

## **THE LOSS OF HIRE INSURANCE OF NORDIC MARINE INSURANCE PLAN – WHY IS IT USED IN MANY JURISDICTIONS AROUND THE GLOBE?**

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**Abstract** Marine insurance covers the loss or damage of ships, cargo, terminals, and any transport or cargo by which property is transferred, acquired, or held between the points of origin and final destination. Loss of hire insurance is a sub-branch of marine insurance that protects the ship owners in a situation when the ship for some reason described in this article is not able to make profit for its owners who still need to cover their expenses. The insurance clauses in different jurisdictions are very different but they are used internationally. The insurance market works globally and the insurance is product based on the insurance conditions and the pricing of the product. The Nordic marine insurance conditions are called The Nordic Marine Insurance Plan (NMIP). The Loss of hire insurance covers in this NMIP conditions covers loss due to the ship being wholly or partially deprived of income as a consequence of damage to the ship, which is recoverable under the conditions of the Plan. If the hull insurance has been effected on conditions other than those of the Plan, and these conditions have been accepted in writing by the insurer, the rules of the Plan shall be replaced by the corresponding conditions of the insurance concerned when assessing whether the damage is recoverable. Due to this fact, the master is often in a situation where his vessel is insured in several different jurisdictions with several different insurance conditions for different risks. The loss of hire insurance covers loss due to the ship being wholly or partially deprived of income: a. because it has stranded, b. because it is prevented by physical obstruction from leaving a port or a similar limited area, or c. as a consequence of measures taken to salvage or remove damaged cargo etc. This article explains the system of marine insurance conditions combining and risk management planning from the master's point of view. Master should be aware of the risk management structure of the vessel as it affects his actions. It also examines the reasons why the modern and valuable vessels are often insured by the Nordic plan.

**Keywords:** Maritime law, Marine insurance, Risk management, Maritime economics.

## **Introduction**

Loss of hire policies are frequently purchased in Europe and Scandinavia. Many traditional mortgagee banks require this insurance cover for the vessels they are financing. Loss of hire can be a huge risk for the owners and investors as vessels may be in off-hire without income for months or even years after a large casualty. This is the reason why Loss of hire insurance is often driven by banks and ship financing. The tradition of Loss of Hire cover for vessels has been developed in traditional shipping countries where the financial world has required this cover for the vessels as they require stable and predictable income. For example German KG financing markets customarily require Loss of hire insurance taken out by the owners they are financing.

The Loss of Hire insurance is fairly new mode of risk cover in relation to the hull and P&I cover as it appeared in the market only after the Second World War (Bull, 2017). As a rough estimation in 2017 of world fleet buy loss of hire insurance. For example, in Asian market, the Loss of hire cover is not as widely used and therefore the Loss of hire insurance market is not as well developed as in Europe and especially in northern Europe (Brooker, 2015). In this article, I will analyze the situation more closely in relation to the three insurance markets, Nordic, English and Asian market.

The insurance clauses in different jurisdictions are very different but they are used internationally. The insurance market works globally and the insurance is product based on the insurance conditions and the pricing of the product. The Nordic market has a considerable market share, which is much higher share than their share for example of the hull and machinery markets (Måkestad, Sveinung, 2014). This article explains the system of marine insurance conditions combining and risk management planning from the master's point of view. Master should be aware of the risk management structure of the vessel as it affects his actions. Previously the loss of hire insurance was only a cover for vessels in time charter. The insurance covered the situation when the vessel went into a state called "off-hire" and the vessel was deprived payment from the time charterer (Bull, 2017).

## **How does Loss of Hire insurance cover work?**

The Nordic conditions for loss of hire cover are popular in the markets. Therefore, it is used as an example envisaging how this insurance works in general. The Nordic cover is widely

used also outside Scandinavia. The Nordic Marine Insurance conditions are called The Nordic Marine Insurance Plan (later NMIP). The Loss of hire insurance covers in this NMIP conditions loss due to the ship being wholly or partially deprived of income as a consequence of damage to the ship, which is recoverable under the conditions of the Plan.

The standard loss of hire insurance cover covers loss due to ship being deprived of income as a consequence of damage to ship, which is recoverable under a H&M policy based on the Plan, but reference to the Plan (Chapter 10-12) can be replaced with provisions of the actual H&M policy (German, English, American etc.), if agreed in writing. If the hull insurance has been effected on conditions other than those of the Plan, and these conditions have been accepted in writing by the insurer, the rules in Chapters 10 – 12 (Hull insurance for total loss and damage) of the Plan shall be replaced by the corresponding conditions of the insurance concerned when assessing whether the damage is recoverable. (The Nordic Association of Marine Insurers (Cefor), 2016) This basic rule makes it possible to combine the different risk managing strategies based on different insurance covers to Nordic conditions of cover for loss of hire.

Due to this fact, the master is often in a situation where his vessel is insured according to two different jurisdictions with several different insurance conditions for different risks. The basic idea of the loss of hire insurance covers loss due to the ship being wholly or partially deprived of income because of a risk based on a hull policy, typically damage to the vessel, or some other risk specifically named in the cover. In NMIP these specific risks are mentioned as follows : a. because it has stranded, b. because it is prevented by physical obstruction from leaving a port or a similar limited area, or c. as a consequence of measures taken to salvage or remove damaged cargo etc. d. as a consequence of an event that is allowed in general average pursuant to the 1994 York-Antwerp Rules. (The Nordic Association of Marine Insurers (Cefor), 2016)

According to Main rule for calculating compensation in NMIP Clause 16-3, the compensation shall be determined on the basis of the time during which the ship has been deprived of income (loss of time) and the loss of income per day (the daily amount). Loss of time shall be stipulated in days, hours and minutes. According to NMIP Clause 16-4 a period of time during which the ship has only partially been deprived of income shall be converted into a corresponding period of total loss of income. According to NMIP Clause 16-5 The assured's loss of income per day (the daily amount) shall be fixed at the equivalent of the amount of freight per day under the current contract of affreightment less such expenses as the assured saves or ought to have saved due to the ship being out of regular employment. If the ship is

unchartered, the daily amount shall be calculated on the basis of average freight rates for ships of the type and size concerned during the period in which the ship is deprived of income.

In Nordic Marine Insurance plan it is also possible to fix the daily amount for insurance period: If it is stated in the insurance contract that loss of time shall be compensated for by a fixed amount per day, this amount shall be regarded as an agreed daily amount (NMIP Clause 16-6. Agreed daily amount). (The Nordic Association of Marine Insurers (Cefor), 2016)

Loss of hire insurance gives a quite independent cover that in today's market is offered also to other vessels than just those on time charter for which it was originally intended. Today it can be used by vessels under voyage charter as well of vessels under other types of contracts of affreightment like charters for consecutive voyages. Even cruise vessels and liner vessels without any such contract form can be covered by loss of hire insurance (Bull, 2017). Generally, however loss of hire is considered as quite expensive form of risk management strategy. Therefore, as we explain above, it more or less uncommon in Asian markets where some other solutions have been developed as an alternative risk management strategy.

### **When will the owner be protected and for which risks?**

The ship owner and the financing institutions are well covered in a situation when the vessel ceases to earn its income when protected by loss of hire insurance cover. When acquiring the cover the ship owner must however familiarize with the cover carefully. Even though the Nordic plan has a large market share, the other covers in the market are products on their own terms and they need to be carefully evaluated. The most common alternatives for Nordic conditions are American Loss of Charter Hire Form, SP-40B (Aug 1961) ("Lazard Form") and the English ABS 1/10/83 wording, including or excluding the War risk (Måkestad, Sveinung, 2014). For the Master it is essential to know which cover and what kind or combination his vessel has when the insurance risk is attached to the vessel as not all risks are covered by all policies.

To obtain cover for the vessel from loss of hire insurance under Nordic Plan, there must in general be damage to the vessel that has caused the loss of income to the vessel. Unless otherwise agreed, an insurance covers only marine perils and war risks are excluded. In practice sometimes a loss of policy is extended to include war perils in addition to marine perils as both hull & machinery as well as war risks can be covered by NMIP under separate insurances under the NMIP condition (Måkestad, Sveinung, 2014). Against piracy loss of hire

under NMIP has hardly any protection of practical value under standard conditions but adequate cover is however available in the market (Måkestad, Sveinung, 2014).

Risk cover for loss of hire revenue is based on named risks in the policy. It is irrelevant if the assured has actually effected for example hull insurance and not all casualties covered by the hull policy can be covered as loss of hire. For example if the vessel is a total loss there will not be normally cover in loss of hire insurance when there is a total loss according to NMIP. According the rules there must be damage covered by the hull clauses. Situations which are not covered by the hull clauses are not covered either as loss of hire like delay by strike, ice or similar situations. The other side of the coin is however that the cover according to the NMIP is extended to include hire lost due to; Grounding without damage to the vessel, blocking and trapping in port, Salvage or removal of damaged cargo, a General Average event. All these extensions make the conditions quite fair and lucrative. For example, the owner does not need to prove that there was damage to the ship when grounding or he doesn't have to prove the severity of damages. This is supported by the rule 16-1 first sentence, as the owner doesn't have to prove that the damage would be recoverable under the hull insurance. It is also irrelevant if the owners has even effected the hull insurance (Bull, 2017). It is only relevant that the loss can be traced back to marine peril (The Nordic Association of Marine Insurers (Cefor), 2016). No standard deductible

Nordic conditions are based on the idea that there is a deductible period of time in loss of hire insurance. Minimum agreed deductible period would generally be 14 days. Alternatively, 21 or 30 days are quite frequently stipulated in the contract (Måkestad, Sveinung, 2014). Each casualty shall be subject to a deductible period, which shall run from the commencement of the loss of time and last until the loss of time, calculated in accordance with the rule in Cl. 16-4, sub-clause 1, second sentence, is equivalent to the deductible period stated in the insurance contract. Loss of time in the deductible period is not recoverable (The Nordic Association of Marine Insurers (Cefor), 2016). Damage caused by heavy weather or navigating in ice which has occurred during the period between departure from one port and arrival at the next one shall be regarded as one casualty. a separate deductible period for damage to machinery has been agreed on in the insurance contract according to the NMIP (The Nordic Association of Marine Insurers (Cefor), 2016).

A separate deductible period is applied for each casualty; this is in accordance with the other deductible provisions in the Plan, cf. Cl. 12-18 and Cl. 13-4. However, if one and the same casualty leads to a number of separate delays, e.g. delay at the place where the casualty occurred, delay in connection with temporary repairs and delay during permanent repairs,

then only one deductible period shall be applied for the aggregate of all the delays. (The Nordic Association of Marine Insurers (Cefor), 2016). The provisions regulate the right of the assured to choose a repair yard and the consequences his choice of yard has for the extent of the loss-of-hire insurer's liability (The Nordic Association of Marine Insurers (Cefor), 2016). This is a specific issue that needs to be addressed by the Master and the owner when choosing the repair yard after the incident.

### **Basic differences in marine insurance/loss of hire covers for vessels**

There is more similarities in the basic marine insurance cover in the world market than differences as the systems need to be able to cope with each other also because of the reinsurance market. The language of the insurance markets is English and therefore the relevant marine insurance conditions are all translated into English language.

The differences in insurance conditions are also meaningful and they give competitive advantages for both insurers as well as the owners using them. Insurance conditions vary also because of the basic legislation they are based at. Even though the English legal system is dominating the market as backroad law for majority of marine insurance, there are competitors, which are strong in relative fields of these markets. Loss of hire insurance is a typical example of these fields in the markets. The Nordic conditions are strong in the market. As mention above, they have a relevant market share. We have examined the cover and found out that many situations causing the loss of income cannot be found in general hull policies. This does not however explain entirely their strong position in the market. There is also basic differences in the insurance law and insurance cover systems which needs to be examined in order envisage the lucrativeness of another set of cover in relation to others.

The English law of marine insurance is based on warranties, which needs to be obeyed by the assured as a part of the contract. Warranty of seaworthiness is specifically important (Soyer, 2017). Nordic Marine insurance plan had a similar clause on seaworthiness until 2007 but it was abolished from these conditions, which were known at the time as Norwegian Marine Insurance Plan. Nordic Marine Insurance Plan has a different approach in the duties of the assured. They are based on the idea that the person effecting the insurance needs to follow the safety regulations determined in the insurance contract in order to keep the cover in force and get his compensation.

The approach also to the duty of disclosure before entering the insurance contract is also more beneficial for the owners than the equivalent approach in the English law. Prudent owners are well protected under the Plan provisions and defending their cover against the insurer's

accusation for breach is easier if they have followed the relevant provisions in the Plan and the contract. This effects especially those owners whose have taken the loss of hire cover with Nordic conditions as in principle it is irrelevant for the loss of hire cover whether the assured has lost his cover in relation to the hull insurer for example due to duty of disclosure (Bull, 2017). The issues considered under the chapter 3 of the plan (duties of the person effecting the insurance and the assured) are evaluated independently in relation to the loss of hire insurer (Bull, 2017). This is a relevant advantage for the prudent owners who run well their tonnage and follow the safety regulations and keep their insurers well informed.

### **Alternatives to Loss of hire insurances**

The freight insurances in general cannot replace the cover loss of hire insurance gives for the owners against loss of revenue (Bull, 2017). There are however, insurances on the market which are used by some ship owner's which find the loss of hire unnecessary expense considering their risk management strategy (Brooker, 2015). Trade Disruption Insurance and Strike & Delay Insurance are two of the most common alternatives. Trade Disruption Insurance (later TDI) gives also cover against losses like fire or explosion on land affecting loading and discharging facilities, port closure, Stowaways, obstruction of a berth or port blockade, delays resulting of refugee rescue, infected deceases etc. This cover varies more depending on which company provides it. Some companies describe their TDI as a product which is a form of Loss of Hire that excludes machinery damage and responds in three specific ways: 1) Loss of Earnings 2) Additional Cost and Expenses 3) Contractual Penalties. Strike & Delay insurances in general are even more focused on the risks that are third party risks away from the vessel (Brooker, 2015). However, Strike and Delay insurances seem to differ quite substantially from provider to provider. They are often advertised to cover many similar risk as the loss of hire insurances: Strike & Delay Cover Insurance and other "onshore" incidents is an additional cover under Hull & Machinery Policy and very similar to Loss of Hire Insurance. This cover allows Shipowner or Charterer to minimize their expenses when delay of the vessel is caused by unforeseen "onshore" circumstances, which are beyond client's control. These are enumerated in the policy and usually insured events are fire, explosion, port/waterway closure, bad weather conditions, boycotts, strikes of stevedores and other port services etc. Some companies offer under certain conditions that it is also possible to include coverage for unexpected events onboard: strike of the crew, machinery breakdown, deviation due to illness of the crew members, quarantine etc.



The risk evaluation between these options above and “traditional” loss of hire insurance depends highly on several determinants in risk management and their evaluation. For example the trading area. If we consider the TDI cover described above, it is clear that not all parts of the cover are needed in all trading areas. On the other hand the loss of hire risk in places where accessibility to repair yard is good, the minimum deductible for loss of hire might be too long for the owner to get full advantage of the cover when vessel can be repaired quickly and can be back in business after relatively short period at the repair yard.

## **Conclusions**

Loss of hire insurance is an important cover especially when connected to shipping finance. When shipping has been in crisis since the earning dropped heavily after 2008 it has been a valuable cover for many even though it is also considered costly insurance when freight rates are low and earnings have been in decline. Having been part of the shipping finance scheme for the last 30-40 years it is well established.

Nordic plan has become more and more popular as a basis for cover since the conditions of cover are pretty straightforward and fair for the owners who play fair and maintain their vessels well. It has several benefits and competitive advantages. It is stable when it has been formed on the basis of Nordic plan, which has a legislative history that goes back more than 100 years (until 2013 with a name Norwegian Marine insurance Plan) and case law collected in one single collection from Scandinavian Maritime courts and Arbitration Tribunals. Effective, highly skilled and especially cost effective arbitration in Norway is also one of its benefits. As a tool with updated Commentary, it is also possible for foreign arbitrators to understand it. Mainly arbitrated in Norway it offers cost effective and smooth arbitration near the main financial markets, which use it as a standard.

Importance of good management together with Master and crew maintaining the vessel is the basis of the risk management under the Nordic Marine insurance plan. Together they guarantee that the vessel as a source of revenue is protected. When vessel can be repaired quickly, loss of revenue is also protected it can be back in business after relatively short period at the repair yard without any severe disturbances for business.



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