ASSOCIATION OF
Average Adjusters

Rush of marine claims in prospect over ships trapped in Ukraine, Association of Average Adjusters/International Underwriting Association briefing hears

Marine markets face a profusion of "total loss" claims for trapped ships early in 2023, one year after the shut-down of Ukrainian ports, a London audience of practitioners has been alerted.

Ukrainian ports have been closed for vessel entry and exit since February 25, 2022, the day after the Russian invasion, and mines are reported to have been planted, effectively blocking as many as 100 vessels in ports and up rivers. The full value of vessels trapped is unclear, but it could be as much as $800m to $1bn.

At the time of the invasion many of the vessels had war risks policies, but on February 24 war risks insurers began to use their right to demand extra premium to extend the cover.

A market briefing on Wednesday November 2, organised in London by the Association of Average Adjusters and the International Underwriting Association, highlighted the depth of the marine insurance issues involved, and to emphasise this was entitled Do Mention the War!

Burkhard Fischer vice-chairman of the Association of Average Adjusters and a partner with Albatross Adjusters in Limassol, joined with Jonathan Bruce a partner at HFW LLP and deputy head of his firm's global insurance and reinsurance group, to survey key Issues over the detention of ships. Among debatable matters is premium charged for a vessel after it has been seized, arrested, or detained.

Mr Bruce said of the current blockage at the ports: "This is a novel situation and there is therefore quite a lot of uncertainty. Unless things change quickly, it seems likely that there will be a lot of deemed total losses all in one 'clump' next February, and some quick decisions will need to be made. Most likely, disputes can be avoided through sensible discussion and creative solutions, but there is potential for flies in the ointment, for example if vessels get destroyed by missiles. There are likely to be disputes also with reinsurers about what is considered the number of occurrences."

He said that if trapped vessels were on charter, extra premium might have continued to be paid but over time that would presumably have stopped and most of the policies lapsed or been cancelled. In some cases, loss of hire has probably been paid by war risks insurers, but such payments were subject to limits. In many instances crews will have been evacuated, leaving only a few members for maintenance.

One Bangladeshi vessel had been hit by a missile, and there was a real possibility of others being hit. When ships sought to escape in due course, they could be damaged or sunk by mines. Some might also be taken over by Russian interests.

Mr Bruce said that under the Institute War & Strikes Clauses (the IWSC) it was likely that the perils of war, hostile act, restraint, and detainment had all been triggered since the invasion and subsequent

closure of ports. For a claim to occur usually there must be physical loss or damage, but a detainment clause made it clear that after 12 months of restraint there was a deemed constructive total loss. In some cases, the period had been amended to six months, but in most cases, it would be 12 months, expiring next February “when we can expect potentially a large number of deemed total losses all being claimed at the same time. It is understandable that war risks insurers are sensitive about situations where a total loss can be claimed even though the vessel is intact and in theory still a valuable asset.”

For a constructive loss to be declared before that, there would have to be the usual test under the Marine Insurance Act of the assured being deprived of the possession of the ship by an insured peril: a difficult test to satisfy, so usually it would be easier to rely on the detainment clause. An addendum known as the blocking and trapping clause, introduced in 1984 following the experiences of ships trapped during the Suez crisis and the Iran/Iraq war, extended "restraint" to apply where waterways are blocked by warlike acts for 12 months.

Mr Bruce outlined the dilemma: “What happens where a policy has been cancelled or has lapsed after the vessel became trapped; then before the 12 months it gets destroyed by a missile or by a mine? The position gets even more difficult if it turns out that other vessels are then able to escape unharmed from the same port before the 12 months, in other words but for the missile strike there would have been no potential loss. That is quite a difficult and interesting question and there is no English reported case which provides the answer on precisely those facts.”

Insurers might say that the cover was not extended, and no premium was being paid at the time of the missile strike, so that was an act which was not covered. On the other hand, it could be argued that the vessel was already doomed when the invasion took place, and at that time the insurers were still on risk.

One case which could be relevant was Scott v Copenhagen Re, which related to a BA aircraft stranded in Kuwait when Saddam Hussain invaded that country. A month after the start of Operation Desert Storm, still within the policy period, the BA aircraft was destroyed by allied bombing. Given that the aircraft was destroyed after commencement of war, the Court of Appeal held that the triggering event for the loss was the start of the war.

Although it seemed clear that cover under the detainment clause would survive if the detainment started before cancellation, it was less clear that there was still cover if the vessel were destroyed after cancellation but before the 12 months from detainment was over. There seemed to be possible support for there being ongoing cover based on Lord Justice Rix’s view in Scott v Copenhagen Re.

Turning to potential complications in relation to the residual value of vessels, Mr Bruce said “We are likely to see some interesting scenarios which have not really been seen before.” There was an unusual situation in that some vessels were worth a lot more than the insured value, meaning that even where the deemed total loss provision were changed to six months, owners might not want to claim for a constructive total loss if they thought they would be able to get the vessel out eventually. It was possible in those cases for the insurers to agree to change the period back to 12 months and this might suit both parties. The problem for insurers was that if they did not exercise the right of taking over ownership, they could lose their right to the residual value. The solution was probably a

negotiation with the owner or a third party whereby effectively they sell the vessel back to the owner at a discount or find someone else to buy it.

As to aggregation of claims, “there is an issue as to whether losses will be aggregated as losses arising from one occurrence or event, and there could well be disputes about that, as well as to which reinsurance policy responds. That in turn depends on the date which you take as the date of loss. Aggregation is a big issue because if the losses are all lumped together there is only one excess which applies. That is usually a good thing for the insurer as against reinsurers unless the per-event limit is exceeded.”

Mr Bruce noted that since August, three ports had reopened for grain exports, although agreement with Russia has ended.

Mr Fischer said that, following the Suez Canal crisis in 1967 the Institute Detainment Clause was introduced, and a detainment clause is now automatically included in the Institute War and Strikes clauses. An arbitration took place in November-December 1981 seen as a test case on how to deal with a vessel trapped in Shatt-al-Arab, and it was held that shipowners had lost the free use and disposal of their vessel. It was thus reasonable to consider the vessel a constructive total loss after 12 months from notice of abandonment.

The reference to a “closure of the connecting channel” in the London Blocking and Trapping Addendum was slightly problematic, said Mr Fischer. For instance, access to the high seas could be blocked for ships due to the presence of floating mines in the coastal area rather than by a blocked waterway, which is what actually happened in Ukraine.

Mr Fischer said that an underwriter assessing the premium for war risk insurance would have to take into consideration that losses would occur during a period of peace between superpowers, but where a ship was trading in an area with regional conflicts, when a termination clause allowed cancellation with seven days’ notice, although insurance cover might be provided for additional premium.

Why seven days? One would assume that the seven days would provide a ship that had entered the now excepted area with the opportunity not only to leave the war risk area but possibly even finish scheduled cargo operations. Shipowners contemplating sending ships into the war risk area could then decide whether to go ahead despite the increased risk, for which an additional premium would be charged by underwriters. But what about ships that entered before the area was declared excepted, but are detained and unable to leave the area? They were already impacted by the insured peril of detainment.

The question was whether it was justified to impose an additional premium on a vessel after it had been struck by “capture, seizure, arrest, restraint, detainment, confiscation or expropriation” and the assured had therefore lost the free use and disposal of the vessel. “My view is that it is at least problematic for underwriters to charge additional premiums for ships that were detained in Ukrainian ports as from February 24, 2022,” said Mr Fischer.

Suppose that for a detained ship the charterer refuses to pay the additional war premium, and the shipowner is unable or reluctant to do so. This means the war risk insurance would be cancelled, or the agreed policy period run out while the ship was detained and before expiry of the 12 months

stipulated by the detainment clause. “Is it a good idea to end an insurance contract at a time when the risk of being detained has already struck, but the claim under the policy has not yet materialised? Because this is what detainment constitutes: a peril with two components, namely an initial strike and a time element. Without these two ingredients a claim under the policy cannot materialise.”

There were similarities between a missing ship and one detained in a war situation, in the sense that both cases might eventually be treated as total loss. The Continuation Clause of the Institute Time Clauses Hulls 1995 provides for a missing ship to be held covered until arrival at the next port in good safety, or until made safe. There are good arguments to suggest that the “held covered” provision also applies if the vessel is finally found to be a total loss. “My view is that it might be a solution to adopt this practice for a war risks policy that contains a detainment clause, namely a provision that a detained vessel be held covered until the time that it is either free to leave or declared a total loss, at a pro rata monthly premium,” concluded Mr Fischer.

Note to editors: The Association of Average Adjusters promotes professional principles in the adjustment of marine claims, uniformity of adjusting practice, and the maintenance of high standards of professional conduct. Irrespective of the identity of the instructing party, the average adjuster is bound to act in an impartial and independent manner. The Association plays an important part in London insurance market committees and has strong relationships with international associations and insurance markets.

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