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Volume 7

Frank Columbus
Editor

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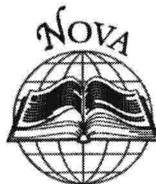

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PREFACE

A continent of vast diversity, stretching from the deserts of the north through the equatorial tropics into the more temperate south, Africa brims with challenges and issues. This book collects a series of papers examining a number of these topics and how they impact African nations, the United States and the global community. The analysis also present possible solutions to some of the continent's most vexing problems as many of its nations chart a course of political and economic development. This book discusses ocean piracy in the strategic waterways in the Gulf of Aden, off the East coast of Africa where hijacking by pirates has focused worldwide attention on economic and humanitarian threats in this region and the troubles affecting Zimbabwe and China's foreign aid activities in Africa through infrastructure and natural resource development projects.

Chapter 1 - Many Members of 111th Congress are concerned about the sharp rise in pirate attacks in the strategic waterways in the Gulf of Aden off the East coast of Africa. The hijacking of a Saudi Arabia-owned oil tanker, *Sirius Star*, off the coast of Kenya on November 15, 2008, by pirates, and its release after a $3 million ransom payment on January 8, 2009, was another in a series of seizures and releases that have focused worldwide attention on economic and humanitarian threats posed by pirates to the global seafaring community and the smooth flow of international trade. Given the sharp increase in the number of pirate attacks, the cost of transporting cargo in international waters could rise dramatically because of the sharp increase in ocean marine insurance rates for ships transiting the Gulf of Aden. Commercial insurers, for example, could require a special "war risk" insurance premium costing an additional ten of thousands of dollars a day. These additional costs could adversely impact international trade during the current global economic slowdown.

In addition to proposals for military deterrence and diplomatic engagements, policymakers may elect to consider adjustments to the federal statute (Title XII of the Merchant Marine Act of 1936, as amended) that authorizes the federal government to underwrite marine war risk insurance in circumstances such as piracy. Title XII, administered by the U.S. Department of Transportation's Maritime Administration, authorizes the federal government to act as an insurer or reinsurer of last resort to facilitate waterborne commerce should private ocean marine insurance markets not be able to ensure that financial losses due to war risks (and piracy) will be largely covered.

Policymakers may also elect to maintain the status quo on this statutory authority. The property and casualty insurance industry policyholder surplus is calculated to be

approximately $505 billion (as of June 2008). Vessel hull and war risk premiums in the U.S. market paid to insurers totaled approximately $350 million in 2007, and the total value of cargo insurance premiums paid in that year was approximately $833 million, according to industry data. Some may contend, as a result, that the insurance industry appears to be financially capable of handling U.S. exposure to the current piracy threat and that the existing policy "backstop" will be adequate.

Chapter 2 - Zimbabwe's prospects appeared promising in 1980, as it gained independence after a long liberation war. Rising inflation and unemployment bred discontent in the 1990s and led in 1999 to the formation of the opposition Movement for Democratic Change (MDC). The new party surprised many with its initial success, campaigning against a 2000 referendum that would have legalized the president's continued rule, made government officials immune from prosecution, and allowed the uncompensated seizure of white-owned land for redistribution to black farmers. The referendum failed, and the MDC won nearly half the seats in the 2000 parliamentary election. The government of President Robert Mugabe has since taken numerous, often undemocratic actions to bolster its power.

President Mugabe's government has been seen in the past decade as autocratic and repressive by its critics, and its human rights record is poor. The government has suppressed freedom of speech and assembly, and many contend that the government has restricted access to food, already scarce, in opposition areas. The MDC, divided over how to respond, split into two factions in 2005, hampering its ability to challenge the ruling party. Reports of political violence rose sharply after Zimbabwe's March 2008 elections, when, for the first time since independence, Mugabe's party lost its majority in the National Assembly. Mugabe's re-election as president in the June runoff was viewed as illegitimate by the United States and the United Nations Secretary-General, among others. In September 2008, after several weeks of negotiations, Mugabe and MDC leader Morgan Tsvangirai signed a power-sharing arrangement aimed at resolving the political standoff. As part of the deal, Tsvangirai became Prime Minister of a new coalition government in February 2009, and cabinet positions have been divided among the parties. Many observers are skeptical that the MDC will be able to implement major reforms through the arrangement, although there has been some initial progress. The cost of rebuilding the economy may be as high as $8 billion.

Zimbabwe's economic output has decreased dramatically since 1998. Official inflation rose above 200,000,000% in 2008, and unemployment is estimated at more than 90%. The adult HIV prevalence rate of 15.3% has contributed to a sharp drop in life expectancy, and three-quarters of the population is expected to require food aid in early 2009. The country has yet to contain a cholera outbreak with over 90,000 infections and over 4,000 deaths. Deteriorating conditions have led many to emigrate to neighboring countries, creating a substantial burden on the region.

Robert Mugabe has enjoyed considerable popularity in Africa as a former liberation leader, but some African leaders have viewed his policies as damaging to the continent and have urged democratic reforms. Following controversial elections in 2000 and citing abuses of human rights and the rule of law, the United States and some other former allies of the government became vocal critics. The United States has enforced targeted sanctions against top Zimbabwe officials and associates since 2002. This chapter provides background on events leading up to the country's most recent elections, in March and June 2008. For further discussion of those elections, the coalition government, and other current events, please see

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CRS Report RL34509, *Zimbabwe: The Power Sharing Agreement and Implications for U.S. Policy*, by Lauren Ploch.

Chapter 3 - In the past several years, the People's Republic of China (PRC) has bolstered its diplomatic presence and garnered international goodwill through its financing of infrastructure and natural resource development projects, assistance in the carrying out of such projects, and large economic investments in many developing countries. This chapter examines China's economic impact in three regions — Africa, Latin America (Western Hemisphere), and Southeast Asia — with an emphasis on bilateral foreign assistance.

China's foreign aid is difficult to quantify. The PRC government does not release or explain Chinese foreign aid statistics and much of PRC foreign aid does not appear to be accounted for in the scholarly literature on foreign aid. Some Chinese foreign assistance partially resembles *official development assistance* (ODA) as defined by the Organization for Economic Cooperation and Development (OECD), but in other aspects shares characteristics of foreign investment. In terms of development grants, the primary form of assistance provided by major OECD countries, China is a relatively small source of global aid. However, when China's concessional loans and state-sponsored or subsidized overseas investments are included, the PRC becomes a major source of foreign aid.

This chapter is based on research done by the New York University Robert F. Wagner Graduate School of Public Service in 2007-2008. The Wagner School study, while not comprehensive, suggests a dramatic increase in PRC foreign aid and related activity. According to the research, which is largely based upon news reports of Chinese foreign economic activity, PRC foreign assistance and government-supported economic projects in Africa, Latin America, and Southeast Asia grew from less than $1 billion in 2002 to $27.5 billion in 2006 and $25 billion in 2007. Aid and related investment to Africa showed the most significant increase. These totals, however, should be interpreted with caution. Some aggregate values may be inflated: Some PRC loans or aid pledges may not have been fulfilled and some aid pledges that include multiple projects or that span several years may have been counted more than once. Some PRC investment activities may more closely resemble FDI than aid. In other ways, totals may be undervalued, such as when economic projects or data have not been reported or when the values of Chinese materials and labor have not been included.

Overall, China's foreign assistance during the past several years has been driven primarily by Beijing's desire to secure and transport natural resources and secondarily for diplomatic reasons. According to the NYU Wagner School study, during the 2002-2007 period, Africa received the greatest amount of loans and development assistance, followed by Latin America and Southeast Asia. The study suggests that China's foreign aid activities in Africa and Latin America serve the PRC's immediate economic interests, while those in Southeast Asia relate to longer term diplomatic or strategic objectives. In Africa and Southeast Asia, Chinese infrastructure and public works projects constitute the most common form of aid, while in Latin America, where some countries are more developed, PRC-sponsored natural resource development activities are more prominent.

China is fast becoming a top trading partner to Africa and Southeast Asia, and it is second to the United States as a market for Latin American commodities and goods. Although the PRC's aid projects are a highly visible reminder of China's growing "soft power," other countries and regions, such as the European Union, the United States, and Japan, continue to dominate foreign direct investment in Africa, Latin America, and Southeast Asia.

Chapter 4 - In October 2008, the forces of the National Congress for the Defense of the Congolese People (CNDP), under the command of General Laurent Nkunda, launched a major offensive against the Democratic Republic of Congo Armed Forces (FARDC) in eastern Congo. Within days, the CNDP captured a number of small towns and Congolese forces retreated in large numbers.

Eastern Congo has been in a state of chaos for over a decade. The first rebellion to oust the late President Mobutu Sese Seko began in the city of Goma in the mid-1990s. The second rebellion in the late 1990s began also in eastern Congo. The root causes of the current crisis are the presence of over a dozen militia and extremist groups, both foreign and Congolese, in eastern Congo, and the failure to fully implement peace agreements signed by the parties. Over the past 14 years, the former Rwandese armed forces and the Interhamwe militia have been given a safe haven in eastern Congo and have carried out many attacks inside Rwanda and against Congolese civilians. A Ugandan rebel group, the Lord's Resistance Army (LRA), is also in Congo, despite an agreement reached between the LRA and the Government of Uganda.

In November 2008, United Nations Secretary General Ban Ki-Moon appointed former Nigerian President Olusegun Obasanjo as his envoy to help broker a peace agreement to end the crisis in eastern Congo. Since his appointment, Obasanjo has met with Congolese President Joseph Kabila, General Nkunda, Rwandan President Paul Kagame, and other officials in the region. The parties have agreed to participate in a U.N.-led peace initiative. The current crisis in eastern Congo has displaced more than 250,000 civilians.

In late 2008, the governments of Rwanda and Congo agreed on a wide range of issues. The two governments agreed to launch a joint military offensive against the National Congress for the Defense of the Congolese People (CNDP) and the Democratic Forces for the Liberation of Rwanda (FDLR). They also agreed to restore full diplomatic relations and to activate economic cooperation. In January 2009, Rwanda and Congo launched the joint military operation in eastern Congo. In late February Rwandese forces pulled out of Congo as part of an agreement reached with Congo.

The United States has been actively engaged in facilitating the Tripartite Plus talks among the four key players in the Great Lakes region: Rwanda, DRC, Burundi, and Uganda. The Tripartite Plus process has led to a number of agreements over the past several years, including the creation of a Joint Verification Mechanism (JVM) to address cross-border issues. The Bush Administration provided an estimated $205.1 million in FY2008, and an estimated $199.7 million for FY2009. The Obama Administration has requested $177 million for FY20 10.

Chapter 5 - In 2003, Rwanda held its first multi-party presidential and parliamentary elections in decades. President Paul Kagame of the Rwanda Patriotic Front (RPF) won 95% of the votes cast, while his nearest rival, Faustin Twagiramungu, received 3.6% of the votes cast. In the legislative elections, the ruling RPF won 73% in the 80-seat National Assembly, while the remaining seats went to RPF allies and former coalition partners. In September 2008, Rwanda held legislative elections, and the RPF won a majority of the seats. Rwandese women are now the majority in the National Assembly. In October 2008, the National Assembly elected Ms. Mukantabam Rose as the first female Speaker of the Assembly. The next presidential elections are scheduled for 2010.

In Rwanda, events of a prior decade are still fresh in the minds of many survivors and perpetrators. In 1993, after several failed efforts, the Rwandan Patriotic Front (RPF) and the

government of Rwanda reached an agreement in Tanzania, referred to as the Arusha Peace Accords. The RPF joined the Rwandan government as called for in the agreement. In April 1994, the Presidents of Rwanda and Burundi, along with several senior government officials, were killed when their plane was shot down as it approached the capital of Rwanda, Kigali. Shortly after, the Rwandan military and a Hutu militia known as the Interhamwe began to systematically massacre Tutsis and moderate Hutu opposition members. In the first 10 weeks of the Rwandan genocide, an estimated 1 million people, mostly Tutsis, were slaughtered by government forces and the Interhamwe militia. In July 1994, the RPF took over power and later formed a coalition government.

In late 2008, the governments of Rwanda and Congo agreed on a wide range of issues. The two governments agreed to launch a joint military offensive against the National Congress for the Defense of the Congolese People (CNDP) and the Democratic Forces for the Liberation of Rwanda (FDLR). They also agreed to restore full diplomatic relations and to activate economic cooperation. In January 2009, Rwanda and Congo launched the joint military operation in eastern Congo. In late February 2009, Rwandese troops pulled out of Congo as part of the agreement with the Kabila government. In October 2009, Ugandan authorities arrested a top genocide suspect, Idelphonse Nizeyimana. He was later transferred to Tanzania to stand trial at the International Criminal Tribunal for Rwanda.

Chapter 6 - After almost a year of uncertainty following Zimbabwe's March 2008 elections, opposition leader Morgan Tsvangirai was sworn as Prime Minister of a new coalition government on February 11, 2009. The new government's establishment came five months after a power-sharing agreement was signed in an effort to resolve the political standoff resulting from the flawed 2008 elections. For the first time since independence, the ruling party has lost its majority in the National Assembly. The results of the presidential race, belatedly announced in May 2008 amid rising tensions, indicated that Tsvangirai had received more votes than the incumbent, President Robert Mugabe, but had failed to garner the 50% needed to avoid a runoff. Days before that runoff was scheduled to take place, in late June 2008, Tsvangirai pulled out of the race, citing widespread political violence and the absence of conditions for a free and fair election. Mugabe was declared the winner in the runoff, but many observer missions suggest the poll did not reflect the will of the people. On September 15, 2008, after weeks of negotiations, Tsvangirai and Mugabe reached an agreement to form a unity government. As part of the deal, Mugabe remains head of state, with Tsvangirai as Prime Minister and cabinet and gubernatorial positions divided among the parties. Disputes over the allocation of key ministries delayed implementation of the agreement. As mediation efforts continued, the United States, the European Union, and several African leaders called for Mugabe's resignation. A final agreement was reached in January 2009, and the new coalition government was established in early February.

The parties to the agreement now face significant challenges in working together to promote political reconciliation and to address serious economic and humanitarian needs. Politically motivated violence and repression followed the March elections, which were held amidst a deepening economic crisis. Zimbabwe's gross domestic product (GDP) has decreased over 50% in the last decade, the inflation rate rose to over 200 million percent in 2008, and the official unemployment rate is over 90%. The adult HIV prevalence rate of 15% has contributed to a sharp drop in life expectancy, and almost three quarters of the population reportedly required food aid in early 2009. Over 4,300 died between August 2008 and July 2009 from a widespread cholera outbreak that infected almost 100,000. Experts suggest a

similar outbreak is likely to occur as the rains return this year. Deteriorating conditions in the country have led many Zimbabweans to immigrate to neighboring countries in recent years, creating a substantial burden on the region. In South Africa, immigrants have been the target of xenophobic attacks. International donors welcomed the January 2009 agreement and have begun a cautious process of re-engagement with the transitional government, but a resumption of significant assistance is expected to be predicated on more substantial political reforms. Many remain skeptical that true power sharing exists within the coalition government. Several officials from the previous administration, which had a poor human rights record and was seen as autocratic and repressive by its critics, remain in the new government. Harassment of opposition and civil society activists continues, and many question the ruling party's commitment to reform.

In 2005, former U.S. Secretary of State Condoleezza Rice labeled Zimbabwe an "outpost of tyranny," and Bush Administration officials accused Mugabe's party of rigging the 2008 election and orchestrating political violence. President Barack Obama and Secretary of State Hillary Clinton have been similarly critical of Mugabe's rule. The United States has enforced targeted sanctions against top Zimbabwe officials and associates since 2002 and Congress has expressed its opposition to the government's undemocratic policies in the Zimbabwe Democracy and Economic Recovery Act of 2001 (ZDERA; P.L. 107-99) and subsequent legislation. Also see CRS Report RL32723, *Zimbabwe*, by Lauren Ploch.

Chapter 7 - Political tensions on the Indian Ocean island of Madagascar between President Marc Ravalomanana and Andry Rajoelina, the former mayor of the capital city, escalated in early 2009, culminating in the President's forced removal from office. In preceding weeks, over 135 people had been killed in riots and demonstrations. Under intensifying pressure from mutinous soldiers and large crowds of protestors, Ravalomanana handed power to the military on March 17, 2009. The military then transferred authority to Rajoelina, who has declared a transitional government. Rajoelina's "inauguration" as president of the transitional authority was followed by days of protests by thousands of supporters of Ravalomanana. Several subsequent demonstrations have led to violent clashes with security forces. Negotiations in August between the parties led to the signing of an agreement in Mozambique to establish an inclusive, transitional government, but Rajoelina subsequently appointed a new government seen to be primarily composed of his own supporters. Southern African leaders and Madagascar's opposition parties rejected the proposed government, and negotiations in Mozambique resumed. On October 6, the parties announced that they had reached agreement on posts in the new government, which will be led by Andry Rajoelina until new elections are held. Ravalomanana reportedly agreed to the arrangement on the condition that Rajoelina would not vie for the presidency in those elections. The agreement must now be implemented, and some observers question whether members of Rajoelina's former administration will adhere to the new arrangement.

The political uncertainty has strained relations between international donors and Madagascar, which was the first country to sign a U.S. Millennium Challenge Account compact, worth an estimated $110 million. That compact was terminated in May 2009. Following coups in Mauritania and Guinea in 2008, the African Union, the United States, and the European Union, among others, warned against an unconstitutional transfer of power on the island nation and have suspended most foreign aid and threatened sanctions. The African Union and the Southern African Development Community have suspended Madagascar until constitutional order is restored.

Chapter 8 - Sudan, geographically the largest country in Africa, has been ravaged by civil war intermittently for four decades. More than 2 million people have died in Southern Sudan over the past two decades due to war-related causes and famine, and millions have been displaced from their homes. There were many failed attempts to end the civil war in southern Sudan. In July 2002, the Sudan government and the Sudan People's Liberation Movement (SPLM) signed a peace framework agreement in Kenya. On May 26, 2004, the government of Sudan and the SPLM signed three protocols on Power Sharing, on the Nuba Mountains and Southern Blue Nile, and on the long disputed Abyei area. The signing of these protocols resolved all outstanding issues between the parties. On June 5, 2004, the parties signed "the Nairobi Declaration on the Final Phase of Peace in the Sudan." On January 9, 2005, the government of Sudan and the SPLM signed the final peace agreement at a ceremony held in Nairobi, Kenya.

In October 2007, the government of Southern Sudan suspended the participation of its Ministers, State Ministers, and Presidential Advisors from the Government of National Unity to protest measures taken by the National Congress Party and to demand full implementation of the Comprehensive Peace Agreement (CPA). In response to these demands and unexpected developments, President Bashir reportedly accepted a number of the government of South Sudan (GoSS) demands in late October, except those related to the Abyei issue. In late December 2007, the new ministers were sworn in office. In May 2008, Government forces burned Abyei town and displaced more than 60,000 people. An agreement reached in June 2008 between the Government of South Sudan (GoSS) and the National Congress Party (NCP) on Abyei largely ended the tense situation between the two sides.

The crisis in Darfur began in February 2003, when two rebel groups emerged to challenge the National Congress Party (NCP) government in Darfur. The crisis in Darfur in western Sudan has led to a major humanitarian disaster, with an estimated 2.45 million people displaced, more than 240,000 people forced into neighboring Chad, and an estimated 450,000 people killed. In July 2004, the House and Senate declared the atrocities in Darfur genocide, and the Bush Administration reached the same conclusion in September 2004. On May 4, 2006, the Government of National Unity and the Sudan Liberation Movement/Army (SLM/A) signed the Darfur Peace Agreement (DPA) after almost two years of negotiations.

In July 2007, the U.N. Security Council passed Resolution 1769, authorizing the deployment of a robust peacekeeping force to Darfur. The resolution calls for the deployment of 26,000 peacekeeping troops to Darfur. The resolution authorized the United Nations African Union force in Darfur (UNAMID) to take all necessary measures to protect its personnel and humanitarian workers. As of May 31, 2009, UNAMID deployed a total of 16,402 peacekeeping personnel. In July 2008, International Criminal Court (ICC) Chief Prosecutor Luis Moreno-Ocampo accused President Omar Bashir of Sudan of genocide, crimes against humanity, and war crimes and asked ICC judges to issue an arrest warrant for President Bashir. On March 4, 2009, the ICC Pre-Trial Chamber issued a warrant of arrest for President Bashir for war crimes and crimes against humanity.

In late October 2009, the Obama Administration announced a new Sudan policy. The new Sudan policy focuses on three policy priorities: the crisis in Darfur, the implementation of the North- South peace agreement, and counter-terrorism. The new policy links the lifting of sanctions and incentives to verifiable progress on the ground.

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Chapter 1

OCEAN PIRACY AND ITS IMPACT ON INSURANCE

Rawle O. King

SUMMARY

Many Members of 111th Congress are concerned about the sharp rise in pirate attacks in the strategic waterways in the Gulf of Aden off the East coast of Africa. The hijacking of a Saudi Arabia-owned oil tanker, *Sirius Star*, off the coast of Kenya on November 15, 2008, by pirates, and its release after a $3 million ransom payment on January 8, 2009, was another in a series of seizures and releases that have focused worldwide attention on economic and humanitarian threats posed by pirates to the global seafaring community and the smooth flow of international trade. Given the sharp increase in the number of pirate attacks, the cost of transporting cargo in international waters could rise dramatically because of the sharp increase in ocean marine insurance rates for ships transiting the Gulf of Aden. Commercial insurers, for example, could require a special "war risk" insurance premium costing an additional ten of thousands of dollars a day. These additional costs could adversely impact international trade during the current global economic slowdown.

In addition to proposals for military deterrence and diplomatic engagements, policymakers may elect to consider adjustments to the federal statute (Title XII of the Merchant Marine Act of 1936, as amended) that authorizes the federal government to underwrite marine war risk insurance in circumstances such as piracy. Title XII, administered by the U.S. Department of Transportation's Maritime Administration, authorizes the federal government to act as an insurer or reinsurer of last resort to facilitate waterborne commerce should private ocean marine insurance markets not be able to ensure that financial losses due to war risks (and piracy) will be largely covered.

Policymakers may also elect to maintain the status quo on this statutory authority. The property and casualty insurance industry policyholder surplus is calculated to be approximately $505 billion (as of June 2008). Vessel hull and war risk premiums in the U.S. market paid to insurers totaled approximately $350 million in 2007, and the total value of cargo insurance premiums paid in that year was approximately $833 million, according to industry data. Some may contend, as a result, that the insurance industry appears to be

financially capable of handling U.S. exposure to the current piracy threat and that the existing policy "backstop" will be adequate.

Introduction

In the wake of the unprecedented number of pirate attacks on merchant ships off the Coast of East Africa in 2008, including the hijacking of a Saudi Arabia oil tanker (*Sirius Star*) carrying $100 million worth of crude, the global shipping industry and its insurance companies have called on governments to take immediate action to stop piracy in the Gulf of Aden and Indian Ocean.[1] Public attention has now focused on suspected Somali pirates who use sophisticated vessels and high-powered weapons to take control of large ocean-going ships carrying valuable cargoes. When pirates seize the ships they usually hold the crew hostage and demand money for the return of the crew, tanker and its contents (cargo). There are no reports of cruelty or destruction of vessels or the cargo. Piracy in the international waters off the East coast of Africa is arguably becoming viewed by the shippers, insurers, and pirates themselves as a well-established practice that functions in a business model that includes precise, well-established calculations of the amount to be paid as a ransom and professional assurances of the safety of crew, ship and cargo while negotiations proceed.

Shippers generally purchase ocean marine insurance to protect against a financial loss or injury to their crew, cargo and the ship itself. Still, pirates pose an economic threat to the global seafaring community and the smooth flow of international trade by commercial shipowners and operators. Also, the cost of transporting cargo could rise dramatically because of the sharp increase in commercial shipping insurance rates for ships transiting the area. By one estimate, due to piracy in the Gulf of Aden, the cost of insuring a container went from $900 in 2007 to $9,000 in the closing months of 2008.[2] These increases could trigger further rises in later phases of manufacturing and production.

The Current Situation

Piracy Events and Impacts

The Gulf of Aden was identified as an area of concern by Lloyd's Market Association (LMA) in May 2008.[3] The Gulf of Aden is considered a strategically important international waterway that carries a third of the world's crude oil. Over 20,000 vessels pass through this area each year. The Gulf of Aden lies between Yemen and Somalia and connects the Indian Ocean to the Red Sea and the Suez Canal. Other areas of the world that are viewed at risk for ocean piracy include Indonesia, Nigeria, Bangladesh and India.

Ocean marine insurers have urged shippers to stay at least 200 miles off the coast. On November 17, 2008, the *Sirius Star*, a Saudi-owned crude oil tanker, was seized in the Indian Ocean by suspected Somali pirates 450 nautical miles off the coast of Kenya in the Indian Ocean. The vessel remains anchored by the pirates near Harardhere, Somalia until its release in January 2009 with a $3 million ransom payment.[4]

The seizure of the *Star* was an unprecedented attack given its distance from shore (450 nautical miles) in the Indian Ocean and the size of its target (supertanker) compared to the majority of recent attacks. Shippers believe they can avoid the pirates by sailing farther offshore, but this means more time at sea and extra costs. As a result, ocean marine insurers are considering enlarging the war risk zone, a decision that would escalate the cost of shipping. Part of the higher cost would be the extra time and fuel consumed by going via the Cape of Good Hope rather than the Suez Canal. Also, insurers could require special "war risk" insurance costing tens of thousands of dollars more per day to cover travel across a much greater area of water.[5] Merchant shippers would also have to incur additional expenses to hire a security force to protect their vessels. One estimate of the added cost for security ranges as high as $60,000 per trip.[6]

On November 19, 2008, Pentagon officials released statistics showing that in 2008, there had been 95 reports of piracy attacks on merchant vessels in the Gulf of Aden, with 39 of these resulting in the capture of vessels.[7] The U.S. government has responded militarily to such piracy by sending four U.S. Navy warships from the Fifth Fleet in Bahrain to the Gulf of Aden off the coast of Somalia. Officials have also expressed an interest in working through the United Nations to encourage Somalia to curb piracy activities operating from its shores; an outcome that would be difficult to achieve since Somalia has no functioning government. The European Union sent a naval fleet to escort ships in the region. The U.S. warships have joined other warships from different countries such as Russia, China and Iran now patrolling the area.[8] According to Pentagon officials, many attacks were thwarted in December 2008 by the presence of military forces or by defensive measures taken by ship captains. U.S. military officials are encouraging merchants to sail with armed guards and to travel within lanes now patrolled by U.S. warships.

Insurance industry effects

Despite the increased threats and estimates of rising costs, the impact on the insurance industry appears negligible. Given the size of the property and casualty insurance industry's policyholder's surplus of about $505 billion, as of June 2008, and the relatively low total cost of vessel hull and war risk premiums of approximately $350 million and total cargo premiums written by U.S. marine insurance market in 2007 of $833 million, it appears that the insurance industry would be financially capable of handling U.S. exposures to acts of piracy in international waterborne commerce.

THE ECONOMIC COSTS AND CONSEQUENCES OF PIRACY

In May 2008, insurance underwriters at the Lloyds of London designated the Gulf of Aden a "war-risk" zone subject to a special insurance premium. London-based ocean marine insurers have raised rates for ships making the voyage through the Gulf of Aden and the Suez canal. These levels of increase can only be estimated because of the competitive nature of the ocean marine insurance business. One group of London insurance brokers and underwriters estimates extra premiums at $10,000 to $20,000 per trip through the Gulf.[9] U.S. rates, however, apparently have not changed. According to representatives of the American Institute of Marine Underwriters (AIMU), U.S. ocean marine insurers have not had to pay ransom for

any act of piracy; therefore, they say, hull and cargo insurance rates for vessels leaving the United States remain the same.

The global shipping industry is most concerned about vessels that carry oil, chemicals, coal, iron ore, wheat and other commodities, because these vessels tend to be more vulnerable to pirate attacks than container vessels that carry manufactured goods. Container vessels are considered more difficult to seize by pirates because they ride higher in the water and are more difficult to board and seize from a small boat.

The increase in pirate attacks is occurring at a time when the shipping industry is expressing concerns about its financial health. One development is that the frequency of hiring dry bulk carriers, a key industry component, has decreased; the "hire" rates have dropped over 90% in the last six months.[10] (In some cases, the hire rate has dropped because the financial industry has stopped financing trade due to the global economic crisis.)[11] In addition, many ship owners and other key industry participants apparently face severe losses from the global financial market crisis. Some major dry bulk shippers lost money speculating on the market in shipping derivatives that offered potential for strong investment returns.[12] Shipping derivatives were developed to manage risk stemming from fluctuations in freight rates, vessel prices, interest rates, and foreign exchange rates, more effectively, in a cheaper and more flexible manner. Many shippers made derivative bets mistakenly on the direction of dry bulk rates during 2008.

With respect to the piracy issue, besides the *Sirius Star*, there are an estimated 14 other ships and their crews currently being held by pirates.[13] London-based shipping firms usually are, at times, prepared to pay ransom because the demanded sums are considered low, ranging from $500,000 to $2 million, compared with the value of the ships and its cargo. Such payments are reimbursed because the hull insurance policies issued in London explicitly cover the peril of piracy.[14] (Hull insurance forms used by American insurers generally exclude coverage for the peril of piracy.) Most of the 18 vessels, however, have cargo valued low enough that shippers likely will not pay the ransom demanded by the pirates; the ransom demanded exceeds the value of the cargo. One exception is a Ukrainian freighter currently being held by pirates, whose cargo includes military tanks, rocket-propelled grenades and antiaircraft guns. According to media reports, a deal has been reached for the ship's owners to pay an undisclosed ransom in exchange for the return of the ship.[15] In this case questions of public safety and threats of civil instability were considered along with financial calculations.

BASICS OF MARINE INSURANCE

Marine insurance is coverage for goods in transit, and for the commercial vehicles that transport them, on water and on land. Marine insurance is divided into *inland marine* and *ocean marine* insurance. Inland marine insurance covers transportation-related or transportable property on land and air transportation as well as bridges, tunnels, and other modes. It is insurance for shipment that does not involve ocean transport.

American ocean marine insurance provides coverage for vessels and their cargo on the high seas, lakes or inland waterways. There are four basic types of ocean marine insurance:

- hull insurance that covers physical risk to the ship, like grounding or damage from heavy seas, collision, sinking, capsizing, being stranded, fire, piracy, and jettisoning cargo to save other property;
- cargo insurance that covers the goods transported in the ship;
- hull war risk insurance (including automatic termination and cancellation provisions in the event of war); and
- protection and indemnity (P&I) which covers liability involving the crew, docks and piers. Ship owners can purchase separate kidnap and ransom insurance for crew members.[16]

Hull Insurance

Hull insurance primarily covers physical damage to vessels (hull) and the machinery and equipment. The insurance also covers collision liability associated with damage to other vessels and their cargoes resulting from collision with the insured vessel. The hull insurance policy indemnifies the insured shipowner for these damages.

Most American shippers use the hull insurance form called *American Institute Hull Clauses* (AIHC), developed by the American Institute of Marine Underwriters, a trade association for marine insurers.[17] The AIHC is used primarily for oceangoing cargo and passenger vessels.

Another form, named the Taylor form, is often used for insuring vessels that traverse American rivers and coastal waters. In addition, it is customary for some insurance brokers to develop their own marine forms for submission to underwriters. This is possible because there is no standard form of marine insurance policy recognized by law in the United States.

American ship owners, operators, and merchants may also purchase marine insurance overseas, especially through the London market, which uses its own form. The London Institute hull form (known as the 1983 clauses or "Institute Time Clauses Hulls") explicitly covers loss or damage caused by piracy (page 58 of the form).[18] There is no exclusion. In order to provide uniformity, Great Britain codified its marine insurance law in the landmark *Marine Insurance Act of 1906*. This act established the Lloyd's form of policy as an example but is not a required policy form. The approach developed in Great Britain is to provide constant rules of interpretation so that there would be certainty of meaning and stability in ocean marine insurance transactions.

With respect to coverage for acts of piracy, it is instructive to note that the AIHC includes piracy as a named peril (on line 71) but excludes piracy (on line 245) as an insured peril in the event of war. Recognizing the war risk exclusion, U.S. shippers have the option of purchasing a separate war risk policy, called the *American Institute Hull War Risk and Strikes Clauses* which effectively covers the excluded war perils, including piracy.[19] However, even under the hull war risk insurance policy, the marine insurer retains the right to cancel the policy at any time. In the event the private insurer's war risk insurance is cancelled, the U.S. Department of Transportation's Maritime Administration's marine war risk insurance and reinsurance federal backstop automatically provides insurance and/or reinsurance to the ocean marine shipping industry (see "War Risk Insurance" discussion below).

Ocean Cargo Insurance

Ocean cargo insurance policies are written as separate coverage from hull insurance because merchants typically ship cargo via vessels owned by others. Ocean cargo insurance may be classified in two ways: policies issued to cover river and harbor cargo, and those issued to cover international trade that occurs on the oceans and seas. Cargo policies may also be classified by whether they are designed to cover a particular voyage, a specific time period, or a commodity such as grain, cotton, iron ore, or whether they are adapted to cover cargo general in its nature. Cargo policies may be issued for a single cargo risk (special or single risk cargo policies), and those that cover automatically all shipments of an insured (open or floating policies), subject to cancellation with 30 days' notice.

War Risk Insurance

Hull insurance usually does not cover the risk of a vessel sailing into a war zone, but such insurance can be purchased separately as "war risk insurance." War risk insurance is special coverage on cargo in transcontinental ships that protects against the risk of confiscation by a government in wartime. War risk insurance coverage protects, at an additional premium, against the danger of loss in a war zone. The war risk zones are established by the London-based Lloyd's Market Association's Joint War Committee (JWC), which has recently included the Gulf of Aden as a war risk area due to piracy.[20] (About a decade ago, the Malacca Straits were similarly designated a war risk area due to piracy.) The JWC represents the interests of underwriters writing war and related risks within the London ocean marine insurance market.

The U.S. Department of Transportation's Maritime Administration's (MARAD) marine war risk insurance program under Title XII, Merchant Marine Act, 1936, as amended, includes a provision of vessel war risk insurance, as follows.[21]

> The Secretary (of Transportation), with the approval of the President, and after such consultation with interested agencies of the Government as the President may require, may provide insurance and reinsurance against loss or damage by war risks in the manner and to the extent provided in this subchapter, whenever it appears to the Secretary that such insurance adequate for the needs of the water-borne commerce of the United States cannot be obtained on reasonable terms and conditions from companies authorized to do an insurance business in a State of the United States.[22]

During times of national emergency, at the request of the Department of Defense, the MARAD underwrites marine insurance risk insurance for DOD-chartered vessels during national emergency. Commercial shippers can obtain war risk insurance coverage from MARAD.

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