.*, claimants cannot sue clubs. Thus, in addition to compulsory insurance, the right of direct action was granted to third parties for them to proceed against clubs, which are financially stronger than shipowners and, thanks to mutuality underpinning the basis of P&I clubs, other insurers.

Neither making insurance compulsory nor granting the right of direct action properly solves this problem having regard to the fact that clubs might rely on the defence of "pay to be paid", in accordance with which the member shall make the necessary payments he is liable for to be reimbursed by his club, also in direct actions against third parties. For that very reason, "pay to be paid" has been waived in the specific fields of maritime law. From a *contrario* aspect, it is still retained in some other fields. The ideal solution should be to establish a direct connection between clubs and claimants, where clubs cannot rely on such defence. Even then, the extent should be determined in respect of which claims and to what extent they should be protected thus and so. In sum, claims covered under P&I insurance was analysed to that end.

Keywords: P&I Insurance, Protection & Indemnity Insurance, P&I Clubs, Compulsory Insurance, Direct Action, "Pay to Be Paid" Rule, International Maritime Organization Conventions (IMO Conventions), Insurance Law, Marine Insurance, Mutual Insurance