Management

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International Trade Guides

Cargo Insurance

Cargo Insurance

This guide provides general information about cargo insurance and why you need it.

You should read it if you are involved in trading your goods worldwide. If you are an exporter you should pass this information onto your sales and marketing team and the department responsible for arranging the shipment of export consignments.

If you are an importer you should ensure your buying department as well as the team handling the supply and import process are aware of the information in this Briefing.

What is cargo insurance?

Cargo insurance (also called marine cargo insurance) covers physical damage to, or loss of your goods whilst in transit by land, sea and air and offers considerable opportunities and cost advantages if managed correctly.

Unfortunately, many UK traders do not want to become involved in arranging this type of insurance because they feel they do not have sufficient knowledge. They see it as an unnecessary expense involving extra administration, and make the mistake of allowing suppliers or customers to control this vital area of business. This loss of control not only increases the difficulties of implementing an effective trade risk management strategy, but can also have far reaching effects on profitability.

Fortunately, this attitude is changing, with more and more companies following the lead of many of the 'blue-chip' manufacturing and trading giants of the UK economy who tend to take full control of this type of insurance.

When you are looking at the types of cargo insurance available, you may come across the term General Average. This is one of the oldest principles of cargo insurance and relates only to ocean and sea voyages but is still relevant in today's trading environment. General Average covers the situation where damage or loss of certain goods occurs so that the remaining cargo and the means of transport are saved. For example goods may sustain water damage during fire fighting. In this situation, if General Average is declared, all the parties involved must contribute to covering the loss.

Cargo insurance is usually provided by the means of one of three Institute Cargo Clauses - A, B or C, plus War Clauses and Strikes Clauses. Simply put Cargo Clauses A provide the most cover with B and C giving less coverage which is reflected in reduced premiums for the lower cover (somewhat similar to car insurance cover with comprehensive, third party, fire and theft, and third party policies). Also there is an Institute Cargo Clauses (Air) for movement by air, which is equivalent to the A clauses. Your insurance company or broker will be able to give details of exactly what cover is given by each clause so you can choose the most appropriate for your business needs and trading patterns.

Why do traders need cargo insurance?

Exports

Many major UK exporters and trading companies sell on Cost Insurance and Freight (CIF) or similar terms, which allows them to arrange marine cargo insurance in the UK - usually on an 'open cover' basis. Because this insurance cost is legitimately passed on to the customer, who also gets the benefit of the insurance, this virtually amounts to free insurance which the exporter controls.

Many foreign buyers see this as essential service provided by the exporter, given that cargo insurance rates in UK are often cheaper than those available to the overseas customer in his local market. Indeed, exporters who do not provide a 'package' which includes insurance, can lose business to competitors who do.

The other side of the coin is where UK exporters allow their customers to arrange the insurance. This can range from selling on Ex Works terms to exporting on Free on Board (FOB) or Cost and Freight (CFR) terms. An Ex Works sale represents the minimum obligation for the seller, who has merely to make the goods available at his premises for collection by the buyer's designated carriers.

However, what tends to be overlooked is that the exporter is totally reliant on the buyer arranging adequate insurance on goods which have probably not been paid for. If the goods arrive damaged or if the buyer's insurance does not cover the loss, the exporter may not receive payment. Additionally if the goods or shipping documents are rejected on arrival at destination, the insurance risk can often revert to the exporter who may not have taken out any insurance.

Imports

Many importers assume that the suppliers are including the marine cargo insurance for free when, in fact, the cost is included in the purchase price. In addition, obtaining information from suppliers about these costs and whether they are being loaded can prove difficult.

Another important issue is the type of cover being provided - is it comprehensive 'all risks' or just 'total loss' only? Is it on a warehouse to warehouse basis or just warehouse to UK port? Without this information, importers may not realise they are paying too much for insurance which does not meet their needs, and may leave them with uninsured exposure.

A further issue is who is actually insuring the goods? The security of some overseas insurers may not compare favourably with the security of insurers in the highly regulated UK market. In the event of goods arriving damaged in the UK, the importer will probably deal with the UK agent of the overseas insurance company - an agent who will be working for the insurer, not the importer. This can lead to delays in processing and settling claims.

If the importer takes control of cargo insurance they can arrange the necessary cover in the UK market, which is often more comprehensive and price competitive than in overseas markets.

What types of cargo insurance are available?

Open Cover

This is the most usual type of cargo insurance, where a policy is drawn up to cover a number of consignments. The policy can be either for a specific value that requires renewal once the insured amount is exhausted or an permanently open policy that will be drawn up for an agreed period, allowing any number of shipments during this time.

Specific (Voyage) Policy

Although not the norm for cargo insurance, you may from time to time need to approach an insurance company (or broker, or other intermediary) to request an insurance policy for a particular consignment. This is usually referred to as Voyage Policy as the insurance covers only that specific shipment.

Contingency (seller's interest) insurance

As an exporter you may often sell goods on terms where your customer (as the importer) is responsible for insuring (or at least bearing the risk of damage of or loss to) the goods, for example under FOB and CFR Incoterms 2000. In these cases you are exposed to the risk of damage to the goods while in transit and your customer refusing to accept them. In the worse case your customer may not have insured the goods.

If this happens and your customer attempts to avoid liability, you could seek redress through the legal system. However, this can prove very expensive, and may often be pointless. Seller's interest insurance, usually for a small premium, will cover you for this contingency. For valid commercial reasons you may not wish your customer to know you have taken out such a policy.

Where can I get cargo insurance?

You can obtain cargo insurance direct from an insurance company, or some freight forwarders and other trade service intermediaries. Also you may find that your bank will offer cargo insurance as part of a trade finance package. However, best practice adopted by many companies has shown that using a specialist (marine) cargo insurance broker provides valueadded services when arranging cover and gives additional benefits when dealing with any claims and settlement procedures. The British Insurance Brokers' Association (BIBA) has a search tool to help you to identify insurance brokers at http://www.biba.org.uk/consumer/findbroker.asp. SITPRO does not sell cargo insurrance or recommend insurers.

What other options are open to me?

There are several other ways to approach the risk involved in the physical movement of the goods you trade across international borders:

- do nothing and carry the risk yourself. If an incident occurs resulting in damage or loss to the goods you could take action against the carrier. But you should remember that carrier liability is strictly limited by internationally agreed conventions. Also you will need the expertise and perseverance to sustain a successful claim. This could have an impact on your business;
- as an exporter you can let your customer insure the goods;
- as an importer you can let your supplier insure the goods.

The factors you must consider for either of the final two options have been described earlier in this Briefing;

How much will it cost me?

Like all insurance cover (premises, employer's liability, credit) you will have to pay for your cargo insurance services. Premium is usually calculated according to the value of the consignment (plus a percentage mark up for profit margin), the type of goods (danger or hazard) and other specific risks (mode of transport, route, destination, etc.) from the insurer's perspective. As with all insurance cover, you should spend time researching the market and getting quotes from a range of cargo insurance providers.

Conclusion

More and more companies recognise the long term advantage of buying cargo insurance in the UK and using the services of specialist cargo insurance brokers. If you are a small or medium sized trader you need to look more closely at this area of your international trading operations. You could reap benefits for your business through enhanced protection of your interests, improved international trade administration, better trading relationships and increased competitiveness, resulting in greater profitability.

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