THOMAS & CO
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Article: The Investigation of the Total Loss of a Cargo Resulting from the Sinking of the Carrying Vessel

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Contents

Section 1 – *Day 1*

- Evidence – The First Hours *(Page 2)*
- Security *(Page 3)*
- Jurisdiction *(Page 3)*
- Limitation *(Page 4)*

Section 2 – *Days 2-7*

- Evidence *(Page 5)*
- General Review *(Page 7)*
- Security *(Page 8)*
- Limitation *(Page 8)*
- Liability *(Page 8)*
- Further Thoughts *(Page 9)*
- Conclusion *(Page 9)*

The total loss of a cargo following the sinking of a vessel presents an extremely challenging situation for an insurer. On the one hand the assured will soon be pressing for payment of its policy claims for, depending on the value of the cargo and the size of the assured, the financial loss could seriously disrupt the business of the assured and even threaten the continued existence. On the other hand, investigations need to be commenced and evidence collected.

Evidence is like a bucket of water where the bucket has a hole in the bottom – as time goes by water is lost through the hole and once lost is difficult, if not impossible, to recover. In a total loss situation evidence not collected is often lost and is perhaps impossible to retrieve at a later date.

In this paper I seek to deal with a total loss situation considering the position of the insurer from day 1 onwards.

The precise circumstances of every total loss situation will be different. Some vessels will break up and sink quickly, almost without trace. Others will be damaged and survive some hours or days so that a salvage operation might even be commenced, although in the situation we are considering, it will prove unsuccessful.

I wish to deal with this subject by reference to a certain set of facts and supplement the facts initially known in much the same way as this could occur in practice. At the outset very little may be known. The first notice that you receive is likely to contain very little information.

Facts: The vessel "Merchant Kiwi", a bulk carrier of 30,000 gross tons, sinks on a loaded passage from Poland to China. It is loaded with a steel cargo insured with your company for US $12 million.

Section 1

Day 1 – Evidence - the first hours

The first reports that reach you may be either from the assured who has received news from the shipowners or charterers, or the first report may even have come from lawyers or adjusters who are alerted through casualty reports.

Your first action will obviously be to verify that you indeed are the insurers of the cargo or consignments of cargo on the vessel, the policy terms and the extent of your exposure. I will assume that in this instance you will discover, unfortunately, that you indeed insure the entire cargo on an "all risk" basis.

The first issues to consider are:

1. Whether the cargo insured was indeed loaded on the vessel and is now a total loss as a result of the vessel's sinking; and
2. How to gather as much evidence as possible both to allow you to confirm the above issue and ultimately decide whether there will be any possibility to recover your outlay from the shipowners or carrier.

First, you will wish to organise whatever facts are already known to you and quickly establish from Lloyds's Register or other databases open to you, the identity of the owners, the nationality of the owners, the flag state of the vessel, the vessel's P&I Club and whether the vessel is owned by a one-ship company or has sisterships.

The assured will probably have been in contact with the vessel's local agent and may be in possession of news. The assured will, as purchasers of the cargo, be holding important documents, which you need to have copied to you immediately.

Investigations should be divided into four main categories: Evidence, Security, Jurisdiction and Limitation. It is as well to have these four in mind from the first notification, but the emphasis in the first hours is to establish basic facts and importantly decide what action must be initiated by you as cargo insurers to collect evidence, albeit at this early stage "without prejudice" to the question of liability under the policy.

The bucket is full, but it is starting to leak.

What happened? Where did the vessel sink?

Casualty reports issued by Lloyds and possibly local agencies will provide basic facts. They may also relay the content of any SOS messages put out by the vessel.

Was the crew lost or are there survivors?

If there are survivors, then can it be established which vessel has rescued them and where the survivors will be put ashore?

Will it be possible to interview the survivors in order to obtain detailed first hand information as to why the vessel sank?

The shipowners and the P&I Club will probably try to prevent anyone appointed by you from interviewing the crew. If however the local authorities where the survivors or rescued crew arrive intend to interview the Master and/or crew you will need to establish what form that interview will take and whether it is possible for anyone appointed by you to be present and either ask questions directly or put questions through the chairman or person conducting the interview.

It is of course worth making serious attempts to obtain statements from the survivors, as theirs may be the only first-hand account of what occurred. If access to them is barred it is worth considering whether to interview the crew of the rescue vessel. Whilst their evidence is likely to be second-hand – unless the rescue ship actually arrived before the vessel sank – it is most likely that the survivors will have spoken openly to those who rescued them.

If the rescue ship did arrive before the vessel sank, then very often members of that crew will have taken photographs of the stricken vessel which could provide invaluable information as to the cause of the sinking and the vessel's condition immediately before it sank.

It is also likely that the press at the place where the survivors are put ashore will be taking an interest. All press reports will need to be monitored although sometimes press reports may contain a certain amount of dramatisation or even fabrication as the truth may not be interesting enough to sell newspapers.

Again, the internet is invaluable as a means to trace reports which are produced in the local press. The name of the ship is easy to search against.

Casualty reports from Lloyds will be issued regularly and these should be continually monitored.

Although I will consider it shortly, depending on the jurisdiction in the contracts of carriage, it may be possible that a Court surveyor or expert can be appointed and if that is the case then he may well have the power to compel the crew to give statements to him. This is particularly the case in relation to some Roman law jurisdictions on the continent of Europe, for example France and Belgium.

You will need to consider whether there will be a formal investigation into the cause of the casualty – this will depend on the flag state of the vessel. Frankly it is more likely that there will be an investigation where there are casualties.

Day 1 – Security

If a claim is to be pursed against the carriers then security is required. The last thing that you as cargo insurers want to do is throw good money after bad by pursuing an unsecured claim against shipowners whose one vessel is at the bottom of the sea. Accordingly some facts have to be established quickly:

1. Is the "Merchant Kiwi" owned by a one ship company or are there sisterships that are trading and could be arrested at a later date?
2. Which P&I Club was the vessel entered with? If the "Merchant Kiwi" was entered with an International Group P&I Club and there are sisterships then security assumes less of an immediate issue.
3. If the "Merchant Kiwi" was owned by a one-ship company, then even if it is entered with an International Group P&I Club you must initiate urgent investigations to trace the whereabouts of the hull insurance proceeds with a view to injuncting these.

Alternatively it may be possible to arrest other assets belonging to the owners of the "Merchant Kiwi", for example bunkers owned by these shipowners on another chartered vessel.

If the "Merchant Kiwi" was owned by a one ship company, but is entered with, for example, one of the Scandinavian clubs then your position is better than with one of the other clubs as there will be the potential for a direct action against the Scandinavian club. Otherwise the difficulties will be with the "pay to be paid" clause in the rules which will mean that a one-ship company who has received and dispersed the hull proceeds is unlikely to be worth suing.

If the owners of "Merchant Kiwi" do own other vessels, but those vessels are entered with a club outside the International Group, then it may be risky to consider accepting a Letter of Undertaking from such a club or insurers for the sort of money that we are considering here. In such a situation it may be necessary to arrest a sistership or even more than one sistership before suitable security is offered.

On one case where a ship from the former Soviet Republic of Georgia sank, we arrested two of their vessels in Rotterdam and only when we threatened to arrest a third was satisfactory security produced.

If in our situation the "Merchant Kiwi" was a one-ship company not entered with a Scandinavian P&I Club then security is of the top most urgency and a search must be initiated to discover the whereabouts of the Hull and Machinery policy, bearing in mind that it is quite often the case that any claim under that policy may be paid in less than 4 weeks following the loss.

Day 1 – Jurisdiction

It will be necessary to for you to do all that is possible to collect contractual documents from the assured as rapidly as possible.

If the Bills of Lading are available, are they Liner Bills of Lading – if so, what jurisdiction is provided for in the Bills?

If the Bill of Lading incorporates a Charterparty – a copy of the Charterparty must be obtained as soon as possible to see what arbitration/jurisdiction provisions appear in that document.

A strong claim, even a secured one, in a bad jurisdiction is unlikely to be financially worthwhile, so an early assessment of the jurisdictional possibilities is necessary.

If a bad jurisdiction is provided for you will need to consider whether, if sisterships exist, they could be arrested at some future time in a more favourable jurisdiction, in order to found jurisdiction as well as possibly security. There are risks attached to this – if a vessel is arrested in country B when there is an exclusive jurisdiction clause in favour of country A in the contract of carriage, then ship interests could start an anti-suit injunction in country A in seeking to prevent cargo interest from proceedings with the proceedings in country B. It may be that this is a risk you decide to run, given the circumstances of the particular case.

Also sometimes a jurisdiction which is unfavourable to cargo interests may also be unfavourable to the shipowners, so it may be possible to agree some other jurisdiction acceptable to both sides.

If there is a choice of jurisdiction then you will need to consider the advantages and the disadvantages of the jurisdictions available – for example, does one jurisdiction allow the appointment of Court Experts to investigate the casualty; if this is not so crucial then does the jurisdiction have a comprehensive discovery procedure? I will return to this later.

Day 1 – Limitation

It will be necessary to consider which tonnage limitation regime is applicable and how this affects the claim. Broadly, there are four regimes. First, limitation based upon the post-casualty value of the vessel- the United States follows this approach. Secondly, limitation under the 1957 Convention relating to the Limitation of the Liability of Shipowners (the Brussels Convention). Thirdly, there is the 1976 Convention on Limitation of Liability for the Maritime Claims (the London Convention) and finally, the 1996 Protocol to the 1976 Convention.

The 1996 Protocol substantially increases the amount of compensation payable. On our example a 30,000 ton vessel will have a limitation fund of around US$5 million under the 1976 Convention. Were, for example, English law and jurisdiction applicable, then under English law the 1976 Convention on Limitation of Liability for Maritime Claims is applicable, but from 13th May 2004 this was amended by the 1996 Protocol.

Whereas under the 1976 Convention the Limitation Fund would be in the region of US$5 million, the 1996 Protocol means that the Limitation Fund would be in excess of US$12 million and so therefore will not affect his claim.

It is virtually impossible to break the 1976 Convention limit. The case would have to be a truly exceptional one, for example where the owners had fair warning through an earlier identical incident that caused the vessel or sistership to almost sink but in spite of this they failed to change their procedures and carried on in exactly the same way with the result that the “Merchant Kiwi” sank. It is necessary to show that there was recklessness on the part of top level of management of the shipowners with knowledge that the damage would probably result. In our scenario, breaking limit is not going to be an issue.

If there is a choice of jurisdiction then the tonnage limitation regime in that jurisdiction would be a major consideration in choosing the most appropriate jurisdiction.

It is also necessary to consider whether the claim is limited under the applicable Hague/Hague Visby/ Hamburg Convention. In our case, Poland is a signatory to the Hague Visby Rules. Assuming the cargo weighs 6,000 tons or more, then using the per kilo limit of 2SDR’s per kilo, the claim would not be limited.

Section 2

Days 2-7 – Evidence

By now more facts will have emerged which could raise the real possibility that the shipowners are liable due to an actionable breach of contract – a failure to exercise due diligence to make the vessel seaworthy prior to the commencement of the voyage.

An alternative way of treating this is that the shipowner failed to deliver cargo and so the onus of proof is on him to bring himself within a contractual exception to liability.

It is during these days that the cargo insurer will be pressed to make a decision on policy liability.

No doubt the assured will be pressing hard for settlement of his claim.

You as insurers will want to give a good and effective service to your assured. However you will first want to satisfy yourselves:-

1. That the cargo was shipped;
2. That the cargo was lost when the vessel sank – in other words the cargo was still on the vessel when it sank;
3. That there are no policy issues which would prevent you paying the claim.

The assured will by now have produced basic cargo documents. The Bill of Lading will probably be accompanied by certificates of weight or analyses of the cargo loaded.

Study of these basic documents should satisfy you that the cargo was in fact shipped and when it was shipped. If there appear to be irregularities then it may be necessary to instruct some surveyor or investigator at the load of port to corroborate the fact the cargo was loaded on the vessel.

Also the commercial sales invoices should satisfy you that the cargo was insured for a fair value and was not vastly over insured.

Was the cargo on board the vessel at the time it sank?

By now more facts will be known. The position in which the vessel sank relative to its departure date should all add up to this being a genuine situation.

If the vessel was seen to sink the eyewitness evidence should corroborate the fact that the vessel was in a loaded condition when it sank.

If it is a case where the vessel sank suddenly, without trace or survivors – as tragically some bulk carriers have in the past – there will probably be records of SOS transmissions or maybe sightings of wreckage which put the vessel's position where it ought to have been when it sank.

Any suspicious circumstances or things that do not add up need to be looked out for. An obvious one is whether the vessel's reported position when it sank was not on the proper route between the load port and the port of discharge.

One case which I had involved a full load of timber insured by Belgian clients. It was found to involve a fraudulent claim when the Captain of the rescue ship produced his home made movie to show that at the time that the crew were rescued – in good order in a lifeboat complete with personal possessions and the ship's cat – it was clear from the draft markings on the stricken, then abandoned vessel, that the vessel was empty not fully laden, immediately prior to sinking. That was a case of deliberate scuttling following the theft and sale of the cargo. The scuttling crew, must have been astonished when , having abandoned the ship in good order and opened the seacocks, a rescue ship appeared over the horizon much too soon for their purposes!

If your assured are the cargo receivers, either consignees or endorsees of the Bills of Lading it is unlikely that they will be involved in a fraud or indeed privy to any unseaworthiness, so as to entitle you to avoid liability under the insurance policy by virtue of the warranty implied into a cargo policy by Section 40(2) of the Marine Insurance Act 1906. Most English marine policies, in any event, partially waive section 40 unless the assured or their servants are privy to such unseaworthiness at the time the cargo is loaded. "Privy" means actual knowledge. Negligence will not do even where the negligence is gross/serious. Even if your assured is chartering the vessel, it will be unlikely that they or their servants would be privy to such unseaworthiness.

During this time, before a decision is made about the claim, the assured will be at their most co-operative, for example in producing documents. Before settlement of the claims are there any ways the assured can further assist with enquires – for example can the assured assist in obtaining the shipowner's co-operation in relation to the investigation at the load port?

We have already considered the possibilities of interviewing the crew of the "Merchant Kiwi" or the crew of the rescue vessel.

We have already considered whether a formal investigation will be started either by the local authorities in whose waters the vessel sank, or, if the crew members have died, by the flag state of the vessel. Frankly, if people have died it increases the likelihood of an investigation by the above authorities or those of the flag state.

As the jurisdiction becomes clear it will become possible to decide to what extent discovery of material documents will have to be given by the shipowners.

Even though in most cases many of the ship's papers will have sunk with the vessel, many material documents will be kept ashore in the manager's office, for example, log books apart from those of the current voyage, and copies of the communications between the crew and the managers. Is there anything in these communications which may provide clues as to why the vessel sank? The ISM Code requires shipowners to comply with many procedures which should be documented. In time discovery of these documents will be sought.

Also, enquires should be started to check through the vessel's Port State Control history to see whether there have been any detentions on the previous voyages and, if so, why the vessel had been detained.

During this period (between 2 and 7 days after first notification) you will be constantly assessing the evidence in order to review the facts that have emerged and decide what further steps must be taken. For the purposes of this discussion, I will assume the following facts have emerged:-

Assumed Facts

- **Whilst a salvage tug was mobilised in Cape town the vessel sank during the early hours of 27th October**
- **The crew members (all of Indian nationality) were picked up by a container vessel which had picked up the "Merchant Kiwi"'s distress signals. Two of the crew, the Chief Officer and an Able Seaman, are still unaccounted for. Casualty reports indicate that the vessel suffered a structural failure resulting in water entering into one and then a second hold.**
- **The vessel is owned by Merchant Kiwi Shipping Inc.who are a one ship Liberian company with managers in Greece. It flew the Liberian flag. The vessel was entered with a London (International Group) P&I Club.**
- **The cargo was shipped under four Bills of Lading which specifically incorporate the terms of a voyage charterparty dated 10th September 2004, including the arbitration clause. The Bills of Lading are signed 'for the Master'. The voyage charterparty dated 10th September contains a London Arbitration clause. The voyage charterers are a Chinese company, not the assured, although a related company.**
- **The survivors have been put ashore at Cape Town and the container ship is now continuing up to Europe where its first port of call will be Le Havre. The South African authorities indicate that they do not intend to hold a formal investigation because the vessel did not sink in their territorial waters.**
- **At present it is unknown whether the Liberian authorities have made any decision to hold an inquiry.**
- **We have identified the berth at which the vessel loaded in Poland and the berth at which it discharged its previous cargo, also in Poland. We have instructed surveyors in Poland to make enquiries at these ports to see whether any interesting evidence exists regarding the condition of the vessel at that time.**
- **The Hull and Machinery policy is placed with underwriters in France.**

Days 2-7 – General Review

The claim is now shaping up. There is a claim under the contracts of carriage evidenced by the bills of lading against the shipowners and these contracts expressly incorporate the terms and conditions of the voyage charterparty including the (London) arbitration clause. At this point the priority is to prevent payment of the hull proceeds to the shipowners. The claim against the shipowners is subject to the London arbitration: however it is possible to issue injunctive proceedings or a freezing order in France to prevent payment out of the hull proceeds.
Before taking this step, it is preferable – if it can be done quickly – to search the ship's registry in order to discover whether any mortgages are registered. If there has been an assignment of the benefit of the Hull and Machinery policy to a bank as security for a mortgage then this assignment could render the freezing order worthless. If this search cannot be undertaken quickly then it may be worth going ahead with the freezing order because delay could mean that the hull proceeds are dispersed before the freezing order is in place.

Once an injunction is in place it will be possible to talk to the P&I Club (an International Group Club) to see whether they would be prepared to substitute a suitable Letter of Undertaking in return for the injunction or freezing order being lifted.

There is then a good prospect of securing the claim, subject to the existence of any encumbrances/ assignments, as discussed above.

The rescue ship is due in Europe at Le Havre.
We will request permission to interview those crew members who were responsible for the survivors of "Merchant Kiwi" prior to them being put ashore in Cape Town.

We are also making enquiries with local correspondents in India about the possibility of tracing crew members from "Merchant Kiwi" who will be paid off and returned to India. If the crew have been paid off, then ship owners will no longer have any control over their former employees. Indeed, if the crew members feel that their lives have been put at risk by the failure of shipowners to maintain the vessel properly they may be only too willing to talk about the instances where they perceive the shipowners failed to maintain the vessel properly.

As the claim is subject to London arbitration we know that discovery of documents is possible- accordingly at the relevant time the shipowners have to provide copies of all material documents – we would put together a list of those documents which we expect the shipowners to produce and send this to the P&I Club and/or the lawyers appointed by them.

It would be helpful to be able to inspect records lodged with the Classification Society, for example Class surveys and any supervision by Class of repairs over the last year or two. Most Classification societies will require you to obtain the consent of the shipowner before allowing access to their documents. This may prove problematic. However, as the claim against the shipowners is subject to London arbitration, the shipowners will know that, eventually, at the stage of discovery of documents, they will have to produce copies of these records. Accordingly, they may agree to an earlier inspection.

We will seek to locate the stevedores and the surveyors at the load port and will ask to interview them for information about the condition of the vessel at the time of loading.

We will be collecting weather reports for the voyage showing what weather the vessel encountered both during the voyage and particularly immediately prior to her encountering the problems which led to the fatal seawater ingress.

The weather reports show that the vessel was encountering rough weather for 10 or 12 days during the early part of the voyage in the Northern Atlantic and that the winds were between forces 6-8.

We have discovered that although there were no actual sisterships the managers in Greece also managed two other vessels of a similar type and age to the "Merchant Kiwi". These are all owned by separate Liberian one ship companies. We will request permission for a surveyor instructed by us to inspect these other two vessels in order to ascertain their condition and general state of maintenance. If permission is not forthcoming we will consider making an application to the arbitrators in London for an order to inspect the vessels.

Days 2-7 – Security

Going back to the question of security, if it has not been possible to secure the claim, for example due to the Hull and Machinery insurance proceeds being paid out before an injunction could be obtained, or because the Hull and machinery proceeds have been assigned to mortgagees, then the fact that there are other vessels in the same management may give an opportunity to arrest one of those vessels in a jurisdiction which recognises "associated" ship arrests.

Unfortunately, such an arrest is not possible in England. We recognise corporate bodies as legal entities and sister companies are quite legitimate. The Court of Appeal decided this in the case "Evpo Agnic" (1988) 3 All England reports 810. In that case separate Panamanian companies were set up with the same offices and shareholders, all controlled by the same person. This was held, by the English Courts, to be a legitimate thing for an individual to do and a vessel owned by a sister company could not be arrested.

Some countries do however permit associated ships to be arrested. South Africa permits the arrest of associated ships where owning companies are owned or controlled by the same person. Vessels are "owned" if the majority shareholders are the same and "controlled" if one person has the power to directly or indirectly control the company.

In such a situation investigations would have to be undertaken to try to prove a sufficiently strong association.

As in our case the one-ship companies are Liberian, we will face difficulties in establishing this, as the shares in the company are likely to be "bearer" shares. Nevertheless if evidence can be obtained, which shows that the other two vessels were in fact part of a fleet owned by the same company or individuals , then an associated ship arrest may be a possibility – if of course the other vessels call at a port in South Africa. Other countries such as the United States, France and Belgium take a less rigid view of the sanctity of different legal entities. If the two other vessels trade to one of these counties then local legal advice would need to be taken on whether such an arrest is a feasible proposition.

Days 2-7 – Limitation

On the question of limitation, as English law is applicable the 1976 Convention on Limitation of Liability for Marine Claims as amended by the 1996 Protocol is applicable and this means that the tonnage limit will exceed the claim figure.

You will see in Appendix 1, in the limitation column that I have set out both the 1976 Convention limits and the 1996 Protocol limits.

Days 2-7 – Liability

The port of loading was Poland, the Bill of lading contains a Paramount Clause. Poland is a Hague Visby Rules country. The claims under the Contract of Carriage evidenced by the Bill of Lading will then be subject to the Hague Visby Rules.

In view of the information that the vessel's shell plating collapsed, we are obviously concentrating our efforts on trying to establish a failure on the part of the shipowners to exercise due diligence to make the vessel seaworthy before and at the beginning of the voyage. A seaworthy vessel of the size of "Merchant Kiwi" should not have sunk during the sort of weather conditions which were encountered. When the claim is actually put forward in arbitration it will be put forward on the basis that the shipowners failed to deliver the cargo and we will allege that in those circumstances the shipowners are liable, unless they can demonstrate that they are entitled to rely on an exception to liability or demonstrate that the vessel was seaworthy prior to the commencement of the voyage.

At this point it is not possible to give a firm indication on the merits. It is possible to say that a seaworthy ship of 30,000 tonnes should not break up and sink in rough, but not exceptional or severe conditions. Evidence has emerged suggesting that the shell plating collapsed. If the claim has been secured then there is a suitable jurisdiction provided for in the Contract of Carriage. The claim will not be affected by limitation.

In the coming weeks it is therefore worth following up on the outstanding lines of enquiry to see whether the claims against the shipowners can be successfully established.

Days 2-7 – Further Thoughts

There is one last area on which I would like to touch.

The position where the vessel sank should be known at least approximately. It is worth considering whether it is feasible to have a specialist company locate and photograph the wreck.

This may give substantial evidence on why the vessel sank (and will indeed confirm the loaded condition of the vessel- if there are any grounds for suspicion).

Underwater technology has moved on tremendously in recent years mainly as a result of deep sea oil exploration. Robotically operated vehicles (ROVs) and/ or cameras can operate successfully down to considerable depths. This will be a costly exercise, however it may be worth considering when thinking in terms of claims this size.

Also, in appropriate cases – depending on the position of the wreck, the depth of water in which it sank, the nature and value of the cargo – it may be possible to interest a contractor in retrieving the cargo. I was involved some years ago in the successful retrieval of a major part of a mineral cargo from a wreck which had sunk in approximately 400 meters of water off the coast of Japan. In that case ROVs were used to remove the hatch covers and then pull the bagged cargo from the wreck before they were placed in a cage and brought to the surface. The contractor involved has since told me that this equipment could recover cargo laying up to 3,000 meters below the surface, although the deeper the cargo the more expensive the exercise will be.

Technology is of course progressing all the time.

Conclusion

In conclusion I hope that this paper could form the basis of your action plan if faced with this kind of total loss situation.

The paper has been an overview and I have dealt in fairly short order with some topics, for example, the obtaining of freezing orders and associated ship arrests, which are of sufficient complexity to justify a paper of their own.

Each case will be unique and some pieces of evidence will lead to further lines of enquiry that one cannot predict.

I hope however, that this paper might offer some guidance in what is bound to be a very stressful situation.

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Appendix One

Limitation

- 1976 Convention on Limitation of Liability for the Maritime Claims
  - Up to 500 tons 167,000 SDRs
  - Between 501 and 30,000 tons add 167 SDRs per ton
  - Between 30,001 and 70,000 ton add 125 SDRs per ton
  - Over 70,000 tonnes add 83 SDRs per ton

- 1996 Protocol
  - Up to 2,000 tons 1,000,000 SDRs
  - Between 2,001 and 30,000 tonnes 400 SDRs per ton
  - Between 30,001 and 70,000 tons 300 SDRs per ton
  - Above 70,000 tons add 200 SDRs per ton