CONTINGENCY INSURANCE:
What is it? Who Should Buy It?

By Timothy Danford

Contingency insurance is like having "backup" insurance, and is available on almost every open cargo policy at a nominal cost.

Also called "seller's or buyer's interest" coverage, contingency insurance protects importers and exporters. It allows them to insure their cargo on a "contingent" basis in situations where Incoterms dictate the other party must provide cargo insurance.

Coverage provided under contingency mirrors as the "all-risk" coverage provided on an open cargo policy. Contingency insurance is triggered by:

- A physical loss to the cargo.
- The other party's insurance being non-responsive and/or the other party refusing to pay for the goods.

In a covered claim situation, the insurance company would advance the loss proceeds to the insured in the form of a no-interest loan. The insured would then work with the insurance company to help collect from the other party or its insurance carrier, and any proceeds would be returned to the insurance company that advanced the funds.

If the proceeds cannot be collected from the responsible parties, the insured has satisfied its duties under the policy and the loan would become the final payment.

There is a strict condition stating the insured cannot divulge the existence of the contingency coverage to any party; otherwise, the responsible party may neglect to secure insurance on the cargo if aware the other party has backup insurance.

Let's first analyze an actual contingency loss example from an importer's perspective where they are the insured and consignee.

A U.S. importer bought several shipments of steel pipe from a mill in China on Cost, Insurance and Freight, or CIF, terms. The pipe arrived damaged, resulting in a $20,000 loss. The importer was instructed to contact the supplier's local surveyor to file the claim, but never received a response. The insurance provider in China was also non-responsive.

After a few months, the importer contacted the supplier, who denied any responsibility as the pipe was shipped as per contractual terms. The importer's request to replace the pipe without a new order and repayment was also denied.

Unfortunately, the claim is still unresolved after several months. Had the importer purchased "buyer's interest contingency" coverage, the loss would have been paid in full and any future proceeds from the supplier's insurance would have been directed to the importer's insurance company.

Unfortunately, these types of scenarios are happening with more frequency. We recommend importers buy on Free On Board or similar terms, whereby the importer controls the insurance on their cargo. However, some importers must buy on CIF terms because of cost factors.

Importers should be aware that when purchasing on CIF or similar terms, Incoterms simply dictate who is responsible to insure the cargo, but do not indicate the scope of coverage to be applied — much less the financial strength of the insurance provider on the risk.

A simple low-cost solution is to purchase contingency coverage through a trusted provider. Importers who buy on credit terms may also want to consider contingency coverage.

For U.S. exporters, the need for contingency insurance is even more prevalent as there are many exporters who sell on FOB or Free Along Side terms and provide open account credit terms to their buyers.

Here is an example of how seller's interest contingency would come into play.

A U.S. exporter sells a containerload of electronics to an importer in Latin America on FOB Ex-works terms and on 60-day open account terms. The container is hijacked in Latin America, resulting in a $300,000 loss.

The importer was responsible to insure and did; however, the importer did not have an armed escort (as was required by its insurance company), and the loss was denied. The importer then refused to pay the exporter. Luckily, the exporter had placed contingency/seller's interest coverage on the load and was reimbursed by its insurance company.

Who should buy contingency coverage? Both importers and exporters who:

- Have a financial interest in the goods.
- Are uncertain as to the quality of coverage provided by the other party's insurance.
- Want the peace of mind of knowing their trusted insurance provider will assist in a serious situation. BB

Timothy Danford is a vice president in Roanoke Trade's Miami office. He can be reached at tim.danford@roanoketrade.com. Roanoke Trade is a member of the Munich Re Group and an affiliate of Watkins Syndicate at Lloyd's of London.