DEALING WITH THE COSTS OF PIRACY

INSURANCE COSTS

H&M coverage does not cover piracy losses where there is no hull damage and P&I coverage will not cover ransom payments. Although war-risk insurers will cover ransom payments and the costs of arranging for the successful delivery of the ransom (which can range anywhere from $75,000 for an air drop to $1 million or more for delivery by sea), they do not cover the costs of negotiating the ransom which often equals or exceeds the ransom itself.

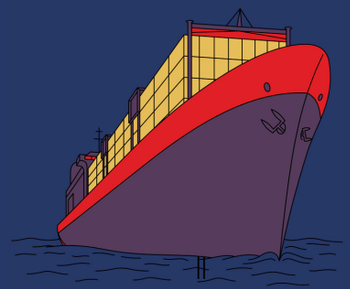
Nor do war-risk insurers typically cover the loss of business caused by the incident or the costs of security consultants, which frequently need to be retained to advise on the negotiating process and interact with the various Government and law enforcement agencies involved in the incident.

Only kidnap and ransom insurance ("K&R") covers all of these costs, including coverage if the ransom money is lost or seized en route to delivery.

APPORTIONING THE RISK OF LOSS BETWEEN SHIPPERS AND CARRIERS

Since COGSA and Hague-Visby do not address piracy or terrorism, carriers often have no legal leverage to force cargo interests to contribute to costs incurred by piracy incidents.

Many shippers are resistant to paying surcharges for piracy. Thus, carriers must either protect themselves by modifying contracts of carriage to cover piracy or by attempting to declare general average in the aftermath of a hijacking. At present it is unclear whether courts will accept pirate attacks as general average incidents but the theory is being currently tested by several carriers.



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Executive Summary

PIRACY UPDATE

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GROWTH OF PIRACY IN RECENT YEARS

While pirates have plagued the seas from time immemorial, their numbers have spiked in recent years and in particular locales. We examine some of the statistics behind the rise of the modern pirate below. *(All figures provided courtesy of the Piracy Reporting Centre at the International Chamber of Commerce's International Maritime Bureau.)*

PIRACY IN 2006 – RELATIVE CALM

In 2006 there were 239 total worldwide incidents of piracy resulting in 17 crew members being assaulted or injured. The relatively low amount of injuries recorded is likely related to the fact that guns were only reported as being used in 53 incidents. Further, out of the 239 total incidents, only 10 occurred in off the Somali coast and 12 occurred in Nigeria.

PIRACY IN 2007 – THE RISE OF SOMALIA

By 2007 the total number of worldwide incidents had increased 10% to 263 incidents, of which 72 involved the use of guns (a 35% increase over 2006). This increased use of weapons resulted in 64 crew members being assaulted or injured. Two of the major sources of the growth in piracy were Nigeria and the Somali coast, where 42 and 31 incidents were reported respectively.

PIRACY IN 2008 – A RECORD YEAR

In 2008 there were 293 incidents of piracy reported worldwide (an 11% increase over 2007), resulting in 49 vessels being hijacked, 889 crew members being taken hostage, and a further 46 vessels reporting being fired upon. Additionally, 32 crew members were injured, 11 killed, and a further 21 reported missing - presumed dead. Guns were used in 139 incidents in 2008, representing a tremendous 93% jump over the prior year.

The majority of the increase stems from the Somali coast where 111 incidents were reported. Guns were used in 102 of these incidents and they resulted in 42 out of the 49 successful hijackings that occurred worldwide. From these figures it is clear that the Somali pirate is a newer, far more dangerous breed of pirate than seen in recent years.

PIRACY IN 2009 – NO SIGN OF SLOWING

2009 is shaping up to be a year of record growth in piracy incidents, as there were 102 incidents reported in the first quarter alone, representing a nearly 20% increase over the number of incidents reported in the same period of 2008. The increase in the first quarter of 2009 is due almost entirely to increased Somali pirate activity, accounting for 61 of the 102 attacks this quarter, as compared to six incidents for the same period in 2008. The 102 attacks resulted in 29 vessels being fired upon, 34 vessels being boarded, 9 vessels being hijacked, 178 crew members taken hostage, 9 crew members injured, 5 crew members kidnapped and 2 crew members killed. Guns were used in 59 of the attacks.

By mid-May of 2009 there were more than 114 pirate attacks on ships, of which 29 were successful, and 500 crew members were taken hostage. Guns were used in 102 of these attacks.

RESPONDING TO THE PIRATE THREAT

The growth seen in the number of piracy incidents reported so far this year is unsurprising considering that pirates received approximately $80-100 million in ransom payments last year alone.

Since 2008, approximately 0.6 percent of all ships passing through Somali waters have been hijacked or attacked, with the average pirate incident lasting 59 days, and the average hijacking resulting in a ransom payment of $1-2 million. With incentives like these it will be extremely difficult to curb piracy in Somalia. This is especially so, given the relatively low costs involved in mounting attacks.

As a practical matter, pirates prefer to target slower, lower vessels that are easier to board such as bulk carriers, container ships, and chemical tankers. The typical attack involves three high-speed boats that can board a ship in as little as 15 minutes. Somali pirates are now regularly armed with machine guns, grappling hooks, and even rocket propelled grenades in many instances.

Governments have begun to respond to the growing threat, largely spurred on by several recent high profile hijackings such as the April 8 attack on the **Maersk Alabama**. The UN Security Counsel adopted four resolutions in 2008 addressing piracy, forming the Contact Group on Piracy Off the Coast of Somalia, a task force of 24 nations, several international organizations and NGOs - established to facilitate and coordinate the Security Counsel's efforts to suppress piracy.

Further, the European Union (Operation Atalanta), NATO (Operation Allied Provider) and the US Navy are currently running anti-piracy naval operations in the Indian Ocean and Gulf of Aden. In addition the Combined Maritime Forces composed of naval units from 25 other nations are patrolling Somali waters. Since August of 2008 they have intercepted 27 pirate vessels. The US Coast Guard has also recently issued a new security directive to US shipowners requiring them to develop security plans against piracy, terrorism, and armed robbery and authorizing them to have armed security forces aboard their vessels.

Unable or unwilling to wait for Governments to act, many shipowners are adding defensive measures such as fire hoses, barbed wire, and locked safe rooms, and are training their crews in how to evade pirates. Others are even going so far as to arm their crews or hired armed guards to act as escorts aboard their vessels.