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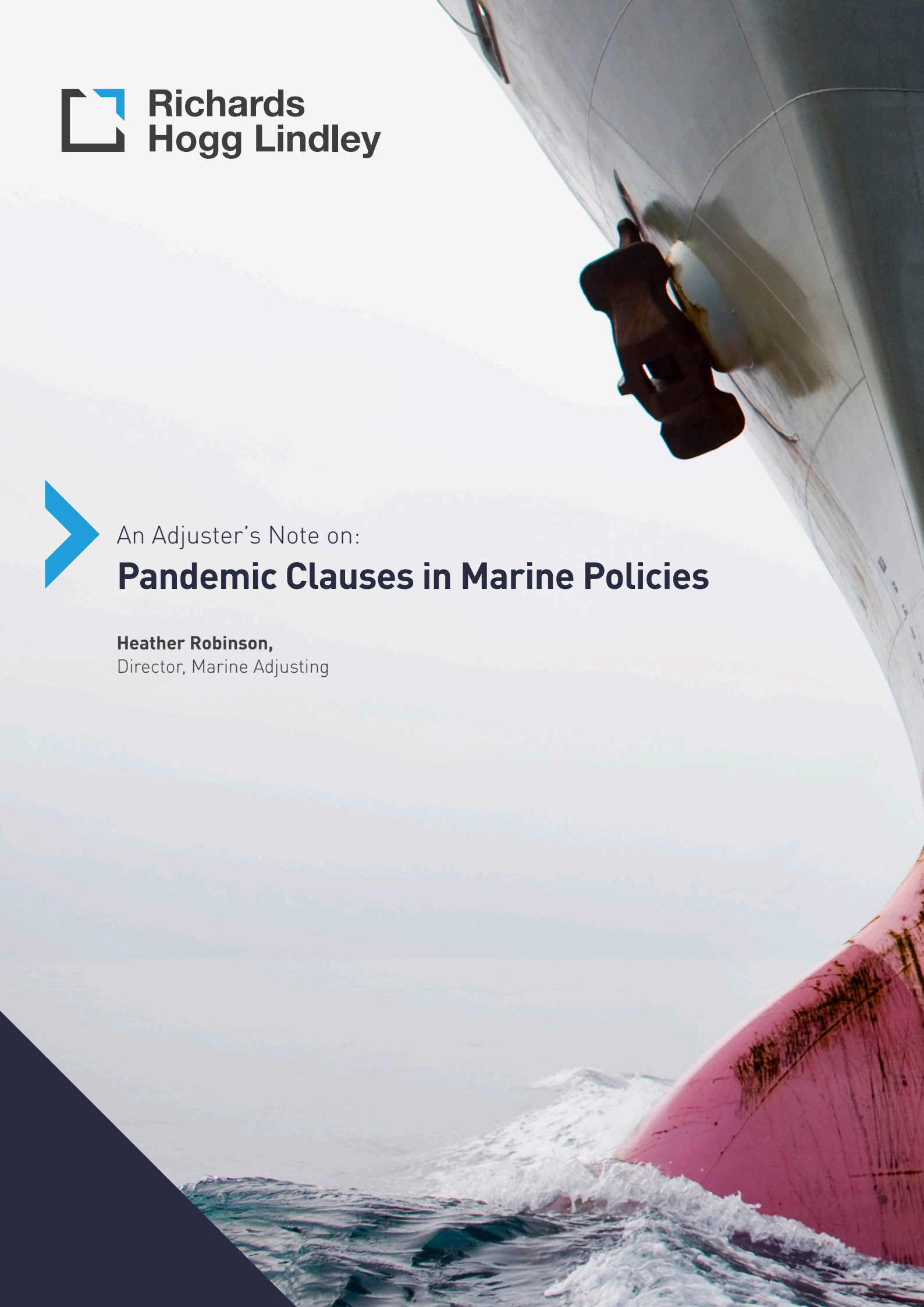

An Adjuster's Note on:

Pandemic Clauses in Marine Policies

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Introduction

The Covid-19 pandemic has introduced a number of additional, unanticipated issues which may affect the cost of claims arising on marine insurers, as a result of:-

- non availability of spare parts due to temporary closure of manufacturers or suppliers, or availability at increased cost from another supplier or geographical location.
- delays in the attendance by salvors, service engineers (from overseas), pilots, harbour authority personnel, tug crews etc owing to quarantine / lockdown etc.
- extended detention for an unexpected lockdown or temporary closure of the repair yard or port.
- additional costs of steaming to the next nearest reasonable alternative port in circumstances where the closest port is locked down
- Covid outbreak amongst the vessel's crew or at the repair yard causing a delay to repairs.

Both parties to a marine insurance contract require certainty, as far as possible, of the extent to which such additional expenses are recoverable from insurers. In the rapidly evolving circumstances of the pandemic, insurers may seek to introduce new contractual terms to limit cover for those additional 'pandemic delay' related expenses or even exclude them altogether. A number of suggested wordings have entered circulation, which merit further analysis and consideration. We will review:-

- LMA Communicable Disease Exclusion, drafted by the Joint Excess Loss Committee (the Lloyds Market Association and the International Underwriting Association)
- CEFOR's communicable disease exclusion and pandemic delay clause

This analysis considers only the possible application of these wordings in practice, to the situation where a vessel is undergoing damage repairs which are exacerbated in cost and time required as a result of the pandemic, in which case an apportionment of time or expenses is required in order to establish the claim on insurers.

Before we turn to the new clauses, it is worth briefly summarising the extent to which the above additional pandemic delay related losses may otherwise be recoverable from insurers, where there are no specific limitation or exclusion clauses (either for policies written in the pre-COVID period or those which do not contain any specific provisions regarding the pandemic).

Reference is made to Richard Cornah's 2020 address "Reflections on Covid-19 and the impact on Hull claims" in his capacity as Chairman of the Association of Average Adjusters for useful detailed guidance on whether such expenses are recoverable on a hull policy which is subject to the Institute Time Clauses – Hulls 1.10.83, with no specific pandemic exclusions or limits.

Marine policies, subject to any express provision otherwise, generally provide an indemnity for:-

- the reasonable cost of damage repairs (s.69 Marine Insurance Act 1906).
- Ship's proportion of the claim for general average.
- Loss of hire which is attributable to an event which is covered under the hull policy

In determining what constitutes the reasonable cost of repairs, a claims practitioner will likely give consideration to whether the cost or time was reasonably foreseeable or unavoidable and whether the assured has acted reasonably in the circumstances to minimise such extra expenses, wherever possible. It may be accepted that reasonable waiting times during a pandemic are longer than usual. Arguably, the claim practitioner, accustomed to applying their knowledge of the law and practice is well placed to determine the reasonable cost of repairs and there is flexibility for them to do so, on an individual case basis.

LMA communicable disease exclusion

It is noted that in their accompanying covering note, the JELC concede that the effect of the exclusion clause should be studied and they suggest that these wordings merely reflect two possible responses to the new and evolving pandemic situation. They add further that these do not constitute recommendations and acknowledge that the approach taken by individual underwriters will vary dependent on their own risk management.

By way of context, it is useful as part of this analysis, to reflect on the London marine insurance market's past responses in the development of new contract terms, to 'new' emerging risks. In particular, it appears that the same difficulties which arise in the practical application of the LMA 'Communicable Disease exclusion' have been encountered previously, namely with the Institute Cyber Attack clause cl.380, drafted in 2003.

The cyber attack clause applied a far reaching exclusion with the result that the policy cover was not suitable for practical use in a context where assured's often rely, to a large extent, on information and communications technology, for commercial purposes. A market review of the cyber attack clause with the aim to produce an improved, workable, commercially sensible wording which could be agreed by insurers and assureds was undertaken.

The communicable disease exclusion has a similarly far reaching application to absolutely all losses, damages, liabilities or expense of any nature "proximately caused by or significantly caused by or contributed to by or resulting from or arising out of or in connection with" a communicable disease, threat (perceived or actual) or any recommendation, decision or measure taken to restrict the spread of the communicable disease.

The clause begins by introducing the proximate cause test applied under the Marine Insurance Act 1906 s.55(2)(b). The difficulty with this approach in this context is that under English law, where a loss is attributable to a combination of proximate causes which are equally efficient, one being a peril insured against insured and one being expressly excluded, then the loss is excluded from policy cover. The exclusion could therefore have the effect of removing from cover, reasonable repair expenses which have been increased by the pandemic and which might otherwise be recoverable.

Although not quite on point, the topic of causation in the context of the pandemic has been considered by the High Court in recent test case, Financial Conduct Authority v Arch [2020]. The Court concluded that the proximate cause of the loss was the national outbreak of covid-19 which constituted a single effective cause indivisible from the resulting local government and public responses/lockdowns. The decision in favour of the FCA was appealed in January 2021. On a strict application of the 'but for' test (for establishing a causal connection between an insured peril and a loss experienced) in circumstances where each incident of covid-19 constituted a separate "occurrence", the effect would be that there was no insurance cover. The Supreme Court recognised that this was not the original intention of either party in forming the contract of business interruption insurance, and again found in favour of the FCA, representing assureds.

It is submitted therefore that the proximate cause of the loss is not the appropriate basis for establishing whether an expense or loss is recoverable from insurers or not, in the circumstances of the practical scenarios envisaged above, where casualty related repairs are exacerbated in cost or time, owing to the pandemic. In such cases, the basis for establishing whether the expenses are recoverable is often more appropriately a question of the reasonable cost of repairs.

The position is further complicated by the provisions in cl. 2.2. The explanatory covering note provided by the JELC provides "In recognition of the current need for vessels and other interests to be taken temporarily out of service, the Committee considers that particular effect of the pandemic should not constitute an Excluded Circumstance and the clause makes that clear." It appears that the intention of cl.2.2 is to remove from the blanket exclusion, those vessels which are taken temporarily out of service owing to current need, in their current location. This appears to be a concession to reintroduce to coverage, certain costs which are attributable to pandemic delays where a vessel is currently laid-up pending resumption of operation, trading etc.

However, the circumstances envisaged by cl.2.2 and the extent to which those additional communicable disease expenses are reintroduced to cover thereunder is unclear. For example, it is not clear how this clause would apply to a loss of hire claim for a vessel laid up for damage repairs, during which a lockdown is imposed which increases the overall time off hire for repairs; or how it might affect the increased expenses and time of additional steaming / towage to the next closest port which is not in lockdown, in order to effect damage repairs. It is considered that the effect of cl. 2.2 is therefore to remove from the blanket exclusion, for example, circumstances where a vessel is damaged by an insured peril (grounding or collision etc) whilst laid up at anchorage owing to the reasons outlined in 2)c) of the exclusion clause (e.g. where vessel is laid up because of lockdown measures by ports etc).

The JH2020–007 clause was originally published in August 2020 and this was revised in November 2020. The covering circular explains that two new clauses were drafted in specific response to direct enquiries as to the extent of application of the exclusion. The revisions include the addition of cl 2.3 and 2.4, which further limit the application of the exclusion clause and reintroduce cover in certain scenarios.

cl.2.3 provides that if a vessel sustains damage owing to a marine peril during a deviation to another port, which is itself is in consequence of an excluded circumstances or measures taken to restrict the spread of infection of a Communicable Disease e.g. a local lockdown, then that marine loss or damage is not excluded from cover.

Cl.2.4 further provides that where loss or damage caused by a marine peril is exacerbated or increased by, for example, delays at a repair yard or during a salvage operation, owing to an outbreak of a Communicable Disease or other lockdown measures etc, then these increased costs shall not be excluded. Whilst it is therefore clear that increased damage repair costs owing to a pandemic are not expressly excluded, it does not offer any assistance in establishing the extent to which such losses may be recoverable from insurers.

The exclusion clause also applies broadly, to any communicable disease or threats thereof. Notably it is not limited only to exceptional and operating pandemic situations.

Finally, cl. 4.1 provides that where a casualty has been caused by or contributed to by an infected individual, this will not prevent a claim from insurers for a loss which would otherwise be recoverable. It recognises the requirement that such damages fall within the cover provided by standard terms and conditions and submits that the additional risk presented by infected individuals during a pandemic situation, can be adequately addressed by premiums etc rather than excluded altogether.

CEFOR

The Cefor clauses intended to apply to Nordic Plan marine insurance policies, are as follows:-

- Communicable Disease Exclusion (hull)

- Pandemic delay clause (loss of hire)

Both clauses apply the 'dominant cause' doctrine i.e. if the proximate cause of the loss is communicable disease or pandemic delay then the claim on insurers is excluded or limited respectively. The commentary to the Nordic Plan, cl. 2-13 provides a scale for establishing the weight of a particular peril in situations where there are concurrent causes.

Communicable Disease Exclusion (Hull)

The application of the exclusion is similar to the LMA wording and shares the exception where a casualty has been dominantly caused by or contributed to by an infected individual i.e. this situation is not caught by the exclusion.

The clause provides further that where damage repair costs arising from an insured peril (in the Plan context, that the cause is not specifically excluded) are increased by a communicable disease, then the provisions in the Plan are to apply. No limitation is therefore applied to those exacerbated repair costs.

Pandemic Delay Clause (Loss Of Hire)

This pandemic delay clause is supplemented by a commentary which provides useful practical examples of how the clause applies. It explains that this clause was drafted specifically with scenarios where damage repairs are delayed owing to the pandemic, in mind. The intention is to limit insurers' exposure for such losses, not to exclude them altogether.

The wording of the pandemic delay clause is specific to Covid-19 and other WHO recognised pandemic diseases. It does not apply more widely to any other communicable diseases.

Both Cefor clauses have the effect of an apportionment of common expenses or time between insurers and assureds in circumstances where casualty related damage repairs are exacerbated, as a result of a pandemic delays. The insurer is only liable for that part of the loss which is attributable to the peril(s) covered by the insurance. The burden of proof is on insurers to demonstrate that loss has been caused solely by pandemic delays if they wish to limit or exclude the claim accordingly. The limit applies to the allowances for pandemic related delays only after the additional time has been apportioned for other reasons e.g. damage repairs.

In practice, where the cost / time required for a vessel undergoing damage repairs is exacerbated by the pandemic, it may be difficult to make an apportionment of the time or expenses on the basis of the dominant cause doctrine. It is a question of the reasonable cost of repairs. It will depend in part on foreseeability. For example, if the shipowners already knew there would be delays in entering the yard owing to the pandemic, then the extent to which the additional costs are recoverable or subject to the limitation under the pandemic clause will depend on the shipowners demonstrating that they have done all that could reasonably be expected of them to avoid such a delay, if the additional time is to form part of the overall reasonable time required for damage repairs.

Alternatively, where there is a delay in obtaining spare parts from manufacturers, as part of a reasonable repair process, this is foreseeable and certainly something a shipowner might expect to encounter at any point during repairs. In this case the dominant cause of the additional time /expense is the original peril which led to the damage repairs and therefore the additional expenses may be recoverable from insurers.

Where a lockdown has been imposed by the local authorities which causes a delay to service technicians attending to effect damage repairs, it is probable that this would constitute a new and intervening act, sufficient to break the chain of causation and therefore the consequential costs arising therefrom would be attributable to the pandemic delay and the clause limit would likely apply to the additional time.

The commentary to the pandemic delay clause also provides a specific example that in the event the pandemic is over, and yet there is a delay in delivery of parts (which are normally in stock) of several months thereafter, then this loss of time will not be subject to the limitation as it is considered to be too remote from the pandemic.

The limit for the number of days which are covered by insurers for pandemic delays under this clause is generally set at 30 days. The basis for the limit of 30 days and whether this is an equitable apportionment between insurers and owners of the additional exposure to risks, as a result of a pandemic, is not entirely clear. The increase in repair costs or times etc attributable to the pandemic could vary significantly on a case by case basis, depending on the particular authorities involved, geographical location of the vessel, repairers or salvors etc. Owners may wish to consider whether 30 days is sufficient for their needs, balanced against the increased costs which insurers may require in order to cover an extended period. 30 days may be a practicable compromise in circumstances where the delays and additional costs can vary extensively globally.

SUMMARY

The extent to which the LMA wording offers any contract certainty regarding policy cover for damage repair costs / times which are exacerbated by the pandemic, is questionable. The structure of the clause as a blanket exclusion, with exclusions from the exclusion (cl.2.2-2.4) is confusing. The wording is difficult to interpret and claims practitioners may struggle to apply it in practice, particularly in the context of recent decisions by the English courts, which significantly broaden the traditional meaning of consequential losses within contractual exclusion clauses. Whilst the pandemic situation has increased insurers' exposure for losses and must be addressed as a 'new normal', a blanket exclusion, with certain caveats, the extent of this is not entirely clear in the scenario where damage repair costs or expenses which are otherwise recoverable from a marine insurer have simply been exacerbated by the pandemic. It must be accepted that if a ship is now damaged, the average overall cost of repairs is likely to be higher. We do not think the intention for this clause to have a very wide reaching application, to prevent costs which might otherwise be recoverable from insurers as part of the reasonable cost of repairs. Whilst the structure of the clause is less convoluted than the LMA wording, we think the same issues in application may apply under the Cefor communicable disease exclusion.

However the Cefor pandemic delay limit wording is clear, concise and appears to provide sufficient contractual certainty, whilst retaining flexibility for claims practitioners to determine the appropriate apportionment of additional time or costs according to the weight of the perils in operation. Notwithstanding, we consider that in practice it is often more likely to be a question of the reasonable cost of repairs, rather than a question of the dominant cause, where repair times / costs are exacerbated by a pandemic delay.

Ideally the contract terms intended to address additional pandemic expenses or delays would offer, as far as possible:-

- Appropriate limits to insurers' exposure for exacerbated pandemic delay expenses
- Contractual certainty to shipowners (in circumstances where delays and additional expenses can vary significantly globally).
- An equitable division of the risk where repair costs or times are exacerbated by a pandemic.

One possible solution could be to limit allowances for exacerbated expenses to say 1.5 x the ordinary, reasonable repair time or cost, subject to an overall higher policy limit.

Whilst it is accepted that reaching an equitable solution is not straightforward, as claims practitioners are well aware, the desire and intention for contract certainty does not always result in clearly constructed wordings which can be easily understood and applied in a commercial context.

We consider that bespoke wordings based on careful and considered drafting and which are the result of negotiations between owners and their insurers at the contract formation stage, to determine an equitable apportionment of risk, are preferable to address the practical scenarios where there are exacerbated damage repairs costs / time owing to the pandemic. We also consider that in many cases, claims practitioners are well placed to determine a suitable apportionment of time or expenses in the context of the reasonable cost of repairs.

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