TT Live – Series 1: episode 2 – 18/11/2020
Distinctions between liability and cargo insurance

Mitigating the risks

Mike Yarwood, Managing Director Loss Prevention is joined by Andrew Watson-Steward ("Drew"), Cargo Underwriter at TT Club, to discuss the differences between liability insurance and cargo insurance.

Mike: "Welcome to this edition of TT Club's Podcast. "TT Live". In this session, we are going to consider the differences between liability insurance and cargo insurance. This I think is a subject that is not always fully understood and can on occasion in the event of a loss, lead to commercial friction, when the customer expects a full recovery and the freight operator's legal liability is limited. Today I am pleased to be joined by my colleague Andrew Watson-Steward, cargo underwriter at TT Club who will provide his expertise in bringing clarity to this subject.

It is estimated that a large percentage (as high as 90% along some trade lanes) of cargo is shipped uninsured. While the vast majority of shipments are completed uneventfully, clearly risk exists. Risks that could lead to the loss of or damage to cargo in transit.

Limitations specified in STCs or international conventions based on weight or numbers of packages, have the potential in the event of a loss, to leave the cargo owner with a significant financial burden. Experience suggests that this burden when incidents do occur is often a surprise, with the cargo interest expecting to be re-imbursed in full by their contracted freight operator.

There are a number of perceptions as to why so much cargo is shipped uninsured and we will take a look at some of those a little later. We will also consider the difference between cargo and liability insurance and the benefits of cargo insurance being in place.

Cargo insurance has an important role to play in international trade for several stakeholders, not least the cargo interest.

Drew, welcome and thank you for joining us for this session."

Andrew: "Hi Mike, thanks for having me along today. As you've just mentioned I am one of the cargo underwriters at TT Club. We write a book of forwarders cargo insurance commonly known as shippers interest that is sold predominately through our Members to cargo owners.

I'm pleased to be here with you today and am looking forward to discussing some of the key differences between liability and cargo insurance."

Mike: "That's great, thank you, as mentioned, I sense from discussions and interactions with various contacts, that the differences between cargo and liability insurance are not always fully understood. This I think is one of those subjects that people don't like acknowledging ignorance of. For hauliers, freight forwarders, NVOCC's and other stakeholders in the supply chain who trade under STCs and are afforded a limitation of liability this can commercially be a problem right?"

Andrew: "Yes, in the event of a loss, not having cargo insurance in place can certainly lead to an exposure for the cargo interest, the difference between the commercial value of the cargo and the amount recoverable under a liability policy can be significant."

Mike: “Are you able to summarise in a few words the primary difference between the two types of insurance?”

Andrew: “Sure, cargo insurance covers all risks of physical loss or damage to cargo whereas liability insurance is negligence based. Cargo insurance also indemnifies the cargo owner for the full value of the goods whereas liability policies will be limited either by convention or by contract.”

Mike: “Thank you, when explained that way, the differences between cargo and liability insurance are stark and it’s clear to see that these insurance policies serve two very different purposes.”

Andrew: “Very much so, it’s worth noting that a cargo policy is for the benefit of the cargo owner and a liability policy protects the freight forwarder.”

Mike: “Estimates suggest huge volumes of cargo move globally uninsured, is there any obvious indication as to why? Such widespread practice suggests that this isn’t simply the few willing to take risk?”

Andrew: “Risk perception is certainly a factor, many shippers and cargo interests have little concept of the risks which the cargo is exposed to during the international shipment and therefore elect to not insure their cargo.”

Mike: “I have heard cargo interests so many times say, “I thought you insured the goods” to the freight operator, is there also an element of ignorance at play here?”

Andrew: “Yes, there are a number of common misconceptions around insurance and perhaps this leads to confusion. Unless the risk has been explained in detail by the freight operator at the time of booking along with the limitations of liability under the operators STCs, both of which are perhaps unlikely, then the cargo interest might well assume that in handing their goods into the care, custody and control of the freight operator, they are insured.”

Mike: “Another element in the decision to insure or not must be cost. Do you think cost is a factor which deters some cargo interests? Is the cost prohibitive?”

Andrew: “There are a number of factors giving rise to a decision not to insure cargo; cost is inevitably one of them. There is clearly a cost associated with insuring the shipment against the perceived risks and this cost will be determined by the route to be taken, the value and nature of the cargo.

For a standard 20’ container of general cargo moving from China to Western Europe by vessel with value of US$20,000, the premium would be calculated on a rate somewhere in the region of 0.1%. So US$20,000.00 worth of cargo can be fully insured for 20 dollars

As you can see, in many cases, the premium is not cost prohibitive. However, in conjunction with ignorance and the willingness to take risk, the offer of cargo insurance is frequently declined.

It is often only in the event of a loss and the realisation that there is a significant gap between the value of the cargo and the amount recoverable from the freight operator that the value of the cargo insurance is realised.”

Mike: “There are clearly a number of factors at play in terms of deciding whether to purchase cargo insurance. What do you think would help reduce the number of shipments that remain uninsured? Is for example ease of access to market and pricing a factor?”

Andrew: "Many insurers have developed intuitive online platforms from which they sell their cargo product. This makes the process much simpler for those looking to purchase cargo insurance. There are several platforms including our own, which allow the customer to complete a transaction, bind cover instantly and print a certificate of insurance themselves for their records. This does simplify the process for shipments that rest within the insurer's appetite. For anything outside of appetite, then interaction with the insurer might become necessary."

Mike: "In addition to the points discussed earlier, do you think that some cargo interests simply find purchasing cargo insurance overwhelming and given that it is not a compulsory insurance, don't concern themselves with it? I expect that this loops back to the cargo interests' perception of risk. Liability insurance is purchased due to the perceived existential risk exposure that could attach. While an individual cargo shipment might not generate an existential scale risk, for an small to medium sized enterprise however, even a modest loss could prove extremely problematic."

Andrew: "There will undoubtedly be those who do not consider cargo insurance to be essential, again it comes down to risk appetite and arguably past experience. If as a shipper you are inclined not to purchase cargo insurance and have had a number of loss free years, you might consider this a good business decision. However, risk continues to exist. As a business, you might be fortunate enough to operate for many years without a loss or claim, in which case not having bought cargo insurance has certainly saved you money. The associate cost of a single loss however is likely to outweigh much of the premium that you might have paid out purchasing policies."

Mike: "Institute cargo clauses… there are a selection of choices to make when purchasing cargo insurance for those who do. It would be great if you were able to briefly outline the primary differences between these products. The lesser used of the three is institute cargo clauses B, could you briefly outline ICC B and what their purpose is."

Andrew: "Well the first point to make is that the coverage is not midway between A & C clauses as the name might suggest. It's a perils based cover like ICC C and covers in addition to C clauses risks such as sea water entering the container or cargo hold. It also covers the total loss of any package lost overboard during the voyage or whilst loading or unloading. In my experience you do not see a lot of cargo insured under B clauses. Both ICC B and C specifically exclude malicious damage."

Mike: "Institute cargo clauses C, my understanding is that the premium for Institute Cargo Clauses C policies are generally lower than A, naturally such policies provide a lesser extent of cover for the cargo being shipped."

Andrew: "That's correct Mike, there will be a lower premium for goods shipped under C clauses cover however it should be noted that it is a very basic level of cover and as such is not suitable for many types of cargoes. Essentially you are only getting cover for fire and damage to cargo as a result of the vessel capsizing or sinking + any general average contributions.

In most cargo transactions there is a buyer and a seller who must agree contractually which party, if any, will insure the goods for the voyage. As part of that agreement it can be stipulated what level of cover is required and which institute cargo clauses should be used."

Mike: "Finally Institute Cargo Clauses A. This is effectively the most comprehensive level of cover that attracts the higher level of premium. Would it please be possible to provide an outline of the main differences between clauses C and A."

Andrew: "I would start by saying that I have heard people refer to C clauses as 'total loss only' insurance. This is not the case, if a full container is lost due to water ingress into that container this would not be covered under C clauses even though the cargo is a total loss. You can only claim of loss of or damage to cargo as a result of named perils.

ICC A is often called as All Risks cover because it covers all risks of physical loss or damage to cargo as opposed to being a perils based cover like B & C clauses. Here we are covering risks such as theft, water damage, loading and unloading losses and piracy and of course everything covered by ICC B & C.

There is a link on the TT Club forwarders website to the Institute cargo clauses."

Mike: "As well as incidents of loss and damage, General average is an often misunderstood area where a lack of cargo insurance can be problematic."

Andrew: "Most definitely Mike, where cargo insurance is in place, should general average be declared during the voyage, then the cargo insurer will respond and provide the necessary guarantees/securities to allow any salved cargo to be released and continue on its journey. The cargo insurer will ultimately pay any related costs when the time comes. Where there is no cargo insurance in place, then the cargo interest will need to obtain and provide their own guarantee/security or in some cases make a cash deposit which for larger values could have a significant impact on a companies' P&L account. Moreover, recent GA cases have been known to run for many years, which is a further consideration for the cargo interest."

Mike: "Would it be true to say that a cargo interest who has suffered such a loss and has experienced the financial burden of not being able to recover their loss in full, would be more inclined to purchase cargo insurance on the next occasion?"

Andrew: "It depends, their risk appetite can change~~s~~ and they are more compelled to purchase cargo insurance, yes. This can depend on how the claim is handled and of course whether somebody goes to the trouble of explaining to the cargo interest what they could theoretically have recovered had a cargo policy been in place."

Mike: "In many cases, the freight operator or freight forwarder often have a greater appreciation of the associated risks. Where a cargo interest might not have the understanding that would compel them to insure their cargo, can a freight operator influence the decision or provide a route to cargo cover for their customer?"

Andrew: "In the UK, the freight operator can act as an agent of the insurer in arranging cargo insurance. They can therefore promote and sell cargo insurance, which in practice protects both their customer from any claim and the commercial relationship between the freight operator and their customer in the event of a loss. Most underwriters will include a commission for the freight forwarder, which can help generate further revenue. The restrictions in this context are that the freight operator cannot themselves insure the goods, as they have no insurable interest (the cargo is not theirs) and the freight operator must work within the parameters of the insurers guidelines. The insurer will have a set risk appetite in terms of geographic areas, value and commodity."

Mike: "Drew, thank you so much for joining us and for sharing your expertise, do you have any final thoughts or considerations around cargo insurance that we can share with the audience?"

Andrew: "I certainly feel like access to a cargo insurance platform is great tool for a freight forwarder and will undoubtedly avoid some very awkward conversations in the event of a loss.

The TT Club platform is intuitive and doesn't require any specific cargo insurance knowledge to use; the forwarder only needs to ask for the value of the goods as they will hold all the other shipment information.

Being able to provide an All Risks insurance solution will ensure that your commercial relationships are not disrupted when claims are not settled to the satisfaction of the cargo owner."

Mike: "I agree, I think that the ability to protect the commercial relationship in this way is very important. In conclusion, cargo and liability insurance policies are distinctly different. They are purchased by different stakeholders and the extent of cover under each as we have discussed here are very different. As a cargo interest, you should strongly consider options to insure cargo, while you might not have suffered claims in the past, risk inevitably still exists.

The primary message is that if a cargo insurance policy is not in place and an incident occurs, you are unlikely to be able to recover in full from your contracting partners. From a freight operator perspective, thought should be given to promoting cargo insurance to your customers, regardless of whether you provide access to such insurance cover yourselves. Educating your customers as to the potential risks of not having cargo insurance in place, will likely prove beneficial and reduce the potential for commercial friction in the event of a loss.

Thank you once again to our guest speaker, Andrew Watson-Steward and thank you for listening, join us next week when we will be considering the risks associated with doing business in unfamiliar jurisdictions with Julien Horn."