MORTGAGEES ENHANCED WAR COVER

Enhanced war cover (EWC) is a hybrid insurance product placed in to the London marine war market which provides extended coverage for certain war perils which otherwise would be insured in the political risks market.

Enhanced war cover is accepted by many leading maritime financiers as a credible insurance solution where the collateral asset against which funds have been advanced is relatively mobile, e.g. a drillship or floating production and storage offloading vessel.

Placed in the London marine war market instead of the conventional political risks market, the EWC product requires less lead in time than a "full" political risks policy as the war market does not require certain time consuming documents associated with a political risks policy namely:

- A signed and completed proposal form.
- Legal opinion confirming the enforceability of the mortgage.

Placed on an amended version of the Institute War & Strikes Clauses, Hulls - Time 1.10.83, great care must be taken to ensure the clauses are correctly adapted to provide cover appropriate for the needs of the mortgagees in each specific instance. Further details of the amendments needed can be provided upon request.

WHAT DOES AN EWC POLICY COVER?

A correctly worded EWC policy will provide all the main elements of a full political risks policy, with certain exceptions.

WHAT ARE THE POTENTIAL SHORTCOMINGS OF AN EWC WHEN COMPARED TO A TYPICAL BANK'S POLITICAL RISKS POLICY?

Unlike a bank's political risks insurance the maximum period an EWC policy can be arranged for is 18 months, this is to comply with regulatory restrictions in the insurance market stipulating the maximum periods for which war insurances can be arranged.

Potentially, therefore, should the political stability of the insured country deteriorate throughout the duration of the 18 month policy, the financier runs the risk that coverage may not be available at the same price at renewal. To minimise this eventuality a correctly worded EWC policy permits the cancellation and early renewal at a mutually agreed time during each 18 month policy, typically at the 9–12 month point. This cancellation provision is only available to the insured (mortgagee), and highlights in advance any problems at the forthcoming renewal and therefore ensures the financier and the borrower have a period of 6–9 months to make alternative coverage arrangements or to arrange the removal of the collateral asset from the waters of the insured country.

For this reason EWC is most suited to collateral assets which can potentially be moved within a reasonable timeframe should the political stability of the insured country deteriorate during the lifetime of the loan.

WHY CAN'T FINANCIERS JUST RELY UPON THE BORROWER'S/MORTGAGOR'S STANDARD WAR RISKS INSURANCE?

The main reasons a financier should not rely upon a standard war risks policy arranged by the borrower are:

- War risks policies can be cancelled at any time by insurers giving seven days' notice of cancellation.
- While a borrower's policy may respond to an overt, or hostile, act of confiscation by a foreign government which undertakes a widespread seizure of assets, an isolated seizure is likely to be resisted by war underwriters on the grounds the proximate cause is considered to be a contractual dispute and/or infringement of a local law/regulation.
- Confiscation or requisition by the country of registration is an exclusion under standard war policies.
- Standard war policies would not cover any attempted repossession of an asset following default under the loan.

DOES AN EWC INSURANCE REPLACE THE NEED FOR AN OWNER-BOUGHT BASIC WAR POLICY?

An EWC can be arranged in the name of the owner and the financier. However, often the jurisdiction in which the asset is to be based/located will require insurances to be placed locally in the first instance and then reinsured into international markets. This makes a joint policy difficult if not impossible to arrange. For this reason, more often than not an EWC policy is arranged in the name of the financier and will typically exclude claims more correctly recoverable from the owner's "primary" war policy; the EWC will usually warrant the primary war policy is maintained during the lifetime of the EWC. It will also be limited to the amount of the outstanding loan (plus an uplift if required) and can be arranged on an amortising basis.

WHAT HAPPENS IF THE PRIMARY WAR INSURERS ISSUE SEVEN DAYS' NOTICE OF CANCELLATION?

By way of the legal obligations under the loan agreement and the undertakings given by a broker when signing the letter of undertaking, both the owner and his insurance broker have the contractual obligation to immediately advise the financiers if notice of cancellation is not rescinded. This gives the financier a short period of time to rectify the situation in conjunction with the owner. A properly worded EWC will provide an extended window during which the financier can achieve this.

HOW MUCH DOES AN EWC POLICY PAY?

EWC pays the lesser of:

- The amount lost by financiers.
- The EWC policy sum insured.

WHY INSURE MORE THAN 100% OF THE OUTSTANDING LOAN?

The seizure of a collateral asset by a foreign government is often accompanied by a default in debt servicing by the borrower, who may well be owed charter payments itself. In addition, the loan will incur certain additional expenses, for example, default interest and additional costs incurred in managing a loan in default. These additional expenses can be included as part of the sum insured under an EWC sum insured; typically up to 120% of the outstanding loan is insured under an EWC policy (note that any additional amount in excess of the loan amount must be substantiated to form part of a claim).

CAN AN EWC CLAIM BE SUBMITTED EVEN IF THE BANK HAS ADDITIONAL SECURITY?

Yes, an EWC policy is not subservient to any collateral or guarantees the financier may have.

WHY NOT ALLOW THE OWNER TO ARRANGE THE EWC WITHIN ITS PRIMARY WAR POLICY?

An owner-arranged EWC may be deficient for a number of reasons and depending upon the circumstances it may not be in the best interests of the owner to have the EWC within its primary policy. Further details can be provided upon request.

HOW MUCH PREMIUM CAN BE SAVED BY PURCHASING AN EWC POLICY IN PREFERENCE TO A "FULL" POLITICAL RISKS POLICY?

As the EWC insurer is not committing its balance sheet on a non-cancellable basis for lengthy periods (sometimes as long as seven years), substantial premium savings can be achieved. It is not uncommon for premiums savings in excess of 50% to be achieved by a discerning financier when compared to the equivalent political risks rate.

WHY DO RATES FOR EWC/POLITICAL RISKS VARY SO MUCH?

Available capacity can vary daily following changes in the political situation in the country on which coverage is to be purchased. Additionally, individual underwriters may have diametrically opposed views on the same country. Each insurer will have a so called "country limit aggregate" for each country (as predetermined by an agreement with its own reinsurers). For these reasons insurers typically only provide costing indications valid for 24 hours. All these factors mean that the political risks/EWC market is one of the last true supply and demand market places in the Lloyds insurance market.

HOW DIFFICULT IS IT TO ARRANGE AN EWC POLICY?

From the perspective of the insurance adviser/broker, arranging an EWC policy is more complex than arranging a standard war policy and equally complex when compared to arranging a political risks policy. For example:

- Amendments to the standard war policies must be carefully considered and discussed with potential underwriters to ensure the policy provides the required coverage.
- Policy periods must be carefully monitored to ensure the policy is rolled forward at the most suitable moment in each policy period.

Conversely, from the perspective of the financer arranging an EWC policy is much simpler. There is no need to complete a detailed proposal form or to obtain legal opinions from local lawyers confirming the potential enforceability of the mortgage through the insured country's legal system should the need arise.

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