# CARGO DELIVERS

CARGO NEWSLETTER JUNE 2015


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# London Market Roundtable

To discuss the latest developments in the cargo market, we invited senior cargo underwriters Dave Allen from Aegis and Gavin Wall from Ascot to join Nick Peck and Daryl Mackay from JLT Specialty's Cargo team.

### What is the current climate in the cargo insurance market?

**Dave:** According to Lloyd's, cargo is averaging between 20% and 30% a year profit, which is why so many people are coming into the market. As a result we have massive overcapacity and whenever that happens, rates tend to go down. Another issue that overcapacity brings is a lack of underwriting expertise because there simply aren't enough experienced underwriters to fill all of the available spots.

**Gavin:** There is a tiered market now within the cargo market. There are traditional insurers and alternative capital, which – if it's a pension fund or similar – can actually hit a 4% return on capital. Traditional insurers can't do that because of the additional overheads, which are becoming more onerous. Plus while the new start-ups are not generally looking to lead business, they can provide support, which is reducing our share of existing business.

**Dave:** We also have to invest in big claims teams, and these new start-ups don't have to as most of them will not be leading business.

**Nick:** It will be interesting to see how long the new capacity providers are prepared to stay in the market. If they slash their rates to win business, they will inevitably build a book based on clients who are more inclined to move based solely on price.

**Gavin:** That's right. When you have a mature book, you know what your expense ratio is and how much your reinsurance costs are. So you know

# WELCOME



Welcome to the first issue of Cargo Delivers, our new regular newsletter rounding up the latest news and trends in the cargo insurance industry.

For our main feature, we invited senior cargo underwriters from Aegis and Ascot to join Nick Peck and Daryl Mackay from our Cargo team to discuss the latest developments in the cargo market.

On page 4, we look at the Claim Preparation Cover and why clients might want them written into their cargo policies.

We look at the importance of the recent RIMS conference – to us and our clients – on page 5, and meet new addition Tony Achinelli on page 6. We also explore the rise in expropriation claims, and how companies can help protect themselves.

Exclusions for cyber risks – and in particular the Institute Cyber Attack Exclusion Clause CL380 – have become a hot topic in the industry once again. I am on a panel debating the key issues at the International Cargo Insurance Conference this week. Find out more on page 7. Also on page 7, we look at how companies can prepare for the new Insurance Contract Act, which is coming into effect in August 2016.

On the back page, we look at issues around project cargo and how to insure it effectively.

We hope you enjoy the issue and we'd love to hear what you think, so please get in touch with any feedback.

**Gordon Longley**
CEO of Cargo, Specie and Fine Art
JLT Specialty Limited

automatically, in theory, for every piece of business what the loss ratio needs to be better than to be accretive to your bottom line.

**Daryl:** Despite the competitive climate you're operating in, your retention levels must still be fairly high?

**Dave:** We budget to lose 10% a year through natural wastage, mergers and acquisitions, competition from other markets and so on. But this year I think it will be higher than that; I'm probably going to lose 15% to 20% of my existing book.

**Gavin:** Our renewal retention rate is between 80% and 85%. The real challenge for us going into 2015 and beyond is to remain relevant to the brokers in a very crowded market place.

**Nick:** Brokers also have to decide whether to become a general, cheapest price wins-type broker or a broker that stands shoulder to shoulder with markets and strives to provide the best service to customers. We try to differentiate the leaders in the market, emphasising the price of not only having expert underwriters, but also expert claim services.

## What is the appetite of capital providers towards the cargo market? What are their expectations?

**Dave:** For Lloyd's overall, the average return on capital is 14% – way more than you can achieve in any financial field – so a lot of venture capitalists are coming in with a lot of money to spend.

**Nick:** Do you think that investment is going to be short term, if it is hedge fund-based?

**Dave:** Yes, it has happened many times before. Once they see the losses they exit the market, but at the moment the losses are quite benign. Also, because of the spread of business now, even what we would consider a big loss is only going to affect a certain number of people. We have suffered some big losses in the last couple of years, but they were not big enough to change the market, unfortunately.

**Nick:** For the capital looking in, they see a predictable short-tail class of business that turns them a profit, year after year.

**Gavin:** Our return on capital was 28% for cargo last year, versus a budget of 26%. Cargo is still a non-correlating attritional class of business. So if you are writing a portfolio of classes – which most syndicates do – cargo is still very attractive because of capital relief and it helps with business plan returns to Lloyd's.

## What is the profitability outlook for the London cargo market?

**Dave:** After four quarters, 2014 is at 65%, according to the current Lloyd's figures. At the same point, 2013 was at about 40%, so I think 2014 will be a loss year.

**Gavin:** I agree.

**Dave:** As for 2015, my guess at the moment is that it will be 85% or 90%, which is still a profit – but not as good as previous years.

**Daryl:** What about whether the market will harden? I don't see it hardening in the sense that we remember previous hard markets.

**Dave:** I don't think we are ever going to see 25% rises again. Plus if you look at the cumulative rate reductions of the last few years, they are unbelievable. If you have been on an account for 10 years and look back, you are probably on 30% of the original rate now. To be fair to the clients, however, some of them are taking on more risk themselves by taking higher deductibles or even setting up their own captive companies.

**Gavin:** A final point regarding reinsurance: some people are buying less to try and improve their bottom line as the market softens – and there have been some large reserve releases, which have buoyed some of the results that have been posted.

*Left to right: Nick Peck (JLT Specialty), Gavin Wall (Ascot Underwriting), Dave Allen (Aegis) and Daryl Mackay (JLT Specialty)*

## Will there be more consolidation in the insurance or broking sectors?

**Daryl:** Certainly on the insurance side, yes.

**Dave:** If you can't grow organically from within, the only way you can grow is by acquisition. And that is exactly what seems to have happened with Catlin and XL. In my view, that will not be the last one.

**Gavin:** I agree. With the increased obligations of PRA, modelling, Solvency II and so on, there is a very simple way of getting around those additional costs and that is through mergers and acquisitions.

**Nick:** For similar reasons, there have been pretty significant mergers happening in the broking market, including the Willis/Miller merger. A pure wholesaler trying to achieve scale is extraordinarily difficult and the larger broking houses are now actively looking at the attractive third party independent broker space – which they can't access because not everyone wants to be with Marsh, Aon or Willis – so there is bound to be an increasing likelihood of further mergers.

## Are there any trends in claims activity?

**Gavin:** We have seen some large car losses, both in transit and storage, which is partly due to the recovery of the car market. A fundamental problem with car accounts is that if there is a loss, it tends to be a total loss because of the manufacturer control of damaged goods clauses. Apart from that, we have seen an increase in Brazilian fire losses, as well as some issues with warehouse operators in China. Such issues will continue as long as Lloyd's exposes itself to these emerging markets, where there are different risk management standards. Hopefully as a market we can learn and improve with the cedents and clients, helping them to improve their risk management processes.

**Dave:** The issue I have on claims is the number of general average advices. For any figures you look at, there are probably up to 50 general averages included that are probably reserved at zero at the moment – as it is very difficult to set reserves for them.

**Nick:** Another trend we have noticed is that the amount of legal activity is increasing when a claim hits a certain amount – maybe half a million upwards. That's a factor we are conscious of when advising clients; sometimes they should be paying a little bit more to be with people who are actually going to do what the insurance contract is all about, which is to pay valid claims without fuss and without delay.

**Dave:** In terms of paying claims, our view is that we should try to pay claims as quickly as we can. I think most of the market has come to that view too. Also, most of us are quite happy to give brokers claims authority because you tend to have very good claims people working for you and it makes the process quicker.

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# What is Claim Preparation Cover?

A claim preparation clause provides coverage for the insured to engage a specialist claims professional to help prepare, present and settle large losses. This clause can be written into cargo policies as an extension to the existing cover.

This clause provides the insured with specific and a specialist skill-set to work hand in hand with JLT's claims specialism to ensure, for the right type of loss, they are entirely represented.

This coverage has been commonplace in the USA, Asia and Europe for many years but UK insurers have been slow to catch up. Although still not uniformly available, it is gaining traction with many UK insurers now providing the cover.

It is understandably popular with insureds who appreciate the benefit of having professional support when a large loss occurs. Insurers are also recognising that it makes a positive difference to the claims experience of their customers.

## WHY IS IT BENEFICIAL?

Insurers demand high levels of forensic evidence in support of claims. When a loss is notified, insurers may appoint a large number of experts to investigate all aspects of the claim in great detail. The burden of proving the claim falls squarely on the insured who has to fully evidence and document both the cause and value of the loss. This is at precisely the same time as their primary focus is on business recovery, maintaining existing contracts, their customers and reputation.

Many insureds expect that presenting spreadsheets itemising the claim or a schedule of invoices and estimated losses is sufficient evidence of their loss but the reality is very different. Insurance policies incorporate conditions that insureds must comply with to substantiate their claim. They must provide full and granular evidence of the losses sustained which will typically include information such as supplier and customer contracts, estimates, invoices, purchase orders, financial accounts, stock details, historic budget, actual and forecast revenue and business trend analysis. Insurers may also request other evidence as may be appropriate to the particular circumstances of loss.

Providing raw data alone is not sufficient – all documentation must be fully explained and properly presented under the relevant heads of cover.

Failure to evidence the claim to the insurer's satisfaction can lead to protracted negotiation and a reduced settlement – resulting in disappointment and dissatisfaction that the policy did not respond as expected.

Appointing an expert who understands the working practices and information requirements of the insurance market and who can apply this knowledge on behalf of the insured to deliver an effective and expedited claims settlement process is therefore of immense value.

## THE CLAIM PREPARATION COVER

The cover is usually intended to operate in respect of "large" losses. What constitutes "large" will depend very much on a number of variables including the type of loss and the industry sector concerned but typically the clause would apply where the loss estimate is above GBP 500 thousand or GBP 1 million.

The wording may be similar to the following:

> *"In the event of an occurrence giving rise or appearing likely to give rise to a claim hereunder, this contract is extended to include expenses incurred by the insured, or by the insured's representatives, for preparing and/or certifying details of any such claim hereunder."*

## VALUE TO INSURERS?

We have seen huge focus on insurers' claims service in recent years as they seek to demonstrate that they 'Treat Customers Fairly' whilst at the same time striving to improve their service in response to increasing criticism over their willingness to pay.

It seems only logical and reasonable that insurers should offer their clients a claim preparation product that truly does strive to deliver a proper indemnity by encompassing the costs associated with the handling of a major claim.

This coverage helps insurers to demonstrate that they both understand and are committed to helping their insureds through what can be costly, time-consuming, high profile and hugely disruptive insured events. This is not merely about resolving a claim. It is about taking the long view of customer relationships; about insurers stepping up to the plate when policyholders expect them to.

For insurers, offering claims preparation cover is a small cost for a very big win.

Claims preparation clauses ensure that policyholders get professional claims representation with appropriate financial contribution and support, resulting in reduced management time and ensuring they get their proper entitlement under the policy. Does your business have claims preparation clauses written into its insurance policies?

## THE COVER IN ACTION

In December 2013 a tidal surge event resulted in severe flooding of premises where the client received and processed fertiliser material. There was widespread damage to raw material, work in progress, finished goods, plant, machinery and building assets. The client held Property Damage (PD), Business Interruption (BI) and Stock cover.

Working under a claim preparation clause, JLT Specialty's large loss practice, Echelon Claims Consultants, provided support in evaluating, preparing, presenting and coordinating the claims across all three policies.

The particular challenges faced by the insured on the claim included:

- the logistics of sorting and assessing in excess of 5,000 tonnes of damaged product;
- maintaining the operation and recovery of the business;
- dealing with assessment and disposal of licenced product containing hazardous ingredients;
- brand protection relating to specialised products;
- determining the salvage value with Insurer's appointed surveyor;
- mitigation plans to minimize impact on future business;
- the interface between Stock and BI coverages.

Echelon attended site meetings with loss adjusters and marine surveyors and established a clear and transparent dialogue regarding the allocation of the claim between the PD/BI and stock policies.

Throughout the claim preparation process, they liaised closely with the appointed loss adjusters, obtaining their agreement to key decisions taken as recovery progressed, to minimise the possibility of disagreement at the point of final settlement.

They resolved a disagreement regarding the correct basis of valuation under the stock policy and kept the client's board appraised of developments and strategies, enabling them to understand and plan the cash-flow impacts of the claim.

They presented regular interim claims which assisted cash flow and the loss mitigation programme.

## THE OUTCOME

The accuracy and robustness of the claim submissions together with favourable resolution of policy coverage issues resulted in a full indemnity with only minimal adjustment made by the loss adjusters for the insured to retain salvage and payment of all relevant salvaging costs.

The total cost of mitigation strategies to maintain production during the recovery period and protect future revenue and profit, were recovered in full.

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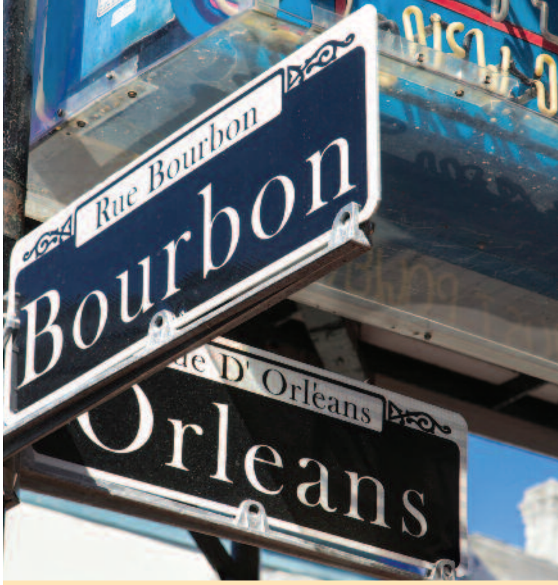
Echelon Claims Consultants are a dedicated team of expert claims professionals, solely committed to settling major losses on behalf of policyholders across a wide range of industries.




# Networking at RIMS

Five senior members from our cargo team attended this year's RIMS conference in New Orleans.

The RIMS 2015 Annual Conference & Exhibition, which was held at the end of April, is the largest and most prestigious insurance conference worldwide, attracting around 10,000 attendees every year.

While the event offers a range of educational seminars, keynote speeches and an exhibit hall, the real value for JLT lies in the networking opportunities, says Nick Peck, Chairman of Cargo, Specie & Fine Art at JLT Specialty.

"We go to RIMS because all of our clients – mainly independent US retail brokers and their clients – attend, making it an extremely useful opportunity to introduce them to insurers from London. It's vital for showing our client base that we're really engaged with them, and that the major markets we present to them are equally engaged."

He adds: "It also provides a great opportunity for clients – away from the stress of renewal – to talk at a high level to brokers and insurers about their challenges."

# Meet Tony Achinelli

## WHEN DID YOU JOIN JLT SPECIALTY?

I've been here for just over two months. I used to work for JLT Group many years ago, but it was in a different role and department and things have changed a lot since then, so it feels like I'm brand new.

## WHAT DOES YOUR ROLE INVOLVE?

I'm a partner in the Cargo, Specie & Fine Art team. My role is predominantly about production; I'll be travelling extensively in North America (about one per month), nurturing our relationships with the independent brokers that make up a very large percentage of our book. I'll also be developing new relationships of my own, as well as carrying out client work and broking in the market.

## WHAT EXPERIENCE DO YOU BRING TO YOUR ROLE?

I've worked in and around the insurance market for nearly 18 years, and I've been specialising in cargo for 11 years. I started at Heath Lambert as a very junior cargo employee, gradually gaining experience and responsibility. I then went to Aon for eight years, eventually becoming head of the cargo division.

## WHY DID YOU CHOOSE JLT SPECIALTY?

The cargo team at JLT Specialty is known as the best in class, so that was the big attraction for me. Now that I'm here, the strength and depth of the team has been eye-opening.

## WHY CARGO?

I fell into it – but I stayed in cargo because every client and every day is different. One minute I might be dealing with a pharmaceutical company, and the next I might be dealing with an agri account shipping wheat. Cargo is also interesting because there are lots of variables, such as the need to stow items in a certain way or at certain temperatures.

## WHAT INTERESTING PLACEMENTS HAVE YOU WORKED ON?

One that stands out was a placement for a very large crane manufacturer that acquired an operation in Europe (in a hostile takeover). I had to work very closely with the client's risk manager and the insurer to arrange the global insurance programme and ensure that the integration went smoothly. It was a long, tough process but we got it done – and all at a price that was more than acceptable to the risk manager and the board.

## WHAT'S HAPPENING IN THE CARGO MARKET?

The market continues to see no shortage in capacity with various new start-up operations coming in to Lloyd's over the past 18 to 24 months. What this does mean though is that should clients require excess of USD 1 billion of cover we have the ability to get that done for them. Rates have continued to fall over recent times, although it is considered that they are now at their lowest point. We are however seeing some reductions for the right client base.

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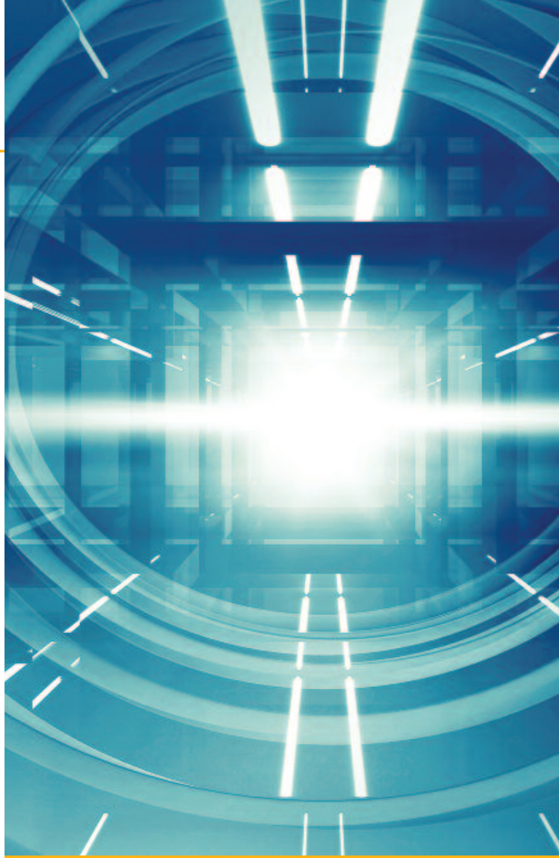

# Expropriation

The global nature of modern business means that there are many more factors beside finance that need to be considered. It is necessary to provide greater consideration to local sensitivities when investing in an international venture, social considerations and also political risks.

This is particularly prevalent in energy, mining and other typically internationally focussed industries. The oil industry is perhaps the most impacted sector. The current economic climate and political outlook post 2008 has changed and we are seeing more expropriation claims. Assets and natural resources are viewed by some governments as a way to loosen the shackles of austerity.

This is likely to be an increasing trend. As more money is committed to projects and various nations are still deep in austerity measures the expropriation of valuable assets is only due to increase.

JLT has crafted a considered solution to such issues. We make use of risk transfer and funding to allow claims to be investigated and then pursued if meritorious.

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# Cyber risks in the spotlight

*Are cyber challenges real or science fiction?* That's the hot topic Gordon Longley, CEO of the Cargo, Specie & Fine Art team at JLT Specialty, will be debating at the International Cargo Insurance Conference this week. Four members from our cargo team will be attending this year's conference.

Longley says: "The current focus on cyber challenges stems back to the early 00's when, following Y2K and 9/11, the market had concerns about cyber attacks causing a potential aggregation of losses they could not manage, so they came up with the Institute Cyber Attack Exclusion Clause CL380."

Longley continues: "Introduced by a reasonably hard market at the time the clause was openly criticised from a number of areas for being too widely drafted and with seemingly little thought given to resultant physical damage as opposed to say loss of personal information, loss of trade secrets and data fraud."

The clause was not mandatory, but lots of brokers did accept it. "However, we refused to accept its inclusion on a blanket basis," says Longley. "We argued that it was not reasonable that general cargo loss, for example theft of cargo from whatever cause or loss resulting from malicious acts which have historically always been covered under a standard 'all risks' form should suddenly fall foul of this new language. Is it reasonable for example to potentially exclude loss by reason of collision of a vessel which might be the result of an isolated incident of someone hacking into its navigation system or an opportunistic theft from a location who's security system may have been compromised by a virus? It's all about protecting the innocent assured."

This issue cropped up again in 2014, after a number of high-profile cyber attacks, including those against JPM, Sony and the use of the 'Stuxnet' virus to name but a few.

"This alerted the reinsurance markets to look at the issue again," says Longley, "and they started asking insurers if they had the CL380 clause in place with their clients. Lloyd's then asked all insurers what their exposures were to cyber risks, and how they were managing them."

All of this put cyber risks firmly back on the agenda. "We've now come full circle to 2002/3," says Longley, "with underwriters trying to insist on CL380. However, we're firmly pushing back as we did before, because the fundamental argument has not changed."

In essence, we still believe CL380 is not fit for purpose in its current form, says Longley. "We would prefer that there is an open dialogue with assureds at the time of any placement regarding cyber risks. If then underwriters want a clause to deal with subsequent events (such as a ship grounding after being hacked), they will need to come up with a suitable wording that brokers are happy to talk to their clients about."

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# Preparing for the new Insurance Contract Act

A new Insurance Contract Act comes into effect in August 2016, impacting insurance contracts governed by the laws of England and Wales. Designed to reflect modern business relationships and the changing nature and diversification of risk, it is intended to rebalance rights and remedies when things go wrong.

The new act makes a number of changes to existing legislation. It places a duty on the insured not to make misrepresentations and to make a fair presentation of the risk. It also formalises the requirement to disclose every material circumstance which it knows or ought to know. Insurers must be given sufficient information to make further enquiries about a risk if deemed appropriate.

Under the new law, an insured is assumed to know what is known to its senior management and insurance purchasing teams. The duty of good faith remains, although a breach of this duty will no longer automatically entitle the insurer to void the policy (unless the breach is deliberate or reckless).

We recommend that organisations with insurance policies governed by the laws of England and Wales prepare by examining the information that they provide to insurers to ensure that it complies with the new act's expectations.

From a global perspective, while there is no immediate impact, the changes that have been put in place could filter out to other markets in the longer term given that they help to level the playing field for underwriters.

Our brokers are working with clients to ensure that the information that they are providing will meet statutory requirements.

*For more information visit*
*www.jltspecialty.com/insuranceact* ■

JLT Specialty Limited provides insurance broking, risk management and claims consulting services to large and international companies. Our success comes from focusing on sectors where we know we can make the greatest difference – using insight, intelligence and imagination to provide expert advice and robust - often unique - solutions. We build partner teams to work side-by-side with you, our network and the market to deliver responses which are carefully considered from all angles.

The Cargo, Specie and Fine Art team are leaders in the London and International market and provides specialist programme design and transactional services to a broad spectrum of industries around the world by combining in-depth sector expertise with innovative claims solutions.

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# Protecting Project Cargo

Project cargo is the transit of very large or heavy equipment around the world, such as blades for wind turbines, equipment for power stations or sections of rail track. On average, around 10% of these items are critical, bespoke pieces of equipment that would severely delay a project if they were damaged in transit.

"The process for transporting such equipment is complex because the items can be large and/or have unusual centres of gravity," says Jay Payne, Senior Partner, "plus they may require assembly or disassembly during the transit, all of which present increased risks."

## A BUYER'S MARKET

Project owners can mitigate the financial risks by buying project cargo insurance, which usually includes delay in start-up (DSU) cover for expenses such as loss of profits, fixed costs and debt service.

The London market currently has plenty of capacity for such cover – it has increased by a third in recent years. "Project owners can now buy up to circa USD 1.3 billion of combined physical damage/DSU insurance," says Payne. "As DSU indemnity amounts tend to be far higher than physical damage losses, a typical project owner might buy USD 100 million of physical damage cover each and every loss and six or seven times as much  DSU cover."

The availability of capacity – along with the sector's good reputation for managing risks – has contributed to rates falling to almost half of what they were in 2010.

## HONING YOUR COVER

A project cargo policy covers items during their transportation; as soon as they are delivered to the project site, the client's construction cover takes over. "Therefore, it is crucial that the project cargo policy dovetails with the Erection All Risks policy to ensure seamless coverage," says Payne.

An important element of this is agreeing a 'loss sharing' system for any losses that are discovered after delivery, where it is unclear whether they have been caused in transit or on site.

Some project owners also extend their insurance to include Blocking and Trapping cover. "This is useful for those whose normal shipping routes may become blocked," says Payne. "In one example, the port of loading was blocked by a stricken vessel which prevented a ship from sailing resulting in additional chartering expenses."

## EFFECTIVE RISK MANAGEMENT

Despite the range of unusual risks involved, the sector has gained a reputation for effective risk management. Payne says: "For example, while normal cargo is shipped all over the world often without surveys, multiple project cargo surveys are carried out throughout the process, and there are always specialists on hand to ensure items are being handled correctly."

In addition, for critical pieces of equipment, an independent marine warranty surveyor is employed to undertake the load, stowage and discharge surveys.

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