



THE NEW INTERNATIONAL HULL CLAUSES: THE CLAIMS PRACTITIONER'S VIEWPOINT

Transcript of a Seminar

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PRESENTATIONS

MR. PETER McINTOSH:

I notice there are very few underwriters here so there is a very high probability that most of the people will have read the clauses. I think a lot of you came to the earlier presentations that we did from Joint Hull. I am going to use some of the material, so I apologise if you have seen them before, but I want to talk a little bit about why we did some of the things we did.

The first issue is the background to why we took the initiative to do a rewrite of the clauses; what were some of the processes and why some of the issues we put into the process of rewriting, and the result of that. The main drive really for why we did rewrite the International Hull Clauses, or the ITC as was, is that we felt there were a lot of changes going on in the shipping industry and in the insurance industry. ISM is a well publicised and obvious one. There is a big drive to try and enhance safer shipping and improve the industry as a whole, so we saw with a lot of both legal and practical changes going on that there was an opportunity to try to incorporate some of these into a redraft.

There was a whole raft of alternative products being launched both in London and internationally. It was felt that some of these had some assets and it was worth looking at those. We also felt that after sustained period of soft market, six years of poor trading, that the London insurance market had lost some ground. We also thought in terms of trying to put together a platform to evolve any new and relevant initiatives going forward, so we felt that there was a good opportunity to put a base together to try to leave foundation for future amendments. Also, a very critical issue is the LMP, the London Market Principles, which has been a drive within the London insurance market to improve the overall efficiency and speed at which we do our business, with ultimately the goal to try to improve settlements.

We talked a lot about All Risks insurance and whether or not the market had the desire for an All Risks policy. There very much seemed to be a lack of enthusiasm from our marketplace, and it is not surprising really after the sustained soft market to try to not only push prices up but to change a Named Peril policy into an All Risks form. When we spoke to a lot of the buyers and their agents, the brokers, it was felt that the Named Peril form that we had all grown accustomed to in ITC had actually served us pretty well. There was a lot of precedent and case law and a lot of adjustment and claims practice that had been established through many, many years, so in fact a lot of the clients were very happy with the Named Peril policy; plus, the lack of appetite from the London underwriting fraternity to convert to All Risks. We felt it was very prudent and necessary to keep to a Named Peril very similar to the ITC. In fact, as you all can see, the change is minimal in the Name Perils.

I will skip through the process, but we did set up a steering group, in which some of my colleagues on today's panel were involved, and various working parties. The main reason, or the main why behind the working parties was to try to get a cross-section from the market, from the brokers, claims practitioners, underwriters, underwriters' claims practitioners and the adjusters, as well as a legal input from Hill Taylor. As I think most of you know, there was a very extensive session of consultation with ultimately the buyers of this policy and culminating in the final draft and the launch on 31st October.

The result: I am skipping around a bit, but the result is that we have ended up with three distinct sections, as you all know, yet integrated. The reason we wanted to do this was to keep, as I say, the main Name Perils and the insuring conditions as one area, yet bringing in all of the additional clauses (which I will talk a little more about in a moment) into what we originally called the

addendum section, the part 2. The view here, and why we took this stance, was to try to give this a platform for any changes that may need to be incorporated or are desired from a buyer's point of view to be incorporated in the future, so part 2 really was going to be not quite a blank form, but an open form that things could be appended to as we saw fit at each annual review.

The claims provisions, which obviously is one of the main interests today, we will talk about in a little more detail in a moment. Just as a synopsis of what we think the result will be and why we really tried to aim to achieve some of these, I will say that there has been a lot of feeling in UK law at the moment that warranties are somewhat outdated, so, in keeping with the change in the fundamental view of the courts, we have moved away from warranties. Most slip policies that are written today include reams of broker clauses or underwriter driven frequently used additional clauses. In keeping with trying to improve the efficiency, we thought that if we can incorporate the most commonly used of these additional clauses on a standard form, rather than having a multiplicity of different broker derived clauses or underwriter derived clauses -- and as I said earlier, we retained the traditional perils and that really was a very deliberate act and we hardly tinkered with those at all, because we did not want to rock a lot of practice that had been established over many years -- a lot of the reasons for doing the changes that you can see on the slide here were common sense driven.

When I asked at the steering groups and the various working parties nobody could actually say why the perils were actually ticked away halfway through the policy, so we put them into a more logical order, and the perils now are the first thing that you come to.

Latent defect will be touched on by one of my colleagues on the panel in more detail later. The changes in the insurance terms here came about through a court ruling on *The Nukila*, which we touched upon in the earlier presentations.

Regarding the onshore management clause, which was a terribly unpopular change put into the 1995 version, we listened over the last six or seven years to what the market wanted and we have amended, as you know, the onshore management to a softer stance relevant to the 1995.

Class & ISM: I think this is more in keeping with the whole drive within the industry of not just insurance but the shipping industry to try to support safer ships and safer shipping and the operation of safe ships. We have incorporated what we feel are nothing more than the sort of mandatory standards under which ships are asked to operate in most legislations around the world today. Equally, the management clauses reflect our view on that.

Part 2: In time I think part 2 will grow. We have put in the old Institute trading warranties which are as we speak being modernised and worked upon. They are now called the Navigation Limits. We felt that these are very much a critical part of the clauses, so why should we not include them in the standard policy? We put a premium payment term in there, and I think it is pretty obvious why, and it is a drive again with trying to expedite the settlement of claims and the LMP process. It is pretty critical that we get the premium, and that we get it fairly promptly.

There are a whole load of optional extensions and we at the various working parties talked about what extensions we should give as mandatory cover and over which ones we would like to retain the ability to negotiate on a case by case basis. These have been put into the part 2. The reason we put them in there was so that there is a standard set of words that can be used if those options are desired by the client and then negotiated through the broker. As I said earlier, there is a framework there in part 2 at each of the annual reviews. If through practical experience or a change in legislation governing insurance or shipping there is a need to enhance a clause, we can do it via the part 2.

Part 3, the claims: We felt there had been various initiatives over the years

to put together claims protocols. The most recent in the last 10 years in have been two which have both been unsuccessful, so we tried very much to find out why they had been unsuccessful and where they fell. We felt the basic desire behind them was a good one. That is why we felt it important to try to bring something into the new clauses without making some of the mistakes or errors that were put into the previous protocols. If I can take you through some of the reasons we put in these various sections:

A leading underwriter clause is pretty simple and in today's world, where very few policies are placed 100% in one market, to have a leading underwriter clause was the aim of this. It was to try to expedite dealings between the assured via his broker and the underwriter in order to get a quick settlement of legitimate claims without being bogged down in realms of leader's agreements and following market co-subscription agreements.

The fee collection charge. Having listened to the market, the adjusters, the surveyors and the lawyers, and other professionals that are employed to help the whole system, it was noted that it was becoming more and more difficult to collect fees efficiently, especially with smaller orders in London. The brokers, rightly so, were finding it more and more of a task, and not cost-effective, to collect these fees. I think we have acknowledged that and put into the part 3 a charge that it can be agreed, if that is the broker or a third party collection service, but it is there now for future use.

A notice clause, which was a fairly political issue in the 1995 clauses, has remained in form, and I think it is only right. Our thinking was that in today's world of technology, it cannot be very difficult for somebody to advise us if there has been an incident that is likely to give rise to a claim under the policy. There was a lot of debate, as you can imagine, between the various parties as to the length of time involved, and we compromised at 180 days. It is a lot softer than it was in the 1995 clauses, but the thinking behind it, really from the underwriter's perspective, is that we need to manage our business. It is not unreasonable that we are advised within a time frame, albeit a generous time frame, of something that may give rise to a liability to that underwriter. That is really our drive, so that we can manage and account our business more efficiently.

Existing duties of assured: In the clauses there is nothing that we felt was different and it is merely a formalisation of what we felt was already enacted and in place on a practical level. Equally, we have tried to clarify and give some of the duties that the underwriters will respond to.

In order to help show goodwill (and this is possibly a PR stunt but it is very much a real part of the clauses) we have undertaken within this to give a decision. A decision is not a payment, but a decision of what we will do, within 28 days of submission of the full and final adjustment. I think this is a great step away from where we have been before and it very much for me summarises the desire from the people involved in the drafting of these clauses to try to show a willingness to pay legitimate claims and pay them promptly. I think this is a big key and a great asset.

Security has always been a well debated issue in the London market. I think this stems from some of the difficulty we have been having with different overseas security and spread description markets. We acknowledge that there is a need on occasion to offer security. Like all other types of business, P & I for example, we have kept this discretionary. A lot of people did ask us if we would make this a mandatory field but the circumstances that governed the issuance of security varies so often that we could not make that mandatory, but I think that is a step and another intent, and that was our reasoning behind it, to show willing.

The recoveries; this goes both ways. Because of law we felt that it was important that the rights of recovery should be protected and should be worked

on with the assured to protect all interests. The reason we have change the pro-rata on the recoveries was in order to show that to co-operate with the assured in seeking recoveries, we would be prepared to offer a pro-rata recovery.

ADR is a relatively new, within in the last 10 years, but growing phenomena, and we have acknowledged that by putting it into the clauses. Again, think I this shows a desire to try to cut down on costs if there is a dispute.

In summary, we have retained the Named Peril policy, albeit we have set I think a platform to continue the debate about changing it to an All Risks policy. There has been a lot of discussion about whether or not the new version of the IHC is in fact not All Risks but as close as All Risks, with some exclusions as is possible. I would be interested on the floor's view on that. Previous versions of the clauses are still available and as I say, there is a platform for any future change.

I think one of the JHC's main drives here, as I said earlier, was to continue the debate on what, from all parties involved in the marine insurance, is wanted and what can be done going forward. I think what we have achieved in the last six months gives us a great platform for that going forward. The main drive and a good conclusion of that and why we really, our raison d'etre behind the whole thing, was that good operators should have nothing to fear but much to gain from these new clauses. Ultimately our drive was to make an easier and more easily understood set of clauses that allowed faster and more expedient as well as cheaper settlement of claims. Thank you.

MR. RICHARD CORNAH:

Our chairman volunteered me for this task with the encouraging words that it was nothing too taxing, just a quick ten minute gallop through part 3 of the new clauses. The last time I was invited for a quick ten minute gallop was in 1975 at 3 o'clock in the morning towards the end of a hunt ball. Sadly I was in no condition to take up the young lady's very kind offer, but I could not think of a similar excuse on this occasion. These are obviously personal views and time alone will tell what actually happens in practice. An average adjuster's view was requested, so here goes: There are lots of new bits, but do not panic. Well, there you have it really. Those of you that wish to can now think about more important things for the next nine minutes while I try to descend from the general to the particular without duplicating Peter's comments too much.

One general observation, which I think is quite important, is that one of the questions or comments that was made very often was: Why there was quite so much stating the obvious in the new clauses, or stating things which were already happening? I think actually these extra parts are very important. Marine insurance has long been viewed as something full of arcane mysteries which were only understood by specialists. I do not think that is any longer a sustainable approach. Of course, marine claims and marine law can be complex, but that is surely all the more reason to set out the bits which are straightforward, the procedural matters, which show how the basics work. Thus, it is good to see that marine insurance is keeping up with commerce in general and public life, and indeed with advertising, by doing what it says on the tin.

The opening clause in part 3 really has nothing to do with the assured but it is a good example of this kind of transparency. We obviously spend a lot of time working with assureds based in other parts of the world who may be coming into the London market, perhaps a little fearfully. They may be used to domestic markets where local insurers do a great deal of hand holding and where the relationships are very close, so they are moving to the other side of the world and to a new system. I think this kind of transparency is very important for

those overseas assureds. It also means that the key relationship is with the leading underwriter. Like all key relationships, you need to be careful and thoughtful about who you hook up with for a long time. It should give even further benefit to assureds who are prepared to sustain long term relationships with their insurers and vice versa. I think over the last 25 years I have absolutely no doubt that assureds who have been prepared to stick with insurers and indeed their brokers in the long term, rather than chop and change every five minutes for a few dollars here and there, in the long run have done much better with claims. Of course, they have also done rather better when the hard market times come.

So far as notice of claim is concerned, again 46.1 really takes us to nothing very different from what we had before. The requirement for a surveyor to be appointed as soon as possible after the assured, owners or managers become aware of the incident is plainly common sense, and it helps to get the case off on the right footing. Peter has explained the reasons for the "within 180 days" requirement. It is important these days for insurers reserve policies, and so that they understand the full potential position of their exposure, renewal times and so on. Obviously, the 180 days is a compromise, and I think not an unreasonable one, but there are some areas in which you do need to strike a balance. The clause does provide that leading underwriters may agree to the contrary in writing if the 180 days limit is missed.

As an example of the kind of circumstance where a balance needs to be struck, if you think in terms of a momentary loss of stern tube oil, perhaps on a touch and go grounding; a diver's inspection reports little damage and the owner, who has a very large deductible, thinks nothing more of it. When the vessel dry docks two years later, you may find there is extensive damage to the tailshaft. I would hope that the interpretation of this clause is going to be based largely on the awareness of the loss or damage, rather than the "accident or occurrence". That would seem to me to satisfy the requirements from both sides. If that is indeed the intention it may be something to go on the list for changes when the next review takes place. At the moment, I would think it should not cause any great alarm.

Tender provisions are exactly the same as ITC Hull's clause 10. A general comment in passing, is that it is of course sensible for owners and operators of specialist vessels to talk to their insurers if there are any reasons that this tender clause is going to cause them difficulty. There are some kinds of specialist tonnage with special requirements for repairs and some times you have governmental restrictions on where you can repair a vessel. Again, that is an issue that can be addressed at the time of placing.

Coming to the duties of the assured, the initial part of clause 48 simply reflects the existing burden of proof. The assured has to provide reasonable amounts of documents in any case to show that he has a valid claim. It is section 48.3 which is causing a little bit more concern. That is because it appears to, if you like, imply potential dishonesty on the part of the assured. The clause is saying that, "it is a condition precedent to the liability of underwriters that the assured shall not at any stage whether legal proceedings have commenced or not knowingly or recklessly mislead or attempt to mislead the underwriters by relying on evidence that is false. Also, he must not conceal any circumstance or matter which might be material to the proper consideration of the claim." .

As a condition precedent, obviously this is a very serious matter, but in fact there is really no difference between what is reflected in the clause and the common law position. It has been settled English law for a considerable amount of time that even if you do not have a "fraud clause", (which we now see in lots of non-marine policies), if you present a claim fraudulently or indeed part of a claim fraudulently, you will forfeit the right of recovery entirely. Therefore, if anything, clause 48.3 is a reminder of what the legal position is. I think I am right in saying that the only new aspect of clause 48 is in the brackets at

the beginning, where it talks about whether legal proceedings be commenced or not.

In the House of Lords in the *Star Sea*, the House of Lords said that duty of good faith continues after the conclusion of the insurance contract, but once you are in litigation then ordinary court rules apply. The words in brackets here amend the legal position but otherwise, so far as I can see, there is nothing else in clause 48 that does. The clause refers to "the assured". Usually that is bracketed with managers and so on, but they are not referred to. I think we are used to defining the assured in other clauses (such as the due diligence proviso) on the basis of a case called the "*Eurysthenes*", where you are talking about the head managing parties of a company. So for this clause to take effect, it would have to be someone from the top management of the company who was both knowingly or recklessly doing the things which obviously he should not be doing. Therefore, it is not going to put an assured's claim in jeopardy because a superintendent or some employee within the company tries to do one of the things which are clearly prohibited.

The duties of underwriters appointing surveyors: Again that is something which happens now and is an important part of the whole claims process. The early appointment of surveyors gives one the technical facts to build the rest of the case on. I often find that if I am asked questions from colleagues within our group, in our technical committee, that I think at least 9 out of 10 of those questions are solved by a proper investigation of the facts. Once you have sorted out the facts, the points of principle tend to answer themselves, so I think the continuing role of surveyors, and of good quality surveyors, is extremely important in the claims process. One of the more frequent reasons for a claim going wrong is often that the surveyor misunderstands his brief or is simply not technically up to the job that is required in a complex case, so they are very, very important people.

Talking of important people: independent adjusters. Obviously, it is a very welcome part of the new clauses and we were very pleased to see it when the early drafts came out. I think it is also a very important message for potential customers for the London market that this market is prepared to say that if you come with a claim to us, we are prepared to see it adjusted by an independent party, and what is more, we are prepared to pay the fees of that independent party. I think in any other kind of insurance or business, people would see that as a very considerable benefit to the customer. In other words, the Assured has a sort of maritime *Esther Rantzen* on his side from day 1.

The other things: Again, status reports, yes we are asked for them and hopefully we give them promptly; payments on accounts are very important; and the 28 day decision time, obviously universally to be welcomed. It refers in fact to receipt of the average adjuster's final adjustment. I would hope in practice the spirit of the clause means that a similar kind of target period will apply to payments on account. Certainly I think many adjusters, if there are difficult areas in a claim, will try to highlight them at an early stage and very often payments on account certificates are an appropriate way of doing that. A number of people commenting on the clauses to us have said that it is all very well saying that, but why do we not have penalty interest and so on? In an ideal world an assured may think that, but it remains a very important mission statement from insurers, and I am sure that all the brokers present will hold them to it with the utmost rigor.

The provision of security: Again, I believe this is on the basis of an existing JHC clause. It requires counter-security, counter-guarantees, and it may involve mortgagees. I know issues of security can be a point of quite some difficulty. Particularly again with assureds who come to London from other markets, where the relationship with the insurer is very close and guarantees seem to be given almost immediately without question, so having something set out in the clause is I think very useful there. I am surprised that very often

assureds do not do more to clear the groundwork with people like mortgagees in terms of counter guarantees. Everything seems to get done in a rush when the need for a guarantee becomes clear. If your favourite Swiss banker has gone on a two week skiing holiday that can cause some problems.

I will go on now to recoveries. Clause 52 sets out a number of things which the assured must do in terms of assessing prospects of recovery, protecting third party rights, keeping underwriters involved and co-operating with them in taking steps to pursue claims against third parties. Again, cargo clauses have had similar stipulations in them for an awfully long time. Under Section 79 of the Marine Insurance Act, subrogation is a right which only accrues on payment and I think this clause reflects a desire to ensure that the whole recovery process is properly managed from day 1, even before underwriters actually make any payments.

The sanction: What happens if an assured does not do all these things? My belief would be that (as I think is now fairly settled opinion with regard to Sue and Labour claims) if an assured fails to Sue and Labour, the view is that the sanction for underwriters is a counterclaim for damages and it does not go to the root of the claim itself. I would assume that the position would be the same here. There is no specific sanction set out in the clause, but I can see nothing here which will go to the root of a claim, but I would imagine that a counterclaim for damages would be the right sanction. That is a legal point which perhaps Tim can confirm.

The good news, and something which is long overdue, given the way in which deductibles have changed over the last decade, we are getting rid of the old top down approach to recoveries and, as my typist wonderfully typed and I have not corrected it, we can now say "bottoms up" to recoveries. I think this is a matter of equity. It is a much fairer way of dealing with recoveries, and as I say, I think it is long overdue. If I can just illustrate it very briefly, with an example: Where there is a PA claim for \$1 million, there is also a demurrage claim for 0.5 million and we basically succeed in recovering 50% of the total, we have a deductible of \$100,000. Under the old clauses underwriters would receive the recovery up to the amount they had paid, so they would get \$500,000. Under the new provision, the amount settled by underwriters receives a proportion of the recovery. The rest of that recovery is shared by the deductible, although having talked about large deductibles I seem to have included a fairly paltry one of \$100,000 on the slide. Even then you can see that the assured is, as a matter of a much more equitable approach, benefiting from that recovery as well as the insurer.

Finally, on mediation and ADR, I recently wrote a commentary on the new clauses, and I concluded rather smugly that Average Adjusters have been providing a form of mediation for the last 200 years, and I do not see why I should spare you that smugness either. What we do is a form of meditation, but of course it is very welcome that, as a matter of official policy within the clauses, mediation is seen as a first step to resolve serious disputes, whether over adjusted or non-adjusted claims. That, I think again is going to be welcome both in practice and as a declaration of intent on the insurers behalf. That concludes the 10 minute gallop. Thank you very much.

MR. MICHAEL HARVEY:

Good afternoon ladies and gentlemen. My intention is to highlight two practical adjusting issues which may arise from the new clauses. These are my personal views and I hope they will perhaps stimulate some discussion later. Just to show that my colleagues are not alone in producing fancy presentations (presents fancy presentation), first of all, I want to look at latent defects. There will be a little bit of sucking eggs here, but I think it does no harm in reminding ourselves of some basics.

A latent defect has been defined as a defect that would not be recoverable on such an examination as a reasonably careful skilled man would make. The defect must be latent at the inception of the policy. Latent defects are a form of inherent vice and are thus not covered under marine insurance policies, being excluded by Statute. Section 55(2)(c) of the Marine Insurance Act, which as you can see provides: "Unless the policy otherwise provides, the insurer is not liable for ordinary wear and tear inherent vice or nature of the subject-matter insured,...." .

Thus unless the policy otherwise provides an insurer cannot be held liable for the cost of rectifying the latent defect itself or any resultant damage. For decades hull insurers have been willing to cover damage caused by latent defect in a vessel's machinery or hull. Both the 1983 and the 1995 versions of the Institute Time Clauses have otherwise provided by specifically covering (under clause 6.2.2 in both instances): "... loss of or damage to the subject-matter insured caused by any latent defect in the machinery or hull".

In applying this provision the practice supported by the decision *Scindia Steamships -v- London Assurance* [1936] and others, was to accept claims in respect of the damages that resulted from, i.e. were caused by, the latent defect and to exclude the cost of repairing or replacing the latently defective part itself.

However, as mentioned by one of my colleagues, the comparatively recently decision in the *Nukila* supports the view that provided that the latent defect has caused damage to the subject matter insured during the currency of the policy, it may be difficult to resist claims for the cost of making good the damage, even if this includes the defective part itself.

As we all know, it is not the business of insurers to generally guarantee that the machinery and hull of a vessel are free from defects or to undertake to make good such defects where they are discovered during the period of the policy. However, insurers do continue to recognise that coverage in respect of damage caused by latent defects is the proper subject of insurance coverage.

In revising the hull clauses, the initial view was that the coverage provided should remain the same as that available under the previous clauses, as understood and accepted prior to the *Nukila* decision. In other words, excluding cost of repairing or replacing the defective part. However, it was felt that to have achieved this objective would have necessitated providing guidance as to what constitutes "a part".

In order to avoid disputes concerning the determination of what constitutes "a part", the new clauses provide coverage as in the previous versions for loss or damage caused by latent defects in the machinery or hull, but they have been amended to specifically make it clear that the cost of correcting the latent defect itself is, in effect, excluded. This approach preserves the principle that insurers should not be liable for the cost of correcting defects which existed, whether or not known to the assured prior to the inception of the policy.

The new clauses, and this is clause 2.2, reads:

"this insurance covers loss of or damage to the subject-matter insured caused by:
2.2.1
2.2.2, any latent defect in the machinery or hull, but only to the extent that the cost of repairing the loss or damage caused thereby exceeds the cost that would have been incurred to correct the latent defect".

Thus insurers will be liable for loss or damage caused by a latent defect in the machinery or hull, but only to the extent that the cost of repairs exceeds the cost that would have been incurred had the defect been discovered and corrected

at the inception of the policy.

A couple of hypothetical examples will serve to illustrate the effect of this clause. Let us assume that during a periodic inspection in dry-dock, a tail shaft is drawn and is found to be badly cracked and to require replacement. Upon close examination, the crack is established to have emanated from a small, and latent, casting defect. The technical evidence establishes that the cracking occurred during the course of the policy and that the casting defect could have been repaired by gouging and welding, had it been discovered before the crack had occurred. Therefore, the cost of replacing the tail shaft, less the cost that would have been incurred in gouging and welding the original defect will be recoverable. However, if the cost that would have been incurred in gouging and welding the original defect equals or exceeds the cost of replacing the tail shaft, no claim would arise. Of course, in either event, the cost of repairing any other damage resultant upon the defective condition of the tail shaft would be recoverable.

If we look at what the position would have been under the ITC in a pre-Nukila situation, the practice prior to the decision in Nukila would have been that there would have been no claim under the policy as the cover would only have responded for the cost of repairing or replacing damage caused by a latent defect. Thus on the authorities that I mentioned earlier, no cover was provided in respect of the cost of repairing or replacing the latently defective part itself. Post-Nukila, and remember The Nukila cast a different light on the interpretation of this clause and that with regard to latent defects it drew a clear distinction between instances where the condition of the vessel on account of the latent defect has not changed since the inception of the policy and those where damage is sustained which is incrementally greater than the pre-existing defect. In this particular example, it is arguable that the position under the new clauses is the same as that under the ITC post-Nukila.

The second example is where a vessel experiences a catastrophic main engine failure as a result of which she is towed to a repair yard where the engine is dismantled. It is established that the damage to the engine was caused by a failure of a crankshaft on account of a material defect which was latent and could not have been repaired even if it had been discovered prior to failure. The crankshaft, together with the other damaged parts are renewed and the engine is rebuilt.

Remember, the new clauses cover the cost of repairing the damage sustained by the main engine caused by the latent defect, but only to the extent that it exceeds the cost that would have been incurred to have corrected the latent defect. As the latently defective crankshaft could not have been repaired even had it been discovered to have been defective prior to failure, the cost of its replacement is clearly the cost of correcting the latent defect and is therefore not recoverable. However, there is a potential issue here and that is: to what extent, if at all, is the cost of the access work recoverable?

The fact that the crankshaft could not have been replaced without stripping down the engine, even if no other components had been damaged, would support the view that the full cost of stripping down and rebuilding represents part of the cost of correcting the latent defect. Of course, the same argument can be made in relation to almost any charges common to both damage and owners' repairs, such as dry-docking, tank cleaning, superintendence. However, the apportionment of these common costs is sanctioned by legal judgements from which has developed a long accepted practice of apportioning common charges.

Although the new clauses do not address the point exactly, I can see no good reason for deviating from this well settled and universally accepted practice. Therefore, in the circumstances of this example, the cost of the replacement crankshaft and half of the cost of stripping down and rebuilding the engine would be borne by the Owners.

The treatment of costs in this example would be the same as that under ITC, either post or pre-Nukila.

A second issue that I want to address is that concerning warranties and conditions precedent, and the practical impact that they can have on the adjustment of claims. The new clauses, as we have already heard, draw a distinction between warranties and conditions precedent. There are some conditions which are fundamental to coverage and still have the effect of a warranty. For example, in other words those which will entitle the underwriters to avoid the policy as from the date of any breach. There are other conditions which are suspensive. They have the effect of suspending the cover until any breach is remedied. For example, conditions relating to navigation and trading. Finally, there are those conditions which only have an impact if they are causative.

Again, an example may serve to explain how breaches may affect the adjustment of a loss:

Take a ferry, an old ferry. A fire occurs in its public spaces due to a carelessly discarded cigarette. The fire spreads and ultimately gains access to the engine room as the fire/watertight doors fail to close due to their being rusted in place. The damage sustained to the public spaces and to the engine room is repaired and a claim is presented.

In stating a claim under the policy, it is the duty of an adjuster to verify that the damage has been caused by a peril insured against, that the costs of repair are fair and reasonable and referable to the casualty and that any particular conditions of the policy have been complied with. In the latter respect, leaving aside navigational and trading conditions, the adjuster will have to consider clauses 13 and 14 of the new clauses.

Clause 13 relates to classification and ISM compliance. This is a fundamental condition which has the effect of a warranty if breached. This condition will be complied with if the assured can produce the following documentation: A certificate issued by the vessel's classification society confirming that the vessel was classed, maintained in class and that all requirements of class were complied with by the due date from the date of the inception of the policy until the date of the casualty; secondly, a valid document of compliance and; thirdly, a valid safety management certificate.

For the purposes of this example we will presume that the owner can produce this documentation but we will note that if the owner could not produce one or another document, the policy would have automatically terminated as at the time of the breach.

Clause 14 of the new clauses relates to the management of the vessel. Sub-clause 14.4 requires the assured owners and managers to comply with all statutory requirements of the vessel's flag state relating to the construction, adaption, condition, fitment, equipment operation and manning of the vessel. The fact that the fire/watertight doors could not be operated on account of corrosion is perhaps prima facie evidence of poor maintenance and non-compliance with the ISM requirements which are regulated by the vessel's flag state.

Since underwriters are not liable for any loss or damage caused by a breach of clause 14, if it transpires that the owners or managers were in breach of the requirements in relation to the maintenance of the doors, it would follow that underwriters would not be liable for any increase in the claim by reason of their failure. Thus, in our example, underwriters might not be liable for the cost of repairing the fire damage to the engine room, but would remain responsible for the fire damage sustained in the public spaces.

One can see from this example that there may be occasions when an adjuster being

charged with stating a claim under a policy will be required to carry out, or at least instigate, enquiries as to the statutory obligations of the owners or managers in order to establish whether or not they have been complied with.

This will not be necessary in all cases, only those where the adjuster is put on notice of a potential breach, say by comments in the logbooks, in the ship's officers' reports or in the survey reports. In cases where compliance is absent, additional enquiry will be necessary to determine the extent to which any loss has been increased by the breach of condition. That concludes my presentation. Thank you very much.

DISCUSSION

MR. TIM TAYLOR: Mike, thank you for that. I am sure we have had a lot of food for thought. There is a short period for questions, which expires in about two minutes, and I am conscious of the time and I do not want to alter the habit of a lifetime by delaying lunch.

However, I think there are a few topics which merit further discussion and possibly questions from the audience, but I would like to have a bit of audience participation first. I would like a straw poll. How many of you have actually looked at the new clauses? That is very good. My next question is: Is there a general feeling in the audience that they strike a fair balance between underwriters and owners, in other words, is there something in them for everyone? All in favour? All those against? Any do not know? That is very fair. I am not going to put those who were against them on the spot, unless they wish to be put on the spot. It is entirely voluntary. I would welcome thoughts from those who are against them, if they feel like making them. I know that Peter has a point that he wants to raise on Richard's presentation. Would you like to do that now?

MR. PETER McINTOSH: Yes, I have a small point to raise. We did talk about interest at length. It was very much felt that as interest is offered in other policies, it was something that we should debate. The conclusion was really that if something is very drawn out, for example, if we take an underwriter who has refused to pay a claim on a misguided decision and some months or years later they have decided that they were wrong and should have paid the claim, then do you pay it? From our legal advice, there is a pretty clear precedent in English law to suggest that in those circumstances underwriters pay interest. That would be meaningful. I think if we are 30 days or 45 days or a few days later than we should be in the payment of the claim, the amount of money involved in interest, in 99 cases out of 100, is likely to be so negligible that actually going through the process of collecting and paying it is going to be more costly than it would be worth. I think we did talk about it at length but on balance it was felt that if it is meaningful enough to be paid, it would be through the precedent and other than that it is not worthwhile, so why build it in. That was really to reiterate what Richard said.

MR. TIM TAYLOR: Peter, thank you for that. There are a couple of points on the legal side, I think Peter's analysis of English law on that is correct. I think it is important to recognise that these clauses in the preamble are subject to English law and practice. Those of you who may be tempted to use them and substitute English law and practice with some other system of law or jurisdiction will need to think very carefully about the consequences of doing that, with particular regard to things like interest and payment obligations and the like.

There are a couple of other loose ends that I would like to pick up. One is to satisfy Mr. Cornah's examination paper. I think his analysis of the law relating to cross claims in damages for failure to Sue and Labour is pretty accurate. There are also under the course of construction modified clauses in relation to Increased Value and a patch to deal with potential issues under the

Institute Mortgagee's Interest clauses. Those are current and those are going to be out fairly soon. I could go on dealing with a number of points, but are there any questions from the audience? Is there a microphone?

DR. SHEPPARD: I am Dr. Aleka Sheppard. We have in fact at the London Shipping Law Centre we have considered the following in discussions: Whether the Marine Insurance Act needs to be revised - the debate continues. We have already three sessions and the last session going to be on 29th January, which will be almost the same panel as this one, talking about the same issues. My worries, and this has struck me today from the discussion, are in three areas: First of all, I congratulate the team that they have produced a very comprehensive document, and they really are very brave to try to amend or reform the Marine Insurance Act in various parts. The three reforms that I noticed are in the crucial areas. The first is in the utmost good faith area and although it seems that the clause has tried to strike the balance, I am not quite clear whether any innocent non-disclosure will affect the assured or, if it is not included in the clauses, will the underwriters rely on the sections of the Marine Insurance Act, sections 18, etc.,. I am not clear whether you dealt with it, although I believe that it covers only reckless or intentional dishonesty.

The second point on utmost good faith is very brave reform by overruling the House of Lords in the *Star Sea*. The *Star Sea* provided a cut-off point that the dishonesty will (inaudible) the sections of the Marine Insurance Act if it occurs before litigation. After litigation commences then the court's procedures should apply. That is my comment on that.

Do I get a reply now, or shall I continue? I better continue. The next major area is the warranties. Of course the warranties have been dealt with quite well by clauses. They seem comprehensive but there are many loopholes there from first sight, I think. They need more study.

By clause 14, the management clause, which is very good, it seems that overrules section 39.5 -- really reforms section 39.5, both clauses really, 13 and 14.

The third point is the Sue and Labour. Under the statute, Sue and Labour is a defence for the underwriter, as I understand, so if there is a breach of the duty of the assured to exercise Sue and Labour then the underwriter, if he proves it, will have a defence. Now the underwriter has a counterclaim for damages, which is a big step, does it mean that the assured can recover his claim and then pay the underwriter whatever the counterclaim is? Thank you very much.

MR. TIM TAYLOR: I will try to take these very quickly. Unless these new clauses specifically alter an express provision in the Marine Insurance Act, then the Marine Insurance Act provisions remain fully in force and intact. Therefore, section 39(5), the unseaworthiness provision in time policies is still there. The question is right, that the provisions of clause 14 could apply in addition to section 39(5) in an appropriate case, and a breach of clause 14 or clause 13 for that matter would not depend upon privity of the owners.

So far as Sue and Labour is concerned, my understanding of the law (and I am happy to be corrected) is that where there is a breach, then the remedy has always been a cross claim in damages for the loss of the potential recovery. That would normally be set off against the claim.

So far as innocent non-disclosure is concerned, I do not think anything in these clauses alters the basic position. If we are looking at the duties of the assured in Part 3 under clause 48, and particularly clause 48.3 the operative words are, "knowingly or recklessly". I do not think that somebody who is doing something knowingly or recklessly could ever be regarded as being innocent. The *Star Sea* was a watershed case in a number of respects. I think it has always been clearly established that someone who is guilty of fraud should not have a recoverable claim. However, the difficulty has arisen where so-called fraudulent devices or misleading devices have been used in support of a claim. The consensus, and it was a consensus, was that in circumstances where an owner deliberately sets about to mislead his underwriter in the presentation of the claim, justice simply did not justify recovery being made.

I can perhaps give you an example. You have a machinery damage, a generator

failure, something of that sort and the underwriter or the adjuster asks for particulars of the maintenance record to satisfy himself as to the due diligence proviso; the owner knowingly produces false documents in relation to that. That may not be fraud in the widest Star Sea sense, but it is certainly discreditable conduct. I do not think, ignoring what the provisions of the law strictly may be, that justice would allow that claim to be recovered. That is what clause 48.3 is designed to address.

The other point I would make on this (and it has already been made by Peter McIntosh) is that these clauses are acknowledged as not being perfect. It has never been represented that they are perfect but they are going to be under review. If, in the light of experience injustices arise, then they can be looked at again and a mechanism exists for that.

MR. PETER McINTOSH: Can I just add as well, that the utmost good faith issue was discussed during the consultation period with the shipping associations. It was a point that they raised. At no stage -- and this is very much like all insuring conditions -- it is a two dimensional document, and Richard talked about the importance of relationship with the leader, which we have gone some way to formalising or spelling out within the clauses -- but the utmost good faith still does apply and the chairman of the joint hull -- and I did go to pains to stress this to the shipping associations. So I think what is reasonable and if you have a long relationship with a leading underwriter as a buyer of this insurance, reason will always be applied.

MR. PERRIN(?): My name is Maurice Perrin(?)(inaudible) I am an engineer. If I was to come back as a lead underwriter, taking the example of the ferry, I would be a particularly unhappy person. In drafting the clauses, are you still happy that the protection is there in terms of the classification now joined by ISM?

MR. TIM TAYLOR: I will attempt to answer that. The view is that if there is a failure by a ship owner to comply with a Flag State or SOLAS requirement and that causes the loss or increases a loss which has been caused by some other fortuity, then to the extent to which the owner is in breach the claim is not recoverable, so we are in a stronger position. I say we, underwriters are in a stronger position in those circumstances now under clause 14, than they would have been before.

MR. PETER McINTOSH: At the drafting stage we did look at some minor infringements of class rules. For example, we looked at a material breach of the policy, but it was felt that it was too broad a subject, so we have really stood behind if it is class, and there are current class certificates and there is an ISM, DOC and SMC, as Richard said, then the policy is intact. As Tim has just explained, if it is non-causative, so it is a peril insured under the policy, that through the doors being welded up or rusted up the initial peril insured was not covered as a result of those doors being rusted up, then we felt that it was only reasonable for us to continue to give that coverage while the class certs and the ISM certs are in place. Obviously, if class is not in place at the point of the casualty or the SMC or the DOC is not valid then the policy is -- there is no claim paid at all. I was not entirely clear on your question. Does that answer it?

MR. PERRIN: Thank you.

MR. AGGERSBURY: Good afternoon. My name is Robin Aggersbury from Mediterranean Average Adjusters, one of the few remaining independent average adjusters (laughter). There are some very good new generous conditions in the proposed policies, but one that really does worry me is the question of the latent defect. That is because I do not look on the interpretation of the clauses so generously as Mike does where he wants to split, or he suggests that the costs of opening up for access is divisible. Because these clauses are international, they are read by many claims adjusters from insurance companies outside the Joint Hull Committee and some of them, I think, when looking at this clause very restrictively -- and we get all sorts of interpretations by claims adjusters, it

is most peculiar that even after all these years they still come up with some reason for delaying a claim or creating a problem. This clause quite clearly says that it will only cover the costs in excess of correcting the latent defect. This is rather different from the clause in the American Hull Form which excludes the cost of replacing the defective part, which is slightly different from the Institute Time Clauses that we have had since 1983. They merely refer to the cover being, "for damage caused by", so the term "correcting" the latent defect will cover a multitude of sins. In a lot of cases there will be, in my view, a few claims people taking this clause literally. I do not think that the provision is there to allow the costs of splitting common costs, despite Mike's interpretation of it, I do not read it in the clause. I think this clause should be reviewed. In my opinion, there is a substantial restriction. I know Mike is going to reply, but surely it is underwriters who have put this clause in and should respond. Is that the way you would view it?

MR. TIM TAYLOR: I will respond after Mike has ---- .

MR. AGGERSBURY: Can I add another point on this subject. There is a considerable difference of practice between adjusters, be they members of the Association or non-members, as to how they treat the costs. In the past, in the early days, most adjusters would, according to tradition, split the costs of access, then others have interpreted it over the years of just excluding the costs of replacing the part itself, i.e., the actual cost of purchasing or manufacturing the part, so the access costs were not treated as common. That is another problem that really needs to be resolved. An acute minded owner could shop around to find the "right adjuster" to present his claim and it may not even be questioned by the market because they would not necessarily know that there is a difference in practice. This has been recognised by the Association since the 1960s. I have a paper here where there is a comment on the difference in practice. Thank you.

MR. MICHAEL HARVEY: I think we could probably talk for several hours on this topic. As I said at the beginning, it was a personal view and I think on the question of practice there are many adjusting practices which exist which are not dealt with in the clauses at all, and one has to say some that are probably wrong, for example the practice on which dry-dock dues are apportioned. In some cases they are almost certainly wrong, but nevertheless they exist and they have existed for many generations; they have been accepted by everyone. In the particular circumstances of dealing with the cost of replacing latently defective parts, it has always been my practice to apportion common costs, but bearing in mind of course that sometimes to actually replace the latently defective part may not actually require you to do the same amount of work that you are required to do to repair the damage. For example, if you have had a latently defective piston that has failed; to actually replace the piston might only require you to take the head off the engine and disconnect the piston and replace it, whereas the consequential damage which has been sustained might well require you to strip the engine down, totally. Therefore, you have to pay particular regard to the facts. I would certainly recognise that it is arguable on what is written in the clauses that underwriters could take a more harsh view and could say no, we are only paying for the cost of the resultant damaged parts. This may be one of the things which we as an association have to look at and maybe in the next review of the clauses this will be considered further

MR. PETER McINTOSH: I would like absolutely to support what Mike has just said. We could not legislate in here for every single circumstance. A lot of the dead ends that we reached -- and this was one of our biggest headaches, trying to put a set of words together and the lawyers, and I know Tim's team spent hours and hours trying to get something that was showing our intent, which is very fundamental, which is to return this policy without additional perils to pre-Nukila judgment. While the next year consultation period goes on, if we get some practical examples from an adjuster's point of view, as Mike said, that show that this clause is woefully inadequate, then we can try and look to do

something with it at the review in November. That is why all the input that we get from everyone here will be massively welcomed. I think that is it. Thank you.

THE CHAIRMAN: Thank you, Tim. Well, I must congratulate the speakers on covering an awful lot of ground in a fairly short space of time. It has been quite a race against time. First of all, I would like to thank Peter McIntosh for starting the race with a very good overview on the new clauses. In second place, I would like to thank Richard Cornah for starting us off at an excellent gallop and advising on the claims position. Thirdly, my thanks to Mike Harvey for making sure we get safely over the hedges, the fences. Finally and particularly I would like to thank Tim Taylor for acting as moderator for the seminar and making sure that the race was completed to the winning post safely without injury. Thank you very much, all of you.

I would also like to thank all of you for coming. I think it has been a very useful opportunity to discuss the new clauses. It is early days yet. I would hope that anyone who is not a subscriber yet will take advantage of the form that was on your seats to become a subscriber and better still, to encourage others to become subscribers to our Association so that you can get an early invitation to future seminars and other occasions, as well as our Association's AGM and the opportunity to attend the dinner at the Savoy on 8th May. Thank you very much for coming. Please stay if you can to join us in some refreshments. Thank you all.

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