Statement of The American Institute of Marine Underwriters
and The Water Quality Insurance Syndicate
Before The Subcommittee on Coast Guard and Maritime Transportation

By
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June 26, 1996

I am appearing here today on behalf of the American Institute of Marine Underwriters ("AIMU") and the Water Quality Insurance Syndicate ("WQIS"), two organizations that hold positions of unique involvement in the maritime industry because of our experience in the issuance of certificates of financial responsibility ("COFRs") under federal pollution laws. AIMU is a not-for-profit trade association representing over 100 marine insurers, accounting for approximately 90% of the commercial marine insurance underwritten in the United States. AIMU has worked closely with the United States Coast Guard (the "Coast Guard") for decades in connection with maritime safety and prevention issues.

WQIS, where I serve as President, is a pool of 17 American marine insurers that has insured liabilities arising from federal statutory provisions for the last 25 years. WQIS is the largest domestic insurer of federal marine pollution liabilities, and supplies 28% of all COFRs issued under the Oil Pollution Act of 1990, ("OPA '90") and the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"). Of the certificates based on insurance, WQIS provides the evidence of financial security for about 40% of the COFRs. We insure liabilities arising from oil or hazardous substance spills for over 39,000 vessels operating primarily in the inland and coastal waterways of the United States.

In addition, through the Maritime Response Syndicate, WQIS provides a full range of spill management services, utilizing state-of-the-art technology to assist our assureds in efficient and effective incident response. We believe that the prompt, expert response capabilities which WQIS makes available to its assureds makes a substantial contribution to the preservation of the marine environment. Most of our assureds are small to mid-sized companies. Most of their fleets are from three to thirty vessels. Many of our assureds are small businesses that do not have the personnel to effectively manage a pollution incident. Consequently, WQIS organized the Maritime Response Syndicate to provide our assureds with state-of-the-art clean-up technologies. Since OPA's enactment, WQIS has responded to a thousand spills and we are pleased for the opportunity to share our experiences with the Committee.

WQIS has worked closely with the Coast Guard to implement the COFR regulations. The American Marine Insurance Market has unfailingly cooperated with COFR requirements for a quarter of a century. We are pleased to report that the Coast Guard staff has been fair, capable and genuinely helpful in administering the COFR process. In the course of our substantial involvement in insuring federal pollution liabilities we have

had the opportunity to observe the ramifications of the Coast Guard's COFR regulations under OPA '90, and to recognize some problems inherent in the law and the regulations that impact on our ability to provide certificates.

The Committee has asked for comments on the cost of the COFR requirements on the maritime industries. WQIS has not charged any additional premium for providing the evidence of financial responsibility upon which the Coast Guard relies to issue certificates of financial responsibility. We provide the evidence necessary for the certificates as a service to our assureds. As long as we are able to limit clearly our liabilities as guarantors and to anticipate the costs of providing the cover so that we can collect sufficient premiums, we hope to be able to continue our services to our assureds.

Premiums are based on loss experience. We factor in elements, such as carriage of crude oil, which result in higher clean-up costs. We also offer a premium reduction for vessels with double-hulls. Nevertheless, we remain concerned about certain aspects of OPA '90 and its implementation, which in the future may jeopardize our continuing ability to cooperate with the COFR requirements.

Policy Defenses

Although Section 1016(e) of OPA '90 allows the Coast Guard to specify the policy terms, conditions and defenses available to the insurer, the COFR regulations do not specify even the most basic defenses. Consequently, two of the most important defenses, fraud and misrepresentation by the assured, are not available. In effect, should the assured misrepresent the tonnage of a vessel, or the nature of its cargo, the insurer will bear the burden of this misrepresentation in the event of a spill. This limitation on the defenses of the insurer goes against one of the core principles of the marine insurance industry -- the duty of the assured to act in good faith. Holding the insurer responsible for the misrepresentations of the assured is unduly burdensome and contravenes the intent of Congress. The express language of OPA '90 allows the Coast Guard to recognize the defenses of fraud and misrepresentation, yet they remain unavailable to insurance underwriters.

Conflicts Between Jurisdictions

Conflicting state regimes continue to put unnecessary burdens on maritime commerce. OPA '90 should provide a uniform liability and compensation scheme. We remain concerned about the potential for conflicts among jurisdictions in resolving OPA '90 claims. Matters which are litigated under OPA '90 should go before a federal court, not a state court. Traditionally, maritime matters are heard by federal judges and OPA '90 is a federal statute applying to vessels in interstate and international commerce. In the event that a spill affects claimants in more than one jurisdiction, we are concerned about conflicts among various courts. We urge that a procedure be devised whereby claimants could be brought before one court (referred to as concursus).

Application to Demise Charterers

In contravention of OPA '90, the COFR regulations also require the insurer to cover the activities of not only the owner and operator of the insured vessel, but also any

subsequent charterer. Section 101(2) of OPA '90 clearly defines a vessel owner or operator as "any person owning, operating or chartering by demise." In contrast, the COFR regulations require that the certificate cover "vessel owners, operators, and demise charterers." This difference in wording could have a considerable impact upon marine insurers. The insurer can readily assess the dependability and safety-mindedness of any given owner or operator identified at the time of contracting, and then adjust premiums accordingly. The problem comes when an identified owner hands off the vessel to an unknown charterer. Even though the charterer may pose an unacceptable insurance risk, the insurer is obligated under COFR regulations to cover the vessel until 30 days after issuing a notice of cancellation. The insurer thus has no opportunity to assess the risk posed by the unidentified charterer assuming control of the vessel, yet is expected to cover any ensuing liability. This is patently unfair, and makes it impossible for insurers to predict potential exposure with any sort of certainty.

Clarification of Limitation Needed

We remain concerned about one especially confusing provision in OPA '90. When a guarantor undertakes clean-up on behalf of a responsible party, it is possible in large spills that the limit certified to the government may not suffice. There may be other resources of the responsible party or of the Fund which should respond for the clean-up process at higher levels. At such a point, the guarantor on the certificate is in a quandary. If he attempts to hand over the clean-up to the Coast Guard, would that violate the responsible party's obligation to cooperate with the on-scene coordinator? This uncertainty creates a needless impediment to a smooth transition in large spills. We urge that OPA '90 be clarified to permit a guarantor to hand over spill responsibility when the certified limit is reached.

Financial Responsibility and NRDAs

In February of this year, the National Oceanic & Atmospheric Administration ("NOAA") issued a new set of OPA '90 regulations that affect insurers providing COFRs. These new regulations allow an appointed trustee to conduct a natural resource damage assessment ("NRDA"), a quasi-scientific process whereby the damage to a natural resource is calculated, quantified, and assessed against the responsible party.

We believe that our nearly 25 years of experience cooperating with the Coast Guard by meeting financial responsibility requirements puts WQIS and AIMU in a unique position to comment on natural resource damage assessments under OPA '90. The dangers posed by potentially excessive and arbitrary assessments present the most serious threat to our ability to continue to insure liabilities under these federal pollution statutes. Rapidly escalating costs associated with assessments for natural resource damages will undermine our continuing ability to provide the financial responsibility required of vessels under OPA '90.

The prospect of high natural resource damage assessments being imposed in virtually every pollution incident casts a dark shadow over the maritime industries. Lack of control over the scope and cost of assessments to be imposed will increase the economic burdens on maritime industries. Despite warnings from industry and scientists, NOAA

will now permit trustees for natural resources to impose assessments utilizing methods which are not scientifically proven. WQIS fears that the unnecessary costs associated with the assessments could well drive smaller operators out of business.

We estimate that the cost of removal and damages associated with a spill are as much as ten times greater since the enactment of OPA '90, but that estimate does not even include NRDA costs. These rapidly increasing clean-up and claims costs have been imposed upon a financially troubled commercial maritime industry in the United States. That industry can ill-afford to pay additional exorbitant assessments for losses which cannot be demonstrated or properly measured. The problems with NRDAs are well documented.

Our major concerns are:

- **No Meaningful Standards**. NOAA's rule does not impose any meaningful standards for calculating assessments. The regulations allow use of virtually any method, no matter how unproven or speculative. The net result will be skyrocketing costs at a time when the maritime industries cannot afford it.
- **Speculative Claims Permitted**. Shipowners and operators will be required to pay assessments for "values" assigned to highly speculative "losses." For example, an individual hundreds of miles from an incident, completely unaware of the existence of the affected natural resource, might be asked in a survey to assign a value to the loss of "non-use" of the affected resource. Such values could be multiplied by the entire population to arrive at exorbitant assessments for "lost non-use." Such theoretical "damages" for non-use have no place in a statutory assessment procedure.
- **Costs May Be Unlimited**. NOAA's rule ignores the limitation of liability that shipowners and operators have under OPA '90. Not only may costs be excessive, but there is also no finality with respect to any assessment because restoration projects are to be monitored and may be reopened years later.
- **No Control Over Trustees.** The rule imposes no restraints on trustees, who have an inherent interest in increasing and recovering their own expenses in connection with assessments. Trustees can undertake costly studies and incur considerable expense over months or years without even notifying the party who will be asked to pay for the assessment.
- **Assessment Methodologies Are Flawed**. NOAA's rule will permit trustees to utilize virtually any unproven method to make assessments. One of the methods of assessment permitted by the regulations is a "literature-based method." Apparently, if an article is written on a so-called method of assessment, that "method" may be used, no matter how unscientific. The problems with one assessment method -- the computer model -- have been well documented. For instance, a ten gallon spill could lead to assessments of $1.28 million. Despite these incredible results, NOAA has sanctioned the use of the computer model. There are other "simplified" methods of assessment which trustees may use, even though it has been shown that they also produce results which bear no connection to the severity of the incident.

- **Trustees' Assessments Are Presumed Correct**. If a responsible party wants to challenge the assessment imposed by a trustee, the court will presume that the trustee's actions were correct. It will be very difficult to challenge an assessment, no matter how speculative or scientifically unproven the methodologies used are. The "rebuttable presumption" should not be accorded to assessments until we have more experience with restoration and valuation methods.
- **Checks and Balances Are Needed.** Under NOAA's regulations, trustees have an inherent conflict of interest. It is their own budgets which will be funded by the assessments. There is no legislative or budgetary oversight, yet trustees can incur and collect considerable administrative expense. Limits and controls are necessary to prevent the squandering of NRDA funds collected. The trustees' unchecked power to collect damages, presumed to be correct, is very troubling. Potential regional plan projects, such as construction of beach parking lots and walkways, are normally subject to the appropriation process. Maritime industries have good reason to fear arbitrary actions by administrative agencies imposing exorbitant assessments outside of the normal budgetary process.

  This unchecked power of administrative agencies or trustees to assess and collect damages is disturbing to those subject to "assumed" damages with little or no recourse. The fear of being forced to pay unreasonable damage assessments is very real. By way of example, an assured of WQIS was recently involved in a spill of caustic soda in a river located in a commercial area. There was no fishkill nor was there any sign of damage to the environment. Because the substance is water-soluble and dissipates, it raised the pH level around the barge, but 100 yards from the area of the spill the water was safe. There was no demonstrable damage to any natural resource. No NRDA process was begun. Nevertheless, we were presented with a bill for $250,000. Only if we were willing to discuss settlement, would information on the basis for the assessment be provided to us, we were told. This failure to provide the NRDA violated the regulations and the law. NRDA reform is necessary. The maritime industry has good reason to fear this sort of arbitrary action by administrative agencies imposing exorbitant assessments. There must be some checks and balances.

The funds available to pay for natural resource damage assessments are not unlimited. Exorbitant assessments result in unnecessary financial burdens which simply cannot be borne by the maritime industry. Under NOAA's regulations, much of the cost of the assessments will not be applied towards restoration of impacted resources, but rather towards creating and nurturing yet another government bureaucracy. This will divert scarce resources away from the intended goals of OPA '90. There is no doubt that Congress wanted OPA '90 assessments to be used for the actual restoration or replacement of impacted natural resources, not to pay for burgeoning administrative and transactional costs driven by trustees acting without appropriate controls.

Thus, the lack of certainty inherent in NRDAs poses a severe threat to maritime insurers' continuing ability to provide evidence of financial responsibility under OPA '90. Where once costs and premiums could be estimated by studying past claims, NRDAs remove

any semblance of predictability. The possibility that an insurer could be compromised by an excessive assessment is a real one, and ultimately must affect the ability of insurers to provide financial responsibility for vessels.

Both the COFR and the NRDA regulations must be changed to provide the maritime insurance industry with a certain, fair and reliable basis for calculating risk. AIMU and WQIS are grateful for the opportunity to present their views here today, and would be pleased to provide any additional information that the Committee requires.