

# AVERAGIUM

Newsletter of Harvey Ashby Limited, Average Adjusters & Claims Consultants  
Winter 2001/2

Welcome to the sixth edition of AVERAGIUM, Harvey Ashby Limited's Newsletter which we endeavour to publish twice each year. We trust that you will find the Newsletter informative and would welcome any comments or contributions.

Those of more mature years may recall that AVERAGIUM was the telegraphic address of Bennett & Co, the average adjusting firm with which Messrs Harvey and Ashby started their average adjusting careers in 1969.

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## **Comings & Goings**



*During the last six months we have visited Abu Dhabi, Dubai, Norway, Sweden, Australia, USA and Canada.*

## **Institute Time Clauses - Hulls 2002?**

Just a year ago we reported the failure of an initiative by hull underwriters in London to resurrect a London Market claims procedure. We now have to report on a setback, but hopefully not the failure, of another initiative.

The traditional hull insurance market in London has seen increasing competition in recent years from other markets, notably the Norwegian Market, which offer broader forms of coverage than that provided by the standard Institute Time Clauses (ITC)-Hulls. We have also seen the development of underwriting facilities within the London Market which provide broader and, what some might call, more modern coverage. These facilities include Dex and Marianne. It is evident that to remain competitive the traditional London Market needs to modernise its coverage.

With this in mind the Joint Hull Committee, the custodian of the ITC-Hulls, prepared itself to undertake a revision of the clauses. To its credit it realised that in order to avoid mistakes made in the past, when a lack of consultation led to the publication of a very unpopular set of clauses in 1995, it should co-opt representatives of the shipowning, broking, adjusting and legal fraternities onto the committee charged with the revision. This was done but before a formal announcement was made it was decided to postpone the effort.

It is to be hoped that this is only a deferment and not a cancellation. Revised clauses are clearly needed to maintain the competitiveness of the traditional hull market in London and in those other smaller markets which utilise the ITC-Hulls as their standard wording.

So what needs to be done?

Although the scope of cover to be provided is primarily a matter for underwriters, it is clear that to remain competitive it will be necessary to broaden the package offered. This means a move away from the named perils of the ITC-Hulls to an all risks cover, subject to specific exceptions or exclusions. Such an approach also has the benefit of simplifying the terms of coverage, particularly as it is customary to include statutory exclusions (applicable by reason the Marine Insurance Act) within the wording. The all risks approach, or, in the case of the Norwegian Plan, the all damage less exceptions approach, has already been adopted by competitors and is proving popular for obvious reasons.

The role of warranties is another aspect which requires consideration. The Marine Insurance Act requires that warranties be interpreted literally and, if they are not complied with, the insurer is entitled to avoid the policy from the date of the breach. Thus an insurer may avoid the policy, and thereby a claim, even though the breach of

the warranty may not have caused or contributed to the loss; what one might call a technical breach. The draconian penalty for the breach of a warranty has resulted in English courts now being very reluctant to find that a warranty is, in fact, a warranty.

The Australian Law Reform Commission has recently reviewed the provisions of the Australian Marine Insurance Act (virtually identical to the English Act) and has proposed that the provisions with regard to warranties be amended to introduce the concept of causal connection before an insurer can avoid a claim. Interestingly, it proposes also the abandonment of implied warranties so that all warranties would need to be included as policy conditions. Meanwhile, a marine sub-committee to the Committee on the Reform of Insurance Contract law in the UK has considered the English Marine Insurance Act and, in relation to warranties, concluded that the amendment of the Act is not required since the position at law could be amended by revision of the Institute Clauses.

Although the competing wordings recently introduced in the London Market, modify the legal position only slightly, it is hoped that any revision of the ITC-Hulls will grasp the nettle more fully.

Other areas which would merit consideration in any revision to maintain competitiveness include 4/4ths collision liability cover including fixed and floating objects, general average absorption, ship's proportion of general average deemed fully insured, bail provision, vessel to be deemed a ctl when the cost of repair / recovery exceeds 80% of the insured value and, finally, a mediation clause to promote dispute resolution with the minimum of conflict and cost.

It is understood that any revised clauses might also include a claims procedure, perhaps incorporating many of the provisions of the failed Hull Claims Protocol; see Winter 2000 issue of AVERAGIUM. However, it would appear that the single most effective action which could be taken to improve the handling of claims would be the introduction of a claims lead system, where the leading underwriter has the authority to take an active role in the claims process and to bind the followers.

Whatever provisions are ultimately incorporated in any revised clauses the opportunity must be taken to present those provisions in a logical and clear way using, as far as is reasonably possible, clear English.

It is to be hoped that the Joint Hull Committee will shortly take up the task of the revision of the ITC-Hulls so that the traditional London Hull Market, and the other markets and insurers which use standard English clauses, may remain competitive.

**/// harvey ashby limited**

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it is essential to take proper professional advice on specific issues.

## Generator Hire – an expense incurred to avoid delay or a temporary repair?

A sudden, major breakdown of a ship's auxiliary engine and resultant loss of its generating power may cause the classification society to impose a restriction on her continued ability to operate, pending repair of the damaged unit or the provision of an alternative generating supply.

The owner, faced possibly with an extended period of idleness of his vessel if the auxiliary engine is to be permanently repaired in port, may opt to engage a travelling repair squad to carry out the work at sea whilst the vessel continues to operate, courtesy of a portable generator 'plumbed' into the vessel's electrical system, that the owner hires and secures on board to satisfy the class requirement.

The owner, prudently, has avoided an involuntary period of lay-up of his vessel. He will be able to recover the expenses of engaging the travelling repair squad from the vessel's hull & machinery underwriters, subject to the expenses being adjudged as fair and reasonable. But what of the cost of hiring the portable generator? From whom can the owner recover this cost?

Although the use of the portable generator clearly has enabled the owner to avoid the vessel losing earnings whilst under repair, nevertheless, if the vessel's hull & machinery is subject to the ITC, Hulls, the claims adjusting and settlement practice appears to be different from what may be regarded as the strict position under English law.

Although the portable generator hire was an expense necessarily incurred as part of the cost of being able to permanently repair the auxiliary engine at sea, there is still a difficulty in overcoming the exclusion of loss by delay under Section 55 (2) (b) of the Marine Insurance Act [1906]; furthermore, charges incurred solely to avoid a delay caused by an insured peril have been held not to be recoverable under the sue and labour clause.

Notwithstanding the statutory position, an adjusting practice has evolved in the London Insurance Market, supported by underwriters' claims' adjusters, whereby generator hire is dealt with as akin to a form of temporary repair and, providing that the overall costs incurred, i.e. generator hire and travelling repair team costs, do not exceed the alternative costs of carrying out repairs at a repair berth, are treated as the reasonable costs of permanent repairs.

Consider another set of circumstances. A portable generator is hired because replacement parts that are required to permanently repair a vessel's damaged auxiliary engine could not be made available for 2 months. The use of the portable generator enables the vessel to continue to trade, with class approval, until the replacement parts become available. Of necessity the new parts are required to be fitted at a repair berth, i.e., the work cannot be carried out whilst the vessel is at sea. In this case, it cannot be argued that the combined cost of generator hire and repair costs incurred avoided a more expensive repair option. The portable generator supplied simply enabled the owner to continue to operate his vessel, rather than have to take it out of service awaiting the availability of new parts. However, it is argued that as the hull & machinery underwriters charge a premium for the ship as a profit-earning chattel, the incurrence of generator hire should be borne by these underwriters as an expense incurred of necessity by the owner. In the same way it is argued that temporary repairs form part of the reasonable cost of repairs in circumstances where material or parts necessary for permanent repairs are unobtainable at the vessel's first port of call, except after unreasonable delay.

Thus the reality is that, in London at least, there is an established practice for hull & machinery underwriters to admit consequential losses, in the form of generator hire, that do not improve the physically damaged condition of a vessel but enables it to avoid delay, notwithstanding the statutory exclusion to the contrary.

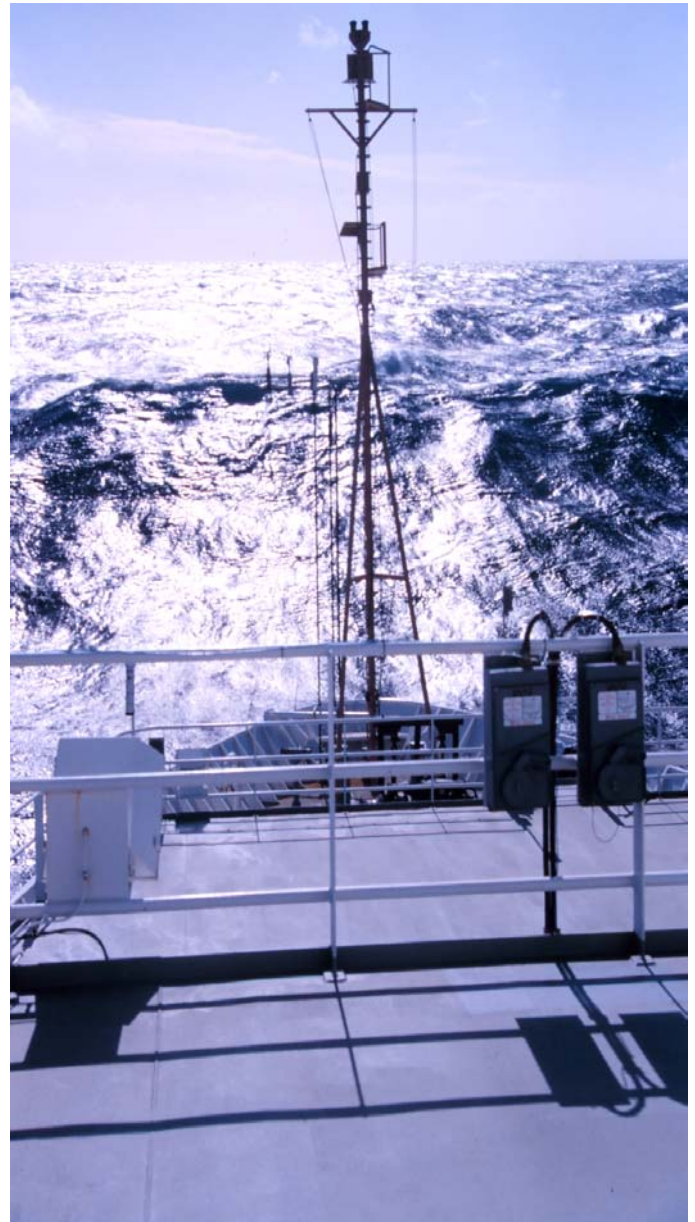
In comparison how does the Norwegian Marine Insurance Plan deal with this issue? The approach to the whole question of saving time is made on the basis that the hull & machinery cover positively absorbs such costs up to an amount equivalent to 20% of the vessel's hull valuation, where permanent repairs are deferred to a later date more convenient to the assured and when temporary repairs only are effected immediately. Similarly with regard to costs incurred that expedite repairs, the hull underwriter accepts these costs up to the equivalent of 20% of the vessel's hull valuation, for the time saved.

On the one hand the potential cost savings, spelt out under the Plan and recoverable from hull & machinery underwriters, for temporary repairs incurred for owners' convenience and extraordinary measures taken to expedite repairs, are more generous than appears from the cover provided by the ITC, Hulls. However, the Plan also makes clear in the Commentary

thereto that time saved by renting equipment, such as a portable generator, is limited in any claim on hull underwriters, to the period of hire required to enable a vessel to proceed to a repair yard; rental incurred beyond this point or in order to save time for the assured generally, is an expense that the Plan anticipates will be claimed under the assured's loss-of-hire insurance, a form of cover that the Plan regards as complementary to the corresponding hull & machinery cover.

Reverting to our two earlier examples, it appears that under the Norwegian Plan, in neither instance could claim be made on hull underwriters for the generator rental costs incurred, although in other circumstances, the assured may be able to recover generator hire, other than simply to proceed to a repair port, where generator hire was incurred as a convenient alternative to temporary repairs that could have been effected.

On reflection, it may be said that the Norwegian Marine Insurance Plan views expenses incurred that avoid delay in effecting repairs as recoverable collectively from the insurances that it is anticipated a prudent assured will arrange to cover both physical loss or damage and loss of time. Whereas, in contrast and as indicated above, at the present time it is believed that London Market Underwriters support a generous interpretation of the ITC, Hulls, with regard to the incurrence of generator hire, treating it as a form of temporary repair of the ship itself, the subject matter insured.



## John Constable 1776 - 1837



## Norwegian Insurance Plan 2002 Version

The Central Union of Marine Underwriters Norway (CEFOR) report that one of the amendments to the Plan of 1996, to be introduced in 2002, is an amendment to the indemnity payable during the periods in which repairs to an insured vessel are being carried out. It is understood that underwriters may agree to cover the wages and maintenance of the vessel and other expenses related to the running of the ship during such a period.

Until now, the crew's wages and maintenance and other ordinary expenses connected with the running of the ship during the period of repair, have been an express exclusion in the Plan, in line with the current ITC, Hulls, the AIHC, the Codex 2001 cover and that offered by 'Marianne' (the Allianz / Britannia hull & machinery facility).

At the time of going to press, the precise detail of the proposed amendment to Paragraph 12-5 had not been published, nor have we seen information as to how selectively this expansion of the cover will be offered.

Nevertheless, one can imagine that a cruise ship operator with a 30 day excess in his loss-of-hire cover might get quite excited at the prospect, although with today's ever-hardening market there's no such thing as free maintenance!

John Constable was one of the Britain's greatest landscape painters. He was born in 1776 at East Bergholt, a village no more than 10 miles from our Office near Colchester. He was the son of a prosperous corn merchant who owned two water-mills and 90 acres of land in Suffolk. Constable was educated at Dedham Grammar School, no longer in existence, and thereafter he entered the family business for which he had no real enthusiasm. His real interest lay in art.

Constable was encouraged to study by Sir George Beaumont, an amateur artist, and in 1799 he entered the Royal Academy in London. In 1802 he exhibited his first landscape paintings and was soon to develop his own individual style.

Constable became financially secure in 1816 when his father died. Shortly after this Constable married Maria Bricknell with whom he had seven children, five of whom became artists.

The artist is best remembered for his landscapes of Suffolk, however, he also painted scenes from Brighton, Dorset and Salisbury. Although, Constable also painted a number of portraits and pictures of topical events, such as the opening of London Bridge, he is not well known for these.

It is said that Constable was influenced by the dutch school of painters and that Jacob van Ruisdael, in particular, had a profound effect on his attitude to landscape. He once described one of Ruisdael's landscapes as 'true, clean, and fresh and as a brisk of champagne'. Constable's own technique involved capturing the atmospheric effects of changing light and the movement of clouds across the sky. He generally worked in the open air, drawing and sketching in oils but produced his final work in the studio.

During the 1820s he began to win recognition: *The Hay Wain* (National Gallery, London, 1821), perhaps his most famous painting, won a gold medal at the Paris Salon of 1824. This recognition in France was not mirrored by popularity in England where he only became well-known after his death.

The death of his wife in 1828 had a profound affect on Constable from which it is said he never recovered. Constable died in 1837.



## Website Review - [www.oilhistory.com](http://www.oilhistory.com)

This site represents the start of what may eventually turn out to be a seminal work on the history of the oil industry. Its Author, Samuel T. Pees, is a Certified Petroleum Geologist who has worked in North, Central and South America, the Caribbean, South Pacific, S E Asia, Indonesia and Australia.

The site comprises 18 chapters so far, that concentrate on the early days of drilling in North America and, in particular, the equipment used. In fact, one of the most interesting aspects of the site is the Author's discovery of abandoned drilling machines and equipment. It includes photographs of one location where drilling was abandoned, apparently with the drill string still in the hole!

The Author says: "Every Geologist has a snake story." He then goes on to recount his confrontation with a 23 foot long anaconda in the Peruvian jungle - he still has the skin to prove that it is not just another "one that got away" story.

The website is well constructed and reasonably quick to load bearing in mind the number of diagrams and photographs included. Highly recommended.



# What is a latent defect?

A latent defect has been judicially defined under English law as, a defect which could not be discovered on such examination as a reasonably careful, skilled man would make.

Both the ITC, Hulls, and the American Institute Hull Clauses, provide cover in their standard form for any loss or damage caused by “any latent defect in the machinery or hull” and sustained during the currency of the policy. At face value it could be suggested that this peril covers loss or damage resulting from any form of hidden defect in the machinery or hull. However, the Courts have imposed limitations on the generality of the wording.

Jackson v. Mumford [1902] concerned a novel marine engine design, trying to attain very high power with the least possible weight. The design included a hollow connecting rod that broke during trials. It was held that the con rod, although itself sound, was unsuitable to meet the conditions of service required in that particular vessel. The assured argued that a weakness in the design that could not be perceived by ordinary calculation, was a latent defect within the meaning of the policy. However, the Judge said that although no negligence was imputed to the designer, the needful degree of strength required of the con rod was greatly underestimated and he held that this did not result in a ‘defect in the machinery’, as provided by the clause because it did not cover the erroneous judgement of the designer as to the effect of the strain which his machinery will have to resist, the machinery itself being faultless, the workmanship faultless, and the construction precisely that which the designer intended it to be.

This judgement reminds us that, without specific wording, insurance is not intended to provide a product guarantee. There has to be some accident, some fortuity that causes loss or damage.

Jackson v. Mumford included obiter dicta to the effect that, the phrase ‘defect in machinery’ means a defect of material, in respect either of its original or after-acquired composition. As a consequence, the view was held for many years that the word ‘defect’ was limited to a ‘defect in material’ and that damage caused by a weakness or defect in design was not within the term ‘latent defect’.

This view of the limits of the expression ‘latent defect’ prevailed until The “Caribbean Sea” was heard in 1979. This case concerned the loss of a 19 year old tanker. A particular type of welding was used in way of a main sea suction valve that was a source of loss of fatigue strength, although this was not generally known when the ship was built. As a result a fatigue crack developed. This led in turn to a fracture in way of the underwater valve and the subsequent loss of the vessel.



The Judge in this case asked whether, in considering whether there was a defect in the machinery or hull, one is concerned with the actual state of the machinery or hull rather than the historical reason why it is in that state. The Judge held that if there can properly be said to be a defect in the machinery or hull and that defect was the proximate cause of the loss, it would seem not to matter that it had come into existence by reason of, poor design, or poor construction, or poor repair, unless other wording precluded recovery (such as a due diligence provision).

The finding in Jackson v. Mumford was considered in The “Caribbean Sea”. The Court noted that the dictum in the earlier case with regard to a ‘defect in material’ would not exclude a defect of material, for example in its after-acquired condition, resulting from a defect in design. The Court questioned the narrowness of the definition of ‘defect in machinery’, whether if machinery had been wrongly assembled, would that not, on the ordinary meaning of the words, be a ‘defect in machinery’?



What if machinery or the hull of a ship is so designed or constructed as to be inadequate for the task required? Or the ship is subjected to work for which it is, by reason of the inadequacy in design, unsuitable and loss or damage results? The judgement in The “Caribbean Sea” suggests that inadequacy of a particular part may constitute a shortcoming in the machinery or hull, rather than a defect. On the basis of these comments, possibly the hollow con rod, as considered in Jackson v. Mumford, might be regarded as a shortcoming in the machinery, rather than a defect therein, the concept being, with hindsight, inadequate for the intended task.

The question, therefore, of whether loss or damage has been brought about by a defect in the machinery or hull or by a shortcoming, appears to be a question of degree. The effect of The “Caribbean Sea” is that a broader view of the words - any latent defect in the machinery or hull - can now be supported by this authority and which might be said to be more in accord with commercial reality.

At the beginning of the article, we quoted the test for latency as being a defect that could not be discovered on such examination as a reasonably careful, skilled man would make. What if the defect could not have been discovered by the assured but may have been discoverable by a manufacturer or seller of the part containing the defect? Can it be argued that the peril should be restricted to those instances where no one reasonably could have known of the defect?

Two English law cases appear to dispel this narrowing of the test of latency. The first is Hutchins Bros. v. Royal Exchange Assurance Corpn. [1911]. A foundry that had supplied the casting for a vessel’s stern frame in 1906, deliberately concealed the fact that shrinkage cracks occurred when the metals used to make the casting cooled. Their deception was successful and the defect in the stern frame did not become patent until three years later. The Court held that the condition of the vessel’s stern frame was a latent defect that had become patent.

The second case is the more recent, “Nukila” [1997]. The Court of Appeal judgement noted the original defect as follows. The circumferential welds attaching the top plates of the spud cans were not properly profiled. The classification society supervising the building of the mobile self-elevating accommodation and work platform, required all the relevant welding to be in accordance with their rules. The Court noted that the inadequately profiled welds were in a high stress concentration location and the poor condition of the welds would increase this concentration excessively and be likely to shorten the fatigue life of the structure and lead to fatigue cracking. The Court noted that over the past 40 years metal fatigue has become a well-understood process. It was stated that a badly designed or made weld may lead to a concentration of stress which will then over a period time cause the condition of metal fatigue to arise. It did in this case, leading to fatigue cracks that in turn gave rise to fractures in the parent metal. The judgements given did not question that the minute fatigue cracks, undiscoverable by the assured, were not latent defects, once they had concluded that damage consequential upon defective circumstantial flawed welds had arisen.

The conclusion to be drawn from the two quoted cases is that what is important in determining whether or not a defect is latent is whether or not it is latent to the assured.