Export ABC's: Cargo Insurance

In our most recent column, we covered the basics of marine cargo insurance. This is a complicated topic, and some details required further explanation. We'll approach this on a "frequently asked questions" basis.

Who Insures?

The questions of who arranges for insurance coverage can be viewed from three perspectives.

Who may arrange for insurance? Anyone with insurable interest, which means anyone who stands to lose if something goes wrong with the shipment. The reason insurers require insurable interest is that insurance was once used as a form of gaming. People would randomly purchase insurance on voyages with which they had no financial interest at all, hoping to profit from catastrophe. This disgusting behavior is contrary to public policy and is illegal in many countries.

Who must arrange for insurance? Anyone with insurable interest who contracts with others to do so, such as sellers using the CIP (Carriage and Insurance Paid To) and CIF (Cost, Insurance, and Freight) Incoterms.

Who should arrange for insurance, or at least be concerned that someone has done so? The party with the most risk in a transaction, such as:

--Sellers, until their risk for the condition of the contract goods ends;

--Buyers, after the seller's risk ends;

--Sellers who have not been paid;

--Buyers who have prepaid;

--Banks financing transactions;

--Anyone else with liability for the condition of the contract goods.

As we can see, this matches up nicely with the concept of insurable interest.

What kind of coverage?

As mentioned in our most recent column, while insurance is sometimes customized around policy holder considerations, there are three general categories of "London Institute Clauses;" C ("free of particular average" also called "minimum cover"); B ("with average:"), and A (so-called "all risks").

Although everyone realizes that "minimum cover" is inadequate for many transactions, Incoterms 2000 specifies it as the default situation for CIP and CIF. This is because some goods are sold in transit and because more countries require that insurance be placed with local insurers which are often substandard. Also, given the increasing trend towards customizing insurance to individual policyholder needs, it would be difficult to provide a standard definition for anything other than “minimum cover.” In its introduction, Incoterms 2000 encourages sellers and buyers to consider additional coverage. Many do, and agrees on Clauses A plus war and strike, riot and civil commotion; in other words, “maximum cover.”

Often, this is purchased on a “warehouse-to-warehouse basis” to cover the goods during pre-carriage and on-carriage as well as main carriage transportation. However, care should be given to determine where the coverage attaches to a particular shipment. For instance, buyer-provided warehouse-to-warehouse coverage might not attach until vessel loading for shipments made under the FOB (Free on Board) and CFR (Cost and Freight) Incoterms as the seller remains at risk until this happens. Same goes for placing the goods alongside the shipper with FAS (Free Alongside Ship). Savvy sellers using these terms and otherwise lacking insurance for domestic shipments purchase so-called “FAS-FOB” coverage for pre-carriage through vessel loading or alongside placement.

How much does it cost?

This is like asking how long is a piece of string, but even maximum cover marine cargo insurance is generally quite inexpensive. For most types of cargo shipping on most modes of transport to most destinations, it has typically run well under 1 percent. Future premium could increase somewhat, depending on how a given insurance company’s investments and non-cargo insurance activities fare during the present financial crisis.

Insurers hate small claims as there can require much the same processing costs as major ones. For this reason, they offer savings through deductibles and franchises. Deductibles work the same as your auto insurance, where the insurer bears the loss up to an agreed amounts and the insurer covers the rest. Franchises are called “disappearing deductibles” because that’s the way they work. The insured bears the entire loss unless the total exceeds agreed amount. When it does, the insurer bears the entire loss.

What if a ‘covered peril’ happens?

Insurance is not a magic wand. Insured parties have obligations to insurers in the event of a covered loss.

The first is to examine incoming shipments promptly for signs of damage or shortage, and claiming for any against the delivering carrier. It may not be this carrier’s fault, but this starts a chain reaction of carriers filing claims on previous carriers so that the insurer’s subrogation rights against the culpable carrier do not become time-barred. It obviously follows that any shipment that fails to arrive when expected should be traced, as the entire shipment may have been lost.

Next, a preliminary claim notice must be filed with the insurer. Depending on the nature of the claim, the insurer may require inspection by a marine cargo surveyor. These damage detectives can ascertain the extent and often pinpoint the cause of damage.

Under the “sue and labor” provisions found in most marine cargo insurance policies, any damaged goods should be segregated and kept from further damage. This often means storage under cover. This is to protect the insurer’s interest, and any reasonable costs should be reimbursed by the insurer.

Finally, the actual claim must be supported by documentation including the commercial invoice, packing list, transport document, and required surveyor report, and the original insurance policy of certificate.

As you can see, claiming gets to be a hassle. This, plus the inconvenience of waiting for replacement of damaged or lost goods, is the reason most marine cargo insurance is written at 110 percent of the value of the goods and the costs of freight and insurance.

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