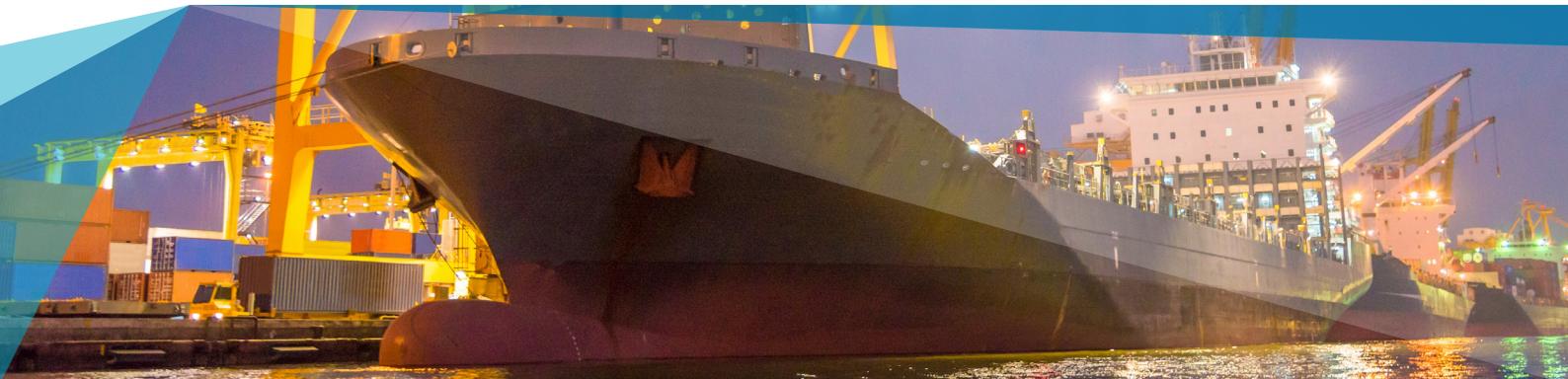


DISTRESSED PORT RISKS INSURANCE



A mortgage bank's port risks insurance typically provides specialist protection for the financing bank during a foreclosure/arrest process, primarily during the time the vessel is in port or at anchorage.

- The policy will cover loss of, or damage to, the collateral asset and related third party liabilities.
- Coverage is subject to the London Institute Port Risks Clauses, a policy wording designed specifically for vessels not operating.
- Coverage includes third party liability protection, including four fourths collision and pollution (thereby negating, in some instances, the need to maintain the owner's protection and indemnity entry).
- Coverage includes loss or damage caused by war or warlike acts, sabotage, malicious damage, vandalism, and damage caused during strike action (thereby potentially negating the need to maintain the owner's war risks policy).
- Shifts to a lay-up location, chosen by the bank, are covered as are shifts within the vicinity of the lay-up location.
- Trial trips are covered, as are demonstration trips for prospective purchasers.
- Coverage typically permits maintenance and repair work, with hot work insurable subject to prior notification.

WHAT IS NOT TYPICALLY COVERED UNDER A DISTRESSED PORT RISKS POLICY?

Coverage provided by the Institute Port Risks clauses does not insure liabilities incurred by the assured in respect to any existing cargo on board or to crew or any employee of the assured working in, on, around and in connection with the vessel. (Separate coverage for these liabilities can be provided as a supplementary coverage). Great care must be taken if a financier wishes to foreclose on a vessel with cargo on board and a financier should make every effort to ascertain the precise status of the cargo to avoid disputes in the event the cargo has sustained damage.

WHY NOT RELY ON THE EXISTING OWNER'S INSURANCES?

At the time of a foreclosure, the bank is confronted with many unknown issues, not least of which is uncertainty regarding the status of the owner's insurances protecting the collateral asset. For example:

- Owner's cover may have lapsed.
- Policy conditions may not have been met.
- Substantial premium amounts may be outstanding.
- Classification may be in doubt.

All of these concerns raise doubt over the validity of any existing insurances.

WHAT SUM INSURED SHOULD A BANK REQUIRE?

Some banks choose to cover loss of, or damage to, the vessel for their financial interest in the collateral asset only, being the outstanding mortgage amount plus say 20% uplift (to cover costs in the same way as on a mortgagees interest insurance). However, it would be prudent to consider insuring at least the estimated market value of the vessel if this is more than the outstanding loan amount. This way, the bank can be certain underwriters can not attempt to apply the law of average in the event of a claim (i.e. reduce the value of any claim by saying the bank has chosen to self-insure part of the exposure) as well as avoiding any allegations by the owner and his lawyers that the bank have not acted properly to fully protect the asset they have taken control of.

Collision liabilities and third party liabilities are automatically covered separately to the same monetary limit as is covered against physical loss or damage. This limit of liability can be increased as necessary to provide the bank with any additional limits they consider prudent, or as may be required by a port authority.

DO THESE POLICIES ADDRESS THE UNUSUAL CIRCUMSTANCES OFTEN EXPERIENCED BY DISTRESSED VESSELS?

Yes. The panel of insurers who underwriter these risks can provide coverage:

- For short term periods.
- At short notice.
- Without initially requiring full details of lay-up arrangements/location.

- Whilst vessels are not in class.
- Without lay-up/location survey, security/firefighting survey etc.
- For damaged vessels (provided they are still seaworthy).
- During repair work and maintenance.
- Whilst skeleton/no crew on board.
- Without full understanding of the status of the owner's insurance (the bank's insurers taking subrogation rights against any other insurers should a claim be paid).

WILL PORT RISKS INSURANCE NEGATE THE NEED FOR THE MORTGAGEES INTEREST INSURANCE (MII) POLICY TO BE MAINTAINED?

This depends on the operational involvement of the bank during the lay-up period. If the bank passes responsibilities to a manager/agent and has little or no involvement in the day-to-day running of the vessel then a MII policy could still be beneficial as a mistake or oversight by the appointed managers of the vessel can negate payment of an otherwise valid claim. The critical question is whether a MII underwriter could dispute a claim stating that the bank caused (or were aware of the circumstances) that allowed the port risks insurers to dispute the claim.

For further information on this matter, please email Marsh Maritime Advisory on: MMA@Marsh.com

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