

GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED

L/561

22 October 1956

Limited Distribution

Original: English/
French

FREEDOM OF CONTRACT IN TRANSPORT INSURANCE

Memorandum submitted by the International Chamber of Commerce

"In order to show that the measures restricting the contractual freedom of the parties in transport insurance cause definite harm to international trade, even though this harm is not readily measurable, the International Chamber of Commerce submitted various concrete examples in support of this view to the Tenth Session of GATT.

"Since then the circulation of the International Chamber of Commerce's brochure on 'Freedom of Transport Insurance' and the inquiries for which this publication was used as a basis made it possible to collect comments, which in fact confirm the difficulties reported in the brochure.

"Although further replies are awaited, it has been felt useful to report the results so far obtained to the attention of the CONTRACTING PARTIES, for consideration at the Eleventh Session of GATT.

"The International Chamber of Commerce has the honour to submit a summary herewith."

EXAMPLES OF THE HARM CAUSED TO TRADE BY MEASURES RESTRICTING THE FREEDOM OF TRANSPORT INSURANCE

General Observations

In general the replies received express full support for the International Chamber of Commerce's policy in the matter. There are, however, some large manufacturing firms which, because of their method of conducting their business, experience little or no inconvenience when obliged to trade on C and F terms. Others, also perhaps in the minority, support the principle of freedom for trading conditions but tend to accept the restrictions under consideration as unavoidable irritants, rather than as positively harmful to trade. It seems helpful to state this viewpoint, because the attitude of traders will generally be found to vary greatly according to the type of business which they transact and the countries with which they deal, and will also depend on whether they have had losses or claims have arisen. All the same this fact does not weaken the case for those who in fact experience inconvenience and difficulty.

Confirmation has therefore been given, by one source or another, of all the difficulties cited in the brochure. One very large firm of the highest international reputation has said:

"In broad terms, as our business is world wide, we have experienced all the difficulties mentioned in the brochure. We are fortunate in some respects in having Associated Companies in some countries where restrictions apply, e.g. Argentine, so we can be sure goods are adequately covered.

"In many markets we know it is the custom not to take up documents until the importer is sure the goods have arrived in apparently sound condition. This being so, it is most unlikely that, if the goods had to be insured in the importing country, satisfactory arrangements would or could be made, particularly if there was a loss. Most likely if there was a loss the importer would have nothing to do with the transaction and the shipper would be left with the consignment lying at his risk and expense. In view of this we endeavour to insist on payment by Letter of Credit although we might otherwise have given credit. Alternatively we take out a contingency insurance.

"Where insurance must be effected in the importing country, e.g. Colombia or Argentine, rates charged are invariably higher than what we would pay in the United Kingdom. In some cases we have seen the cost is three or four times the United Kingdom Market quotation.

"The need to cable an overseas customer or foreign insurance company particulars of intended shipments - their description, values, C and F, names of vessels and sailing dates, taking into account the many changes that can arise, is an added responsibility and costly. It is a needless additional requirement introduced by restrictive practice."

French forwarding agents also confirm that, without themselves suffering any direct loss from the restrictions on transport insurance laid down in certain countries, since the goods do not belong to them at any time, they have, as intermediaries between seller and buyer, an opportunity of witnessing discussions and even disputes between them. They thus observe that obligation to contract insurance imposed on one of the parties distorts the normal conditions of sales or purchase contracts, as is shown in its study of the case of a seller who offers his goods on CIF terms, whereas the buyer can only accept it C and F.

This is also, they add, the case of a seller who finds he is unable to negotiate shipping documents with his bank in order to obtain credit from the latter, because the insurance is covered by the consignee and the guarantee would thus be out of the hands of the creditor in the event of damage or loss.

Lastly, they state that the harm done is especially due to the fact that it becomes impossible for them to conclude certain business deals, although all the other conditions were satisfactory.

It is thus difficult to give figures for the loss. It consists especially in preparatory expenses and in completely fruitless journeys, and also in a waste of time.

Difficulties due to the obligation to sell C and F

The difficulties resulting from this obligation to sell C and F, instead of CIF, are confirmed and illustrated by the replies received from various countries.

Two Belgian traders report, without being able to give figures, the difficulties caused them by the obligation imposed on buyers in Argentina, Colombia, Pakistan and the Philippines to insure the transport themselves.

When they have to ship goods to overseas countries and have to draw on foreign customers on demand, these exporters run serious risks if the customer stipulates that the delivery must be made on a C and F basis. It may very well happen that the customer at the destination forgets or fails to insure the goods and when their banker presents the draft at the destination the goods have suffered damage which should normally have been covered by insurance. If the customer in question has payment difficulties before presentation of the draft, they run the risk of being and remaining their own insurers for such goods.

Some detailed examples from Germany confirm the existence of the same difficulties:

- (a) A German exporting firm despatched a consignment to Colombia. In such a case the insurance has to be covered by the customer in Colombia. The goods were damaged in transit and the customer simply deducted the sum of money involved from his remittance to the German exporter. So far, efforts to persuade the customer either to refer the matter to the insurance company or to make the necessary documents available for recovery of the loss have been of no avail.
- (b) In the summer of 1955 a firm in Bremen shipped a consignment of enamelled ware to Baranquilla in Colombia. The goods were damaged by the enamel being chipped off. The Colombian insurance company rejected the claim and the consignee deducted the sum of US \$ 200 from his remittance to the German exporter.
- (c) A Hamburg firm had shipped a load of iron goods C and F to Bolivia. The shipment was damaged by rust on arrival. Here too, the Bolivian insurance company rejected the claim because, as they claimed, the goods were already rusty when loaded. The consignee deducted the sum involved from the total on the invoice.

(d) As a part of a general order received from a customer in Colombia, a Hamburg exporter sent the customer a crate containing 63 x 1 kilogram tins of plant extract in the form of a thick liquid. On the arrival of the crate at the place of destination, it was discovered that 14 tins were missing and that the others had leaked considerably. The representative of the Hamburg firm was instructed to take charge of the crate, and convey it to the customer and claim payment on the loss from the Colombian company, with which the customer had himself insured the goods. Only after several reminders did the representative of the exporting firm learn from the customer that the goods were only insured against total loss, so the insurance company could not be held liable for partial loss.

The existence of discrimination is evident: since the Colombian Government has decreed that consignments sent to Colombia must be insured exclusively with Colombian companies, a foreign buyer has not the least influence on the form of the insurance. In other words, he cannot provide insurance suited to the nature of the goods.

Double Insurance Costs

The brochure had already mentioned the double insurance costs in which the exporter is involved owing to his uncertainty as to the insurance when it has to be contracted by the buyer.

Two large industrial firms in the United Kingdom state that the rates of such premiums may amount to as much as half and two-thirds respectively of the normal marine premium to the destination concerned. One of these firms says that to cover this cost the practice is to charge CIF prices but to invoice C and F.

The situation which may arise when goods are lost in transit or for any other reason do not reach their destination has been well expressed by another firm, as follows:

"If such goods are not fully insured under the consignee's insurance policy, the consignee, being unable to recover the value of the goods from his insurance, may in certain circumstances be unable to honour his obligation to the seller by remitting the price of the goods. Unless the seller has his own insurance on the goods his only remedy would be by a claim against some third party, such as the steamship company, and even then he would obtain only the net value of the goods as declared at the time of shipment."

The same firm adds that there have been many instances in which customers have instructed the seller not to insure because they are making their own arrangements but it is found, when an emergency arises, that no insurance at all has been taken out, the customer having elected to take the risk.

Another firm has reported that on a number of occasions, when instructions have been received to advise a certain insurance company abroad for cover purposes, that company has replied that it no longer receives the business of the buyer concerned.

Referring to the regulations in Pakistan, this firm reports as follows:

"We should raise no objection to this stipulation provided our interests as shippers, and that of our assigns, is held covered for each shipment made. It is, however, too often the case that a Pakistan importer will provide us with a paper from a Pakistan Insurance Broker or Company which is, in fact, no more than an acknowledgement that Insurance has been provisionally declared. What we have to press for in every case is an actual Insurance Cover Note naming ourselves as the beneficiary and naming a United Kingdom Insurance Office to which we can make an Insurance Declaration of shipments and from which we can obtain an actual Insurance Certificate.

"There are instances where, because of the time element, arrangements for which we ask are not made by the time that goods are shipped. In such cases we are therefore virtually carrying the Insurance Risk ourselves."

Yet another firm has cited an actual case to exemplify how loss can be caused through inadequate insurance by the buyer. This case concerned a shipment of textile machinery insured (compulsorily) in the country of destination:

"Quite unknown to the exporter there was a considerable delay in clearing the goods on arrival, and in the meantime a claim arose. It was then found that the importer had arranged insurance with a domestic company, which did not automatically extend its cover, as is British practice, in the case of delays in clearance. As a result, any insurance liability was rejected, and the exporter was involved in a loss amounting roughly to 5 per cent of the value of his shipment. This could not have occurred if the exporter had arranged insurance cover with a British company, and illustrates how financial loss can be incurred through the fact that the exporter has no control over the action of the importer in arranging adequate insurance for the goods in transit."

PARALYSIS OF COMMERCIAL TRANSACTIONS

In addition to the difficulties arising from the obligation to accept C & F terms and the consequent double insurance costs, the brochure had stressed the paralysis of commercial transactions resulting from the measures in question. They have three major effects:

1. Effect on competition

Double insurance costs may affect competition. For the reasons stated in the brochure, an exporter, who does not know the terms of the insurance effected by the buyer and who cannot without loss of business insist on prompt payment, is obliged to take out contingency insurance.

Where profit margins are narrow this may result in an addition to his prices which may in turn seriously affect his competitive position. As one firm has expressed this situation:-

"A shipment was effected on C & F terms to a country employing discriminatory transport insurance regulations. The exporter subsequently found that the insurance cover arranged by the overseas importer was only for perfect goods. This meant that if the goods had been damaged during the voyage and the documents not taken up on their arrival, the exporter would have been left without any cover at all. As a result, he and other exporters shipping to this market have had to arrange a contingency insurance with a British company for which a substantial portion of the normal premium is charged. This adds to the price of the goods and damages international trade where competition is keen and a marginal price increase can mean the loss of an export order."

2. Effect on commercial credit

The restrictive measures affect the commercial credit that a number of enterprises would like to be able to grant their foreign customers without insisting on being paid by letter of credit or in advance in the importing country.

In such cases, as has been pointed out, they may either have no cover at all against loss or damage, or inability or refusal of the buyer to accept the goods, or else they will be dependent on cover taken out with an insurer in the importing country without certain knowledge that the risks are adequately covered or that claims will be met without difficulty. If they insist on pre-payment in cash or against letter of credit they run the risk of failing in a competitive market. As a large cotton yarn firm has stated:-

"In the Argentine we have hitherto not been affected because we have sold on irrevocable letter of credit terms, thus obtaining our money (provided all documents were in order) before the maritime risk was incurred. Where the conditions are cash against document on arrival, we cannot sell on those terms without incurring the risks so clearly expressed in the brochure.

"In other words, the restriction of insurance facilities is an inducement to the seller to insist on stricter terms than could otherwise be allowed to the buying country. That is one of the aspects in which the importing country hampers its own interests by unreasonable insistence on insurance with its national companies which limit the desirable breadth of underwriting, and raise the problem of exchange if claims have to be paid."

3. Combined effect of restrictions and exchange control

There is also the case of the association of insurance restrictions with exchange control. The brochure has shown how trade may be paralysed when a country combines strict licensing of imports and exchange control with insistence on insurance with domestic companies; examples have been given both of a seller's difficulty in obtaining payment of insurance money in suitable currency and of an importer's difficulty in obtaining the foreign currency necessary to order a replacement of lost or damaged goods.

The difficulties of the importer are particularly interesting, and they point to certain advantages of CIF terms to the importer, in the following manner. In a C & F transaction, if loss or damage occurs and payment for the goods has already been made before the time of loss or damage, the importer may be content to receive his insurance money in his own currency, and if he wishes to make a replacement order he must apply afresh for foreign currency. Frequently, however, importers make prior arrangements with their insurers for payment of claims in a foreign currency acceptable to the seller and, if the terms are cash against documents on arrival, it might be expected that payment in the event of loss should be made direct by the insurers to the seller in that currency. If so, the importer might still be able to use his original currency allotment to order replacement goods. However, in such cases it sometimes happens that the exchange control authorities cancel the importer's original allotment of currency on the two-fold ground that the goods were not in fact delivered and that payment for them was made by the insurers out of the insurers' allotment. The importer may then be left without foreign currency to pay for replacement goods despite the care which he took to protect his position. It is therefore very much in the interest of importers, in countries where foreign currency is strictly limited, to be able to purchase CIF, if they wish, so that payment in the event of loss or damage may be made by the exporter's insurers and thus without recourse to the foreign currency reserves of the country of import. An example is quoted by one Chamber of Commerce:-

"One of our members shipped a quantity of textiles to Argentina, the insurance being effected in that country in accordance with government regulations. During transit the goods were damaged and off-loaded at an intermediate port. A claim was subsequently made on the Argentine insurance company for the loss involved; which took nearly

two years to settle. When payment was finally made in respect of the claim, it was held by the Argentine authorities to have utilised the import license. The Argentine importer could not get another import license in place of the original and thus was deprived of his goods. Had the insurance been effected with a British company, the Central Bank in Argentina would not have had to disburse sterling in settlement of the claim, thus depleting its currency reserves. Also, a replacement shipment could have been effected under the original import license and the importer would have got the goods he had ordered. Although the case quoted related to a shipment of textiles, we have had similar reports, not only from Argentina, in regard to vital spare parts for industrial machinery. In these cases the effect of such regulations has been very much more serious, as equipment has been lying idle waiting for vital spares which could not be supplied due to the original import license having been utilised through the payment of an insurance claim for the loss of spares during transit. Not only have such instances resulted in British exporters losing valuable business, but serious damage has been caused to the internal economy of the country concerned."

Other cases of losses sustained by exporters in C & F sales, because it has not been possible to transfer the payment of the insurance on account of exchange regulations, are reported from Germany.

(a) A Hamburg firm reports on a case in which a machine wire plant for the Argentine sustained damage amounting to 1,100 DM during loading. At first the claim was only acknowledged by the Argentine insurance company by word of mouth. After nearly a year of constant intervention the insurance company paid the sum involved to the Argentine consignee in the currency of that country. The consignee was unable to transfer the money.

(b) A firm in Western Germany manufacturing boilers and equipment for power stations delivered parts for a power station to Turkey.. The consignment suffered damage on board the ship and on the Turkish railway to the extent of 3,470.57 DM and 3,023.20 Turkish pounds (4,550 DM). Due to the Turkish regulations the customer had apparently asked for insurance to be covered in Turkey and this was done with the Ankara Türk Anonim Sigorta Sirkreti in Istanbul. The premium was paid at the proper time in Turkish pounds. In spite of this the Turkish insurance company has not yet settled the claim and, if such a payment does take place, it would probably only be possible in non-transferable Turkish pounds, owing to the Turkish currency laws.