ROANOKE TRADE

General Average–An Ancient Concept Taking On New Exposures

While General Average is a term with which most transportation professionals are familiar, it is a subject worth reviewing in light of new exposures that may fall within it.

Vessels on the high seas are subject to the General Average concept, which dates back to the ancient mariners. Under these terms, not only are ocean carriers not liable for loss or damage to cargo, but the cargo owner is actually responsible, in part, for the cargo of others, as well as the ship itself.

General Average arises when a sacrifice or expenditure is intentionally made or incurred in time of peril by one of the parties to the adventure, not for his own benefit, but for the benefit of all concerned in the enterprise, including the ship, cargo and freight.

The classic example of a General Average sacrifice is jettison to lighten a stranded vessel. Jettison is the throwing overboard of cargo or ship's material, equipment or stores. Most General Averages are caused by stranding, fires, collisions, or when a vessel is engaging in salvage assistance, or putting into a port of refuge due to an accident during the voyage.

When General Average is declared, the owners of the vessel and cargo are required to absorb a proportionate share of the loss to compensate the owner of the vessel and/or cargo that was singled out for the sacrifice. All participants in the maritime adventure contribute to offset the losses incurred, at an amount set forth by the average adjusters.

The object of a General Average adjustment is to place the parties to the adventure in the same positions, regardless of which of them initially sustained the loss or incurred the expenditure. The basis for General Average adjustment is customarily established in the contract of affreightment, which usually states that adjustment will be made according to the rules of a certain port, or if that port or country lacks jurisdiction, according to the York-Antwerp Rules.

The potential financial loss from General Average exemplifies the importance of cargo insurance, even for shippers of low-value merchandise. Without All Risk or Free of Particular Average (FPA) cargo insurance, cargo owners would be forced to post a cash deposit with the vessel owner to have the cargo released. This deposit would likely be tied up for two or more years until the General Average adjustment was completed.

Every shipper should have cargo insurance, even if they think their cargo does not have a value worth covering. The liability for General Average makes purchasing cargo insurance an essential business decision.

The American Institute for Marine Underwriters reports a decline in total loss figures in 2009, compared with 2008, and that is probably attributable to the continued slack of volume overall. According to the International Union of Marine Insurers (IUMI), the number of losses is likely to rise as the year progresses.

Below is a partial list of recent vessel casualties that have resulted in General Average claims:

January 2011 – The 15,988 gt bulk carrier Zim Itajai experienced engine failure in the Carribean seas.

March 2010 – The 37,709 gt bulk carrier Giant Pescadores collided with the 5,993 gt bulk carrier Bora in the Istanbul Straits.

December 2009 – The 39,941 gt container vessel CSCL Hamburg ran aground off Sharma El Sheik, requiring a 65 percent salvage security to be posted by cargo owners onboard.

November 2009 – The 14,431 gt bulk carrier Filitsa was hijacked by Somali pirates off the Seychelles.

October 2009 – The general cargo vessel Kimon A suffered a main engine breakdown between Texas and Bari and was towed to Las Palmas.

August 2009 – The 6,300 gt bulk carrier Harns ran aground on a reef off the Dominican Republic.

A few issues facing the industry have placed General Average back in the spotlight, one of which is the trend to slow steaming. Many carriers are leaving no stone unturned in an effort to reduce vessel operating costs, and slow steaming can save five to seven percent on operating costs for some long-haul carriers.

IUMI warns that slow steaming has prompted concerns about damage to main engines which are not designed to run within these new parameters, and although slow steaming upgrade kits are available from many engine manufacturers, it is questionable whether upgrades are being made. A concern in the industry is that main engine failures due to slow steaming may increase the number of General Average claims.

Some underwriters have also voiced concern about 'cold' lay-up of vessels, and the possibility that this may give rise to equipment failure when those vessels re-enter service.

Another issue that continues to escalate is piracy, and in particular piracy off the Somali coast. The International Maritime Bureau reports that piracy attacks increased from 114 in just the first six months of 2008 to 240 during the first six months in 2009.

While most cargo insurance policies will cover loss or damage to cargo stemming from piracy, there is concern as to whether ransom payments made to pirates are illegal, and moreover whether the vessel and cargo insurers contribute to an 'illegal' activity. Worldwide, anti-terrorism laws prohibit payments to groups tied to terrorism, and while there is no link between piracy and terrorism now, this continues to be an open question.

On April 13, 2010, President Obama issued an executive order preventing US citizens and entities from making payments to certain named individuals, and there is also the potential to prevent any payments to individuals or groups involved in or supporting piracy in Somalia. This executive order has spurred several questions and the Lloyd's of London Joint Underwriting Committee is seeking clarification. While it is generally agreed that piracy ransoms fall within the scope of General Average, the debate over ransom legality will ultimately be the deciding factor in how insurers will respond.

So while General Average may seem like an antiquated piece of maritime law, it is a dynamic vehicle that allows for a fair and equitable division of costs attributable to saving a voyage.

For more information, please contact us at 1-800-ROANOKE, ext. 1252 or info@roanoketrade.com