What are the **biggest claims?**

Enam Hussain, of The Standard Club, reviews the trends in claims right now

P&I insurance risks across international markets present a uniquely complex and challenging environment. International regulations, established and emerging risks, natural and man-made hazards, not to mention the inherent complexity of 21st century shipping, all combine to create a constantly evolving environment for P&I insurers, brokers and members. We believe this challenge can only be met by continuing to evolve our own claims services to keep pace with the change.

Today, claims management is a strategic role, not just a servicing one, and is a key part of the risk management and insurance process alongside other customer-facing functions such as underwriting, risk consulting and market (client and broker) management. We believe a claim is the true test of an insurer – the "moment of truth" in a member relationship which defines our service and reputation – and so this demands a proactive engagement with our members and their advisors to ensure optimal service. To deliver, we field more than 100 claims experts worldwide, covering the full spectrum of P&I risk. This expertise places us in a unique position, in that we are able to draw on our collective experience to provide qualitative and quantitative insight into these risks. When managing complex claims, there really is no substitute for experience. This article draws on our experts' knowledge to identify and review trends which directly affect our members' businesses.

Claims

Rising claims inflation, the growing problem of crew negligence and the high cost of wreck removal have all been contributing to a worrying rise in the cost of marine claims. Crew negligence is often a main driver behind three of the top five causes of loss (grounding, hull damage, and collision), excluding natural hazards and many fires, with it being a potential contributing factor in more than 60% of claims above €1m (US$1.36m). In the UK alone it is estimated 60% of all hull and machinery claims are for machinery damage and the vast majority of these are due to crew negligence.

The increase in crew negligence-related claims is one by-product of ship operators' efforts to more effectively manage costs. This has seen an increasing proportion of crew and masters recruited from around the world. Training and experience of crew sourced from various regions around the world becomes more and more of a concern, as standards and quality may be lower in many cases.

However, crew negligence is a complex issue that is not necessarily resolved by shipowners spending more money. A number of factors, including consumers demanding the lowest prices for goods and a shortage of well-trained quality crew in the first place and the fact that seafaring is not seen as an attractive career by many graduates, has resulted in a number of issues. For example, crews with lower standards of qualifications and training; language problems leading to issues with communication and understanding maintenance manuals; and modern crew relying too much on computer data. Underpinning all of this is the fragmented regulatory environment concerning the operation of ships and crew. Many bodies have little teeth in enforcing any regulations which often take a long time to get passed in the first place. It is relatively easy for the less diligent ship operator to circumnavigate the blue chip classification and flag states which means a vessel can be crewed with cheap labour and charge competitive freight rates which can be attractive to shippers.

The increasing cost of large hull claims in recent years also reflects claims inflation, fuelled by the rising cost of port facilities, labour and materials and the increasing costs of goods themselves. For example, The Standard Club is seeing an increase in values of 30% to 50% compared with previous declarations 12 months earlier. This trend is increasing and these claims are becoming more expensive for the reasons outlined. In reality these claims will never reach the level of a *Costa Concordia* loss, for example, but for insurers it is the level of frequency with which these claims occur that is of concern. It is difficult to see how this trend will be reversed and it is a trend that seems to impact most ship operators, irrespective of where they are domiciled.

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Containers and wreck removal

The largest loss in 2013 was the 86,692 GT *MOL Comfort* container ship, which broke in two and sank in deep water after sustaining a major mid-ship crack. The loss raises questions on the structural integrity of large vessels and the risk that some container ships are unknowingly overloaded. Misdeclared cargo and overweight containers are still a problem in the maritime industry. The current estimated insured loss for *MOL Comfort* is US$523m, comprising $440m in cargo losses and $83m for the hull.

Another particular area of concern for marine insurers is the cost of dealing with groundings, especially the potentially high cost of wreck removal. Wreck removal is becoming more complex and expensive as environmental concerns and improved salvage technology place greater demands on ship operators and their insurers. The *Costa Concordia* loss is a case in point. The vessel, which struck a reef and capsized off the Italian island of Giglio in January 2012 – but was successfully raised from the undersea platform on which it had been resting – resulted in one of the largest marine claims in history. According to reports, the cost of re-floating and removing the wreckage of *Costa Concordia* is likely to hit $1.5bn, with the total claim, including the hull value and passenger compensation, approaching $2bn (€1.47bn), according to a number of insurance market reports.

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Given the challenging operating environment, ship operators are looking for efficiencies and economies of scale, a trend driving a number of innovations in marine, such as larger ship sizes and the use of alternative fuels. Larger ships have implications for marine claims handling, both in cargo and hull. Claims arising out of maritime emergencies of "mega ships" could be huge, especially if an accident was to block the entrance to a port, generating sizable business interruption claims. Structural integrity of untested designs is also a concern, as is salvage. Wreck removal of large ships is technically feasible. However, the *Costa Concordia* grounding showed wreck removal costs can easily be a multiple of the hull value. And this is before considering the concerns about the salvage limitations for the latest and largest generation of container ships. For example, it has yet to be seen how the industry would cope with the salvage of almost 18,000 containers from a grounded mega ship. A salvage of such scale would take time, requiring new salvage techniques and equipment. There are also concerns around crew safety and training with regard to large ships, with the required experienced crew in short supply. Another emerging risk that claims practitioners in the sector are closely following is the increasing use of low-sulphur fuels, which is exacerbating the problem posed by cat fines – one of the greatest threats to engines. Cat fines are a by-product of refining made up of small particles of metal. As low-sulphur fuels require additional refining more cat fines are present in the fuel. Once a cat fine finds its way into engine parts it is very difficult to dislodge, causing serious damage and even engine failure.

Higher value, more complex and interconnected claims will require claims handlers to acquire new skills and knowledge, and make better use of technology and analytical tools in the future. Insurers need to learn lessons from losses and give feedback to clients to inform loss prevention measures. Members will increasingly want feedback and the ability to benchmark their own claims experience. Data and analytics will become more important and could help insurers and members get to the root cause of losses. Insurers will also need to co-operate more, both internally and externally.

Claims are exhibiting a mixture of unpredictable trends. Rising deductibles have undoubtedly cut into the frequency of attritional claims, and the number of such claims continues to fall. However the typical claim cost of an attritional claim continues to rise. In part the higher average cost is down to smaller claims being eliminated by rising deductibles, but also claims severity continues to rise. An average attritional claim costs 50% more than it did 10 years earlier.

The greatest unpredictability is seen in large claims – those higher than $1m: be they within The Standard Club's retention of those impacting the pool. Due to their random nature, these claims strike different clubs in different ways (in different years) and so we see volatility in individual clubs' performance. This claims volatility is becoming more and more influential on the club system, especially since the clubs are retaining more and more risk, both individually and collectively. Hydra is retaining bigger lines within the first $100m and is taking a bigger share on the first layer of the group reinsurance programme. The characteristic of "club risk" has changed markedly in the last 10 years: retaining bigger shares of the more volatile and random losses. This naturally stresses the clubs' individual finances and the changes all point to an increased risk-based capital requirement when Solvency II comes into force. *MRI*

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