88-11

Department of Justice

FOR IMMEDIATE RELEASE
THURSDAY, NOVEMBER 17, 1988

AT
202-633-2016
(TDD) 202-786-5731

The Department of Justice announced today that it has advised the American Steamship Owners Mutual Protection and Indemnity Association Inc., commonly known as the American Club, that the American Club's plan to become a member of the International Group of Protection and Indemnity Clubs and a party to the International Group Agreement would not by itself significantly reduce competition and would have no effect upon the Department's enforcement intentions as to the International Group.

The Department's position was stated in a letter from Charles F. Rule, Assistant Attorney General in charge of the Antitrust Division, to counsel to the American Club. The American Club had asked the Department for a business review letter stating the Department's enforcement intention if the American Club joined the International Group and became a party to the International Group Agreement.

The American Club is a non-profit association that provides marine protection and indemnity insurance to its members, who are primarily United States ship owners and operators. Seventeen other associations located in other countries throughout the world provide such insurance to their members. These other

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Location: Washington DC

associations have joined together to form the International Group, which provides reinsurance to its member associations.

The American Club is the only association of its kind that is not a member of the International Group. Members of the International Group provide as much as 99 percent of all marine protection and indemnity insurance worldwide.

United States ship owners are free to join associations that are members of the International Group, and some have done so. The American Club wishes to join the International Group in order to reduce its members' costs of obtaining insurance, the Association said in its request for the business review. The request stated that the American Club may lose some of its members if it does not join the International Group.

Rule's letter noted that the Department's business review procedures provide for the statement of enforcement intentions only as to proposed business conduct. Since the activities of the International Group are ongoing, he said, the business review letter cannot comment on that conduct, nor can the Department state its enforcement intentions as to the American Club if it chooses to join in such ongoing conduct.

The letter stated, however, that the Department's enforcement intentions as to the activities of the International Group would not be significantly affected by the American Club's decision to join, or not to join, the International Group. The

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letter concluded that participation in the International Group by the American Club probably would not enhance whatever market power the International Group might already have, if any, which is a critical factor in any antitrust analysis of a joint venture like the International Group.

The letter emphasized that the Department was not stating any enforcement intention with respect to the International Group and its members.

Under the Department's business review procedure, an organization may submit a proposed course of action to the Antitrust Division and receive a statement as to whether the Division would challenge that action under the federal antitrust laws.

A file containing the business review request and the Department's response may be examined in Room 3233, Antitrust Division, U.S. Department of Justice, Tenth Street and Pennsylvania Avenue, N.W., Washington, D.C. 20530 (telephone: 202-633-2481). After a 30-day waiting period, the documents supporting the business review will be added to the file.

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88-463

Antitrust Division

Office of the Assistant Attorney General

Washington, D.C. 20530

NOV 16 1988

Bruce A. McAllister, Esquire
Mishkin & Gleiner
30 Rockefeller Plaza
45th Floor
New York, NY 10112

Re: Request for Business Review Letter:
American Steamship Owners Mutual Protection
and Indemnity Association, Inc.

Dear Mr. McAllister:

This letter responds to your request of April 4, 1988, for a statement, pursuant to the Antitrust Division's Business Review Procedure, of the current enforcement intentions of the Department of Justice with respect to the proposal of the American Steamship Owners Mutual Protection and Indemnity Association, Inc. ("American Club") to become a member of the International Group of Protection and Indemnity Clubs ("IG") and a party to the 1985 International Group Agreement ("IGA").

We understand the relevant facts to be as follows. The American Club is a non-profit association located in the United States that provides marine protection and indemnity insurance ("P&I insurance") to its members, who are primarily United States shipowners and operators. Seventeen other associations located in other countries throughout the world provide P&I insurance to their members. These other associations have joined together to establish the IG, which provides reinsurance to its member associations pursuant to the provisions of the IGA. The IGA contains provisions which, among other things, limit the ability of member associations to reduce their rates for P&I insurance in order to attract new members.

You have represented that the American Club or the IG and its member associations provide virtually all marine P&I insurance. The American Club provides approximately one percent of marine P&I insurance, and the IG and its members provide approximately 99 percent of marine P&I insurance. You have stated that the share of marine P&I insurance provided by the American Club has declined in recent years, and that American shipowners and operators can and do join associations other than the American Club to obtain their marine P&I insurance. The American Club wishes to join the IG in order to reduce its members' costs of obtaining marine P&I insurance. The American Club believes that if it does not join the IG, some of its members will leave to join associations that are already members of the IG.

As you know, the Department's Business Review Procedure was adopted to serve a limited purpose: to inform parties of the Department's present enforcement intentions "with respect to proposed business conduct," 28 C.F.R. § 50.6, ¶ 2 (emphasis added). The Department does not provide advisory opinions to parties and does not use the business review procedure to state its enforcement intentions regarding ongoing, rather than proposed, conduct. Because of these limitations, the Department cannot state its enforcement intentions regarding the ongoing conduct of the IG and its members. Similarly, we cannot state our enforcement intentions as to the American Club if it chooses to join in such ongoing conduct.

We are able to state, however, that our enforcement intentions regarding the IG and its members will not be significantly affected by the American Club's decision to join, or not to join, the IG. In general, a joint venture violates the antitrust laws only if it creates, enhances, or facilitates the exercise of market power by the joint venture participants. Based upon your representations, it appears unlikely that the participation of the American Club would significantly enhance whatever market power the IG may already possess. It also appears unlikely that if the participants in the IG now have market power, the participation of the American Club would have any significant affect on their ability to exercise such power. In short, it does not appear that competition from the American Club appreciably constrains the business behavior of the IG and its members, or that the current degree of competition would be significantly reduced if the American Club joins the IG. For that reason, a decision by the American Club to join the IG would not, in and of itself, be determinative of the Department's enforcement intentions as to the IG and its members. We emphasize, however, that this letter is not intended to state the Department's enforcement intentions with respect to the IG and its members. Moreover, if the Department

ever chose to challenge any agreement among the members of the IG under the antitrust laws, the American Club, if it joins in such agreement, could be subject to such enforcement action.

Your business review request and this letter will be made publicly available immediately. Any supporting data will be made publicly available within 30 days of the date of this letter unless you request that any of the materials be withheld pursuant to subparagraph 10(c) of the Business Review Procedure.

Sincerely,

Charles F. Rule
Assistant Attorney General

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April 4, 1988

Charles F. Rule, Esq.
Assistant Attorney General
Antitrust Division
United States Department of Justice
Tenth & Constitution Avenue, N.W.
Room 3107
Washington, D.C. 20530

Re: Request for Business Review Letter: American Steamship Owners Mutual Protection and Indemnity Association, Inc.

Dear Mr. Rule:

Pursuant to the Antitrust Division's Business Review Procedure set forth at 28 C.F.R. § 50.6, this letter is written on behalf of the American Steamship Owners Mutual Protection and Indemnity Association, Inc. (the "American Club") to request a statement of the Division's present enforcement intention regarding the American Club's proposal to become a party to the 1985 International Group Agreement (the "IGA") and a member of the International Group of P & I Clubs (the "IG"), and thereby gain access to beneficial arrangements for the pooling of risks and the purchase of reinsurance. (A copy of the IGA is attached hereto as Exhibit A.)

Introduction

The American Club is the only mutual association located in the United States insuring marine protection and indemnity risks. The American Club is controlled by its members, primarily United States shipowners and operators, who share on a not-for-profit basis their contractual,

third-party, and certain other legal liabilities (all of which are referred to collectively as "protection and indemnity" liabilities) arising from the operation of their ships. The American Club proposes to become a party to the IGA, in anticipation of participating in the IG's favorable pooling and reinsurance arrangements. These arrangements would allow the American Club to offer greatly enhanced insurance coverage to its members, including previously unavailable oil pollution coverage, and substantially reduce its reinsurance costs.

The American Club believes that its proposed conduct is exempt from the federal antitrust laws pursuant to Section 29 of the Merchant Marine Act of 1920, 46 U.S.C. §885.* That statute specifically exempts cooperative insurance activities undertaken by marine insurance companies authorized to write insurance under state law. Because the American Club is authorized to write marine insurance under the laws of New York and, as demonstrated herein, its proposed activity involves the apportionment of risks among members of an association, the American Club and its intended conduct fit the Merchant Marine Act exemption precisely. Moreover, the benefits the American Club seeks to achieve by becoming a party to the IGA, and gaining access to the pooling arrangements discussed below, are wholly consistent with the

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* Section 29 states:

(a) Whenever used in this Section -

(1) The term "Association" means any association, exchange, pool, combination, or other arrangement for concerted action; and

(2) The term "marine insurance companies" means any persons, companies, or associations, authorized to write marine insurance or reinsurance under the laws of the United States or of a State, Territory, District, or possession thereof.

(b) Nothing contained in the "antitrust laws" as designated in Section 1 of the [Clayton Act,] shall be construed as declaring illegal an association entered into by marine insurance companies for the following purposes: To transact a marine insurance and reinsurance business in the United States and in foreign countries and to reinsure or otherwise apportion among its membership the risks undertaken by such association or any of the component members.

statute's goal of strengthening the American marine industry.

Although the American Club is firmly convinced that the Merchant Marine Act exemption applies here, the statute has little interpretative history. Thus the American Club has presented below alternative grounds for a favorable Business Review Letter. If the Division agrees that the exemption applies to the American Club's proposed conduct, the alternative grounds presented herein need not be considered.

The present parties to the IGA are seventeen protection and indemnity associations, which together constitute the London-based International Group. Each of the seventeen associations is a mutual Club whose members are owners or operators of ships who, like the members of the American Club, share on a not-for-profit basis their protection and indemnity risks. The members of the Clubs are the sole consumers of the insurance and reinsurance provided by the Clubs. The Clubs in the IG have arrangements for the pooling of the major protection and indemnity risks of their members. These arrangements enable the Clubs to provide to their members at very low cost a breadth and level of coverage that is not available from commercial insurers. Adherence to the IGA is a prerequisite to participating in the IG's pooling and reinsurance arrangements.

All but one of the IG Clubs are located in Europe or have managers' agents in Europe; none is located in the United States. Moreover, the largest single grouping of tonnage insured by the IG consists of European-flag vessels. Less than 5 percent of the tonnage in the IG is United States flag, an amount that would increase slightly to less than 6 percent with American Club participation.

The IGA has already been approved by the Commission of the European Communities, which rendered its decision on December 16, 1985, after extended consideration.* As is clear

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* A copy of the December 16, 1985, Commission Decision ("EC Decision") approving the IGA is attached hereto as Exhibit B. A copy of the IG's initial submission to the European Commission in June, 1981, presenting the 1981 version of the IGA ("Memorandum to EC") is attached hereto as Exhibit C.

Copies of the 1981 IGA and the Memorandum to EC were

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from the EC Decision, the Commission has also undertaken responsibility for continuing oversight of the operation and effect of the IGA. The principles applied by the European Commission are broadly similar to those applied in analyzing the competitive effects of arrangements or practices under the antitrust laws of the United States. Applying these principles in its 1985 Decision, the Commission found the provisions of the IGA "indispensable" to achievement of the important benefits and efficiencies of the Clubs' mutual protection and indemnity insurance system, including, in particular, their pooling arrangements. As the Commission stated, "There is a strong likelihood that prohibiting the IGA would have harmful effects on the mutual insurance system itself as operated for over a century by the Clubs." EC Decision ¶56.

Given the similarity between the principles applied by the EC and the principles of U.S. law, and the Commission's ongoing oversight of the IGA,* the American Club respectfully suggests that the Antitrust Division should permit it to share the benefits of the IGA and the pooling arrangements to which it seeks access.

Protection and Indemnity Insurance

Shipowners customarily purchase for their ships both "hull and machinery" insurance, and insurance against many kinds of contractual, third-party and other legal liabilities arising from the operation of their ships, referred to in the industry as "protection and indemnity ("P & I") risks." P & I risks are notable for their variety. The dangers to which ships are exposed vary with the types of trade in which they are engaged and the cargoes they carry, and can range from small, relatively frequent claims arising from cargo damage, crew injury and damage to other ships or port installations, to large but infrequent claims arising from oil spills or from explosions resulting in heavy loss of life and substantial property damage. P & I coverage also extends to losses and expenses unique to the maritime trades, including those arising from stowaways, ship quarantines,

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provided to Charles S. Stark, Chief, Foreign Commerce Section of the Antitrust Division, in a meeting at the Department of Justice in July, 1981. A letter to Mr. Stark following that meeting is attached hereto as Exhibit D.

putting in to land with injured or sick seamen, and removal of wrecks.

P & I claims are also notable for their "long tail." Long tail liabilities arise from claims that may not be discovered, let alone settled, for many years after the policy year in which they arose. Experience has shown that forty percent of claims involving a Club's members can remain unsettled by the fifth year after the policy year to which they were attributable, some because they remained in litigation, and others because they had not yet even been presented.

Protection and Indemnity Clubs

Whereas owners of large ships usually place their hull and machinery insurance with commercial insurers, their P & I risks are almost invariably insured with Protection and Indemnity Clubs ("P & I Clubs"). P & I Clubs are associations of owners, charterers, operators and managers of ships who share each other's P & I risks on a mutual, not-for-profit basis. Because there is no profit element, a P & I Club member's contributions consist only of his share of the total amount required to meet the liabilities of all members of his Club, of the Club's pooling and reinsurance costs, and of the costs of the Club's administration.*

Members contribute to their P & I Clubs in the following manner. Before the beginning of a particular policy year (which begins for most Clubs on February 20), the Club estimates its total cost for that year, including the liabilities of its members, the cost of pooling and reinsurance, and the cost of administration. The Club then decides what proportion of its total cost is to be borne by

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* The Clubs' administrative expenses are much lower than those of commercial insurers. According to the 1987 edition of Best's Aggregates and Averages, the administrative expenses of United States commercial insurers insuring ocean marine risks averaged 28.9% of their premium income during 1977-1986. By contrast, the Clubs' overheads and expenses averaged approximately 7.5% of their contributions from members. Yet the Clubs also carry out certain additional functions, such as claims handling, which, in the case of commercial insurers, may be handled by brokers.

each member. This exercise is known as "rating," since the amount payable by each member is expressed as a rate per gross registered ton of each vessel entered in the Club. During the policy year, each member makes an initial contribution (an "advance call") toward the Club's estimate of its total cost for that year. The advance call can represent a small or a large portion of the estimated total cost, depending on the Club's cash management procedures. The member remains liable to make one or more additional contributions to his Club, known as supplementary calls or assessments, if the Club's actual costs for that year exceed the members' initial contributions and the investment income earned by the Club. Conversely, if a Club's actual costs are less than the funds available, the Club may make an appropriate return of contributions to its members. Although a Club has the option of setting low advance calls, in the final analysis this has no impact on the total cost shared by the members of that Club.

The principle of mutuality on which P & I Clubs are founded requires Clubs to establish fair and equitable relationships among their members in determining their rates. A benefit or advantage gained by one member, whether by means of an unjustified reduction in his rate or by some other means, is necessarily and directly a detriment to the remainder of the Club's members. This is a fundamental difference between the operations of P & I Clubs and those of commercial insurers. Commercial insurers owe no duty to their insureds to rate them equitably in relation to each other, and an unjustified increase or reduction in a rate to an insured merely affects the level of the commercial insurer's profit. By contrast, in mutual Clubs, rates must be established without preference to any one member or class of members, and Club managers must be bound to uphold the equity among Club members.

The Market for Mutual Protection & Indemnity Insurance

The vessels insured by P & I Clubs fall into two categories. First, and primarily, the Clubs insure P & I risks for large ocean-going ships, known as "blue water" ships. Virtually all blue water P & I coverage in the world is provided through not-for-profit mutual Clubs. The very large risks, potentially heavy losses, and long tail liabilities characteristic of P & I claims have caused commercial companies, which sell fixed-premium insurance, to withdraw over the years from offering P & I coverage for blue water ships.

Second, P & I Clubs may insure "brown water" vessels, although virtually all P & I coverage for these vessels is purchased from commercial companies for fixed premiums. Brown water vessels are designed to perform all manner of tasks other than open ocean transportation of cargo and passengers. These vessels, primarily tugboats, barges, oil-rig service vessels and other special-design boats, are named after the muddy character of the river, harbor and coastal waters in which they operate. Typically, they are smaller than blue water ships, carry smaller cargo and crews, and do not traverse the long distances travelled by blue water ships. Their smaller size and limited geographic range, and hence their generally smaller claims, eliminate the need for the high limits required by blue water ships, and make insurance of these vessels attractive to the commercial profit-making companies.

The American Club

Since its creation in 1917, the American Club has been the only mutual, not-for-profit P & I Club in the United States. Until 1980, its membership was composed only of United States shipowners and operators. The entered tonnage in the American Club was approximately 4.33 million gross registered tons in 1987. It provides P & I insurance to less than 1 percent of the world's blue water tonnage; for the remaining 99 percent, virtually all P & I insurance is provided by IG Clubs.

The American Club's share of the market for brown water P & I insurance is insignificant. The American Club estimates its income from brown water P & I insurance for United States flag vessels at $2.3 million, or less than 2.3 percent of the net premium earned by U.S. companies for brown water P & I insurance.*

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* Although it has not been possible to obtain market-wide premium figures for brown water P & I insurance, experts in ocean marine insurance believe that P & I insurance for brown water vessels accounted for 10 to 20% of the approximately $1.19 billion in net earned premiums written by U.S. commercial insurers for ocean marine insurance in 1986.

In recent years, the American Club has provided to each of its members P & I coverage of at least $100 million per accident or occurrence. For the four policy years 1984/85 through 1987/88, the American Club retained the first $1 million per accident or occurrence above the member's deductible, and purchased reinsurance to cover claims exceeding the $1 million retention. In addition, the American Club made available, at cost to those members who sought it, additional insurance up to a maximum of $375 million per accident or occurrence.* The American Club has not offered oil pollution coverage to tanker owners** because it can spread these risks only over its own low tanker tonnage, which makes the cost of reinsurance prohibitively expensive.

The International Group

Thirteen IG members are based in Europe, three are based in Bermuda with managers' agents in Europe, and one is based in Japan.*** Most of the Clubs were established in

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* For the policy year 1988/89, the American Club has been able to make some additional coverage available to its members under a temporary reinsurance arrangement with certain member Clubs of the IG while the American Club seeks a favorable Business Review Letter. This temporary arrangement, which expires on February 20, 1989, does not enable the American Club to participate in the IG's pooling or reinsurance arrangements, nor does it require compliance with the IGA.

** The American Club's oil tanker members are among the members of the International Tanker Indemnity Association ("ITIA"). ITIA, which is based in Bermuda, is a not-for-profit mutual which provides only oil pollution insurance for tanker owners.

*** The following associations are Members of the International Group of P & I Clubs: The Britannia Steam Ship Insurance Association Limited, The London Steam-Ship Owners' Mutual Insurance Association Limited, Newcastle Protection and Indemnity Association, The North of England Protecting and Indemnity Association Limited, The Shipowners' Mutual Protection and Indemnity Association (Luxembourg), The Standard Steamship Owners'

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England in the middle of the 19th century to insure British shipowners. The Clubs created opportunities to spread P & I risks over enough tonnage to make available P & I insurance covering a broad range of risks at predictable and affordable costs. As the merchant fleets of other nations have grown, the Clubs have adapted to meet the needs of the world's shipowning community, and they now provide a truly international service that insures liabilities incurred by vessels flying the flags of some eighty different countries. It is the nature of such operations that they touch the interests of most countries.

The premise of the mutual insurance offered by a P & I Club is the sharing of liabilities among a Club's members. With a sufficient number of members among whom liabilities can be shared, the impact of large claims on individual members is reduced. The Clubs have a pooling arrangement ("the Pool") through which they share liabilities of any of their members in excess of $1.2 million for each accident or occurrence.**** Thus, any large claim made

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Protection and Indemnity Association Limited, The Standard Steamship Owners' Protection and Indemnity Association (Bermuda) Limited, The Steamship Mutual Underwriting Association Limited, The Steamship Mutual Underwriting Association (Bermuda) Limited, The Sunderland Steamship Protecting and Indemnity Association, The United Kingdom Mutual Steam Ship Assurance Association (Bermuda) Limited, The West of England Ship Owners' Mutual Insurance Association (Luxembourg), Assuranceforeningen Gard (Gjensidig) (of Norway), Assuranceforeningen Skuld (Gjensidig) (of Norway), The Japan Ship Owners' Mutual Protection and Indemnity Association, The Liverpool and London Steamship Protection and Indemnity Association Limited, and Sveriges Angfartygs Assurans Forening (of Sweden).

****Two of the signatories to the IGA are not direct participants in the Pool but have access to the Pool and contribute to it through other IG Clubs with which they are reinsured.

A copy of the current Pooling Agreement, as amended, is attached as Exhibit E. The Pooling Agreement is presently being redrafted to define more clearly certain risks that are not covered by the Pool.

against a Club member is spread not only among the members of that Club but also among the members of all Clubs. To protect the members of the Pool against the consequences of catastrophe, the Pool purchases reinsurance for liabilities in excess of $12 million up to $1.25 billion per accident or occurrence (except oil pollution risks, for which cover is limited to $400 million). The Pooling Agreement calls for the sharing of any claim (except oil pollution claims) in excess of $1.25 billion among the Pool Clubs; these are known as "Overspill" claims.

With the support of the Pool, the excess reinsurance purchased by the Pool, and the Overspill provisions, the Clubs are able to provide virtually all* members with unlimited cover other than for oil pollution. It is highly improbable whether a Club having an independent reinsurance arrangement would be able to purchase the level of protection available to the IG as a whole. Moreover, the volume of tonnage entered with the Clubs is large enough that the cost to their members of the excess reinsurance purchased by the Pool is substantially less per ton than it would be for a Club that sought to cover the same risks for its members on its own. In addition, the broad spread in the Pool means that the cost of P & I insurance to members of the Clubs is reasonably predictable, which is of considerable practical importance to shipowners.

When a Club settles a claim, it seeks reimbursement in accordance with the Pooling Agreement from other members of the Pool and debits the other Clubs for their proportions. Each Club's proportion of the Pool's liabilities is calculated pursuant to a formula including the contributions received by the Club from its members, the tonnage entered in the Club, the Club's claims on the Pool, and the Club's loss ratio with the Pool. A Club's Pool proportion is determined provisionally at the start of each policy year and is not finalized until at least 18 months after the end of the policy year in question.

In addition, because the Clubs are managed for the benefit of their members, the Clubs' Rules (which form the basis of the members' contracts of insurance) allow wide latitude in admitting claims that the Rules may not cover specifically. Such discretionary cover is of particular value

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* Special limits apply to certain entries. (see Paragraph 1.4.7 and 1.4.8 of the Memorandum to EC).

in the maritime industry, where the variety of incidents causing loss is not wholly foreseeable.

The International Group Agreement

The mutual insurance system operated by the IG Clubs is unique and differs markedly from commercial profit-making insurance. To operate successfully, the system needs safeguards to preserve the mutuality between members, the predictability of their contributions, and the equity and trust among the Clubs that is necessary to operate the Pool and permit the allowance of discretionary claims. The IGA provides these safeguards. See EC Decision ¶¶ 33-37, 47.

The IGA seeks to control the temptation of Club managers to enhance their prestige and increase their remuneration (which may be affected by increased tonnage or income or other measures of a Club's size) by quoting discriminatory rates to attract tonnage from other Clubs. When a manager discriminates, his Club receives a lesser contribution than the underwriting history of the vessel or fleet in question would otherwise warrant. This discriminatory rating adversely affects the other members of (the member's) Club because, in a mutual system, any shortfall in meeting the Club's obligations must be made good by its members. In addition, other Pool Clubs may be affected by the offer of such discriminatory rates because, quite apart from the diminished confidence in the good faith and cooperation necessary to operate the system, each Club's share of Pool liabilities is based in part on the Club's total contributions received from its members. Were a Club to receive less than it should from a member, a Club may be assigned too low a share of the Pool's liabilities, and the other Clubs would be assigned disproportionately larger shares.

Further, a Club faced with a discriminatory rate quoted to one of its members by another Club, would have only two choices unless it wishes to abandon the business: either it must destroy the equity among its members by meeting that rate for the vessel or fleet in question, or it must reduce its rates to all members. Although a reduction in rates quoted to all of its members might create the illusion that a Club is offering lower-priced insurance, in a mutual system any underestimate of total costs must be corrected with increased supplementary calls. The quotation of a reduced rate might lead another Club to quote an even lower rate, thus forcing another round of decreased rates that would have to be corrected by even greater supplementary calls. These

illusory lower quotations would benefit nobody (because all liabilities and costs must be shared by Club members) and have the detrimental consequence of rendering the level of supplementary calls less predictable for the vessel owner. Moreover, if unexpected and heavy supplementary calls are imposed, a shipowner may be unable to honor them.

In acknowledgment of the fact that unregulated price competition has no role in the mutual insurance system operated by the Clubs, the IGA contains quotation rules concerning the rates that may be quoted to members when they move vessels between IG Clubs. Each Club, nevertheless, autonomously determines in what proportions its members share the Club's overall liabilities. See EC Decision §36.*

The quotation rules discourage Club managers from quoting discriminatory rates and control systemic underrating by calling for the exchange of certain information between Clubs and providing a check of "reasonableness" on the quotation of rates that could be discriminatory. Before a vessel insured in one Club (the "Holding Club") is offered a new rate by another Club (the "New Club"), the IGA requires disclosure by the Holding Club, with the member's permission, of the member's loss history and of the Holding Club's rate, which reflects its underwriting judgment. Over the years, a Club's underwriter acquires a detailed understanding of matters such as a member's management expertise, the quality of his staff, and the nature of his trade. Disclosure of the Holding Club's rate** applied to the member, which necessarily reflects the underwriter's experience with the member, and his expectations of future claims, materially enhances the New Club's ability to make a proper underwriting assessment

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* It should be noted that the Clubs compete vigorously on the basis of service and the quality and speed of claims handling. This type of competition is fully consistent with principles of mutuality.

** If the New Club's quote is to be made on or before September 30, the Holding Club discloses its current rate. If the quote is to be made after September 30, the proposed renewal rate is disclosed. The European Commission, which selected the September 30 date, found this cut-off essential to the operation of the IG system because, inter alia, of a Club's need to estimate accurately the quality and quantity of its membership in the coming policy year. See EC Decision ¶¶ 48-50.

of the proposed new member, without jeopardy to the equity among its existing members or among the Clubs in the Pool.

Once the New Club has requested and received the member's record and the Holding Club's rate, it can negotiate a new rate with him. If the New Club then enters into a binding commitment with the member, it must inform the Holding Club of the new rate within three days. The member is free to join the New Club at the New Club's rate but, if the commitment is made before September 30, the Holding Club may invoke the authority of the IG's "Committee" for a determination whether the new rate is discriminatory, i.e, "unreasonably low." If the Committee finds that the rate is unreasonably low, then claims made against the vessel entered in the New Club will not be fully recoverable from the Pool or its reinsurance. This is referred to in the IGA as a "Reduced Pooling Facility." See infra at page 15.

On the other hand, if the member and the New Club do not enter into a commitment at a new rate until after September 30, the member is free to enter the vessel in the New Club, but if the New Club's rate is lower than the Holding Club's rate, the Holding Club may invoke the authority of the IG's Committee for a determination whether the Holding Club's rate is "unreasonably high."* If the Committee determines that the Holding Club's quotation was not unreasonably high, but the member nonetheless has entered the vessel in the New Club, then, as discussed infra at page 15, claims made against

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* The European Commission created the distinction between the determinations to be made by the Committee before and after September 30, finding, inter alia, that this distinction effects a reasonable compromise between the legitimate interests of the Clubs in maintaining some stability of membership (which facilitates accurate rating and orderly management of supplementary calls), and the free movement of operators between Clubs. See EC Decision ¶¶48-50.

the vessel will be subject to the Reduced Pooling Facility.*

The IGA also provides that Clubs distribute information among themselves about their underwriting experience of tankers. It is a precondition to pooling tanker losses that adequate provision be made for tanker claims. Compared to dry cargo vessels, tankers are subject to casualties that occur infrequently but, when they do occur, are often of disastrous proportions. Tankers thus pose peculiar difficulties for Club underwriters, because the infrequent losses they incur are generally not sufficient to provide underwriters in any one Club with the broad exposure to claims necessary to make accurate assessments of tanker risks. In addition, recent developments in oil pollution legislation have led to continued expansion of the potential claims to which a tanker owner is exposed. Because these factors may lead to serious underrating of tankers,** the IGA requires that tanker rates make fair and adequate provision for the following elements of estimated total cost: the tanker's claims within the Club's retention, its contribution to Pool claims, its contribution to the cost of excess reinsurance, and to administrative costs. In addition, the Clubs collectively recommend the minimum provision required for Pool claims annually and exchange statistical information on tanker claims. If a Club believes that the rate offered for a tanker by another Club fails to cover these cost elements, it may request review by the Committee. If the Committee determines that the rate is too low, the quoting Club is allowed only limited access to the Pool for claims made against that vessel for one year. See infra at page 15.

The IGA also makes available an additional procedure for the "Release Call" that a Holding Club may, if it elects,

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* The IGA provides that similar procedures apply where P&I insurance is sought by an owner or operator for a newly-acquired vessel. If that owner's or operator's existing fleet is already insured by one or more IG Clubs, each is treated as a Holding Club and is required to provide the requested information for the existing fleet. Each is also treated as a Holding Club for the purpose of reviewing rates when the owner or operator is considering entering the newly-acquired vessel in the New Club.

** This indeed occurred before the Clubs identified this problem and took measures to correct it. See paragraphs 5.4.3 to 5.4.5 of the Memorandum to EC.

make upon transfer of a vessel to another Club. A Release Call represents the member's anticipated supplementary contributions to the Holding Club and extinguishes the member's obligation to pay the Holding Club's future supplementary calls. The IGA provides that if a Release Call is required, the member may, at his option, provide a bank guarantee instead of an immediate payment.

The Reduced Pooling Facility is the only penalty imposed for failures to comply with the IGA. Violations of the quotation rules regulating movement among Clubs result in exclusion for two years of the Club that violated the rule from the Pool and the reinsurance purchased by the Pool, but only as to claims related to the vessel directly affected by the violation, and only up to $150 million, or the amount of reinsurance available from other sources. Because the Pool could not function if the Clubs did not treat each other equitably, it is sensible that the sanction should be one that seeks to avoid inequitable burdens on the Pool.

Not even this sanction, however, can be imposed under the IGA, absent a determination by the Committee. The Committee is composed of three members. The procedure for creation of the Committee requires the Club seeking review, and the Club whose rate or conduct is to be reviewed, each to select an individual from a panel of directors, employees or partners of a Club or its managers, each of whom has been previously nominated to the panel by a member Club. The two individuals so selected must not be in any way associated with either of the two Clubs in question. The third Committee member, an individual not associated with any Club or Club manager, is then chosen by the other two members from another panel. The panel from which the third member is selected is composed of persons nominated by not less than three Clubs. The Committee acts as arbitrator in disputes, in accordance with the English Arbitration Acts.

The European Commission Decision and the IGA

The considerations weighed by the European Commission in reviewing the IGA are the same as many of those relevant to the analysis of competition under United States law. Article 85(1) of the Treaty of Rome prohibits all agreements between undertakings which may affect trade between member states of the EEC, and which have as their object or effect the prevention, restriction or distortion of competition within the Common Market. See EC Decision ¶21. The Treaty of Rome, in Article 85(3), permits the European

Commission to approve conduct and grant exemptions from the prohibition contained in Article 85(1) where an agreement contributes to improving production or distribution, passes on to consumers a fair share of the resulting benefit, and does not unduly restrict competition.*

In the EC Decision, the European Commission approved the IGA and exempted it under Article 85(3) of the Treaty of Rome. The European Commission found that the terms of the IGA contribute to an efficient allocation of resources and are essential to achieving the IGA's purposes. The European Commission also concluded that the benefits of the IGA outweigh any effects on competition.

The European Commission carefully scrutinized the IG system and the specific provisions of the IGA discussed above, including the quotation rules, the tanker rating rule, the Release Call rule, and the operation of the Committee. The European Commission found that these provisions strike a permissible balance between competitive concerns and the special needs of a mutual insurance system covering major risks.

Identifying some of the benefits offered by the IG Clubs' system of mutual insurance, the European Commission

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* The pertinent provisions of the Article were summarized in the EC Decision:

> Article 85(3) of the EC Treaty states that the provisions of Article 85(1) may be declared inapplicable in the case of any agreement between undertakings which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:
>
> (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;
>
> (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

See ¶ 30.

stated that the Clubs reduce the insurance costs of their members, provide unlimited cover, provide an excellent and speedy claims-handling system, and provide broad cover by permitting discretionary inclusion of P & I claims that are not expressly covered. EC Decision ¶32.

The European Commission further found that the provisions of the IGA are "indispensable" to four crucial objectives of the operation of the Clubs: continuity of membership; preservation of the principle of mutuality; stability of premiums; and continuation of the pool arrangements. EC Decision ¶33. The Commission observed that continuity of membership is important to enable underwriters to acquire the expertise necessary to rate a member properly, and to permit the Clubs to manage long-tail liabilities efficiently and equitably. EC Decision ¶ 35. The Commission found that rate discrimination could harm Club members and that the IGA's rules were clearly designed to avoid discriminatory rating and transfers of ships between Clubs based on such rates. EC Decision ¶ 35, 47, 53. The Commission also stated that stability in members' contributions is necessary to enable shipowners to forecast their real costs. EC Decision ¶ 36. Finally, the Commission found both that rates that discriminate among members and below cost tanker rates would undermine the confidence and trust between Clubs necessary to continue to operate the Pool. EC Decision ¶¶ 37, 38.

The EC's recognition of the several essential features of the Clubs' mutual system, and the role of the IGA in that system, led the EC to conclude: "Without the rule on quotations, the mutual confidence necessary for the operating of the system would not exist." EC Decision ¶47.

Benefits of American Club Participation

The low level of coverage that the American Club has been able to offer, and its inability to offer tanker pollution coverage, have weakened its competitive position. The blue water tonnage entered in the American Club has declined significantly over the last several years. While this decline reflects in part a decline in the number of ships flying the United States flag, the American Club's ability to respond to the decline has been impaired by the expensive and less than comprehensive coverage it offers.

In 1987/1988, the American Club provided P & I insurance for over thirty United States companies that own

or operate over 1,400 vessels of every type and size. The Board of Directors of the American Club, which consists solely of representatives of these companies, has directed that this request be presented to the Antitrust Division, because the Board believes that the Club's members would enjoy significant benefits from participating in the IG and the Pool. First, the P & I coverage offered to American Club members would be vastly increased. The maximum coverage available through the American Club through 1987/88 has been only $375 million. This vastly enhanced coverage would provide greater protection to the American Club's members and, of course, to those who assert claims against those members.

Second, for the first time in many years the American Club would be able to offer tanker oil pollution coverage.

Third, the American Club, and its members, would gain access to the low cost reinsurance made possible by the Pool. The American Club estimates that in 1988/1989 its excess reinsurance would have cost $7 million were it not for the temporary arrangement it has made for this policy year. In contrast, if the American Club had had access to the Pool for the same year, its estimated cost of reinsurance (for higher limits) would have been only about $4 million. The $3 million savings would have a dramatic impact on the total cost of insurance to the American Club and its members, for whom the cost of reinsurance has recently represented 70 percent of operating and overhead costs (exclusive of claims and brokerage).

The American Club thus believes that through the IG, it would become a competitive choice for the owners and operators of blue water ships seeking P & I insurance, and that its strengthened position would enhance the options of shipowners. The American Club would expect to become a particularly attractive source of P & I insurance to United States flag ships and ships controlled by United States entities. As specialists in the American market and the only P & I Club headquartered in the United States, the American Club could compete favorably on the basis of service, proximity, and claims control, while charging its members premiums as low as are available to most other shipowners in the world.

Considerations of Comity

The American Club believes that, having regard to the presence of most of the Clubs within the EEC and to considerations of international comity, the United States should honor the decision of the European Commission in this matter. Both the courts and the Department of Justice* have demonstrated a growing willingness to honor antitrust policies of foreign enforcement bodies where the conduct subject to enforcement affects foreign individuals and commerce, and where prohibition of the conduct by the U.S. would frustrate the purpose of the foreign policy. This recognition is especially appropriate where the foreign enforcement body, here the European Commission, has conducted a comprehensive and intensive review of the IGA, has negotiated some of its

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* The Ninth Circuit Court of Appeals ruled in Timberlane Limber Co. v. Bank of America, 549 F.2d 597 (9th Cir. 1976) that the exercise of U.S. antitrust jurisdiction should be tempered by a balancing of U.S. and foreign interests, taking into account, inter alia, the nationality of the parties, the relative significance of effects in the U.S. compared with those elsewhere, and the degree to which U.S. antitrust policy conflicts with foreign policy. See also Timberlane Lumber Co. v. Bank of America, 749 F.2d 1378 (9th Cir. 1984). The Third Circuit Court of Appeals cited those same factors as bearing upon whether a U.S. court should decline jurisdiction as a matter of comity in Mannington Mills v. Congoleum Corp., 595 F.2d 1287 (3d Cir. 1979). See also, e.g., Charles F. Rule, Deputy Assistant Attorney General, Antitrust Guide for International Operations: A Progress Report (Oct. 16, 1986), 13th Annual Fordham Corporate Law Institute, Fordham Law School, reprinted in Von Kalinowski, Antitrust Counseling and Litigation Techniques Appendix 14B (1987); Statement by Attorney General Edwin Meese III (Feb. 19, 1986) (Department of Justice Press Release).

The need for governments to consider the extent to which conduct is accept by foreign regulatory bodies has also been recognized by the United Nations. See UNCTAD, The Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices, U.N. Doc. TD/RBP/CONF/10, Section C.6 (1980).

terms, has explicitly approved it, and continues to monitor it.

Conclusion

The American Club believes that the same considerations that led the EC to approve the IGA should lead the Justice Department to recognize the IGA's utility in fostering mutuality, and the efficiencies of permitting expanded P & I coverage at lower cost to shipowners and operators. The American Club respectfully requests that the Justice Department issue a statement that it does not intend to challenge the American Club's proposal to become a party to the IGA, become a member of the IG, and gain access to the Pool.

We would be happy to supply any further information that may be helpful or to answer any questions that may arise.

Thank you for consideration of this request.

Very truly yours,

Bruce A. McAllister, Esq.