

Shipping Industry Vulnerable Following Hanjin Administration

Shipping company Hanjin recently announced it was entering administration, following financial difficulties. As part of a shipping industry that is becoming increasingly interdependent, the company's issues are likely to have an impact on ports and terminals, crews, other shipping companies, transport companies, and beyond.

THE SITUATION SO FAR

Hanjin Shipping of South Korea, the world's seventh largest containership operator, operating 98 containerships (some owned, some chartered) and several other types of ships, had been struggling financially for some time, building up debts of reportedly more than US\$4 billion. On 30 August, a restructuring finance deal fell through and the company went into administration. The results of this were immediate and dramatic.

Within hours of the announcement by Hanjin, creditors moved swiftly. Meanwhile, other shipping companies have sought to defend their own positions, so as not to be dragged down as well. Hanjin's entering into administration has created issues for the CKYHE alliance, existing between Cosco, "K" Line, Yang Ming, Evergreen, and Hanjin Shipping. The alliance partners of Hanjin have announced that they will no longer ship their goods on Hanjin vessels and would not carry Hanjin containers on their own vessels.

Within a day of the announcement, ports began to refuse to allow Hanjin vessels entry into their ports, for fear of not being paid port fees. The 3,700-TEU containership, *Hanjin Rome*, has become the first Hanjin vessel to be arrested by creditors, while it was in the port of Singapore, according to reports. Goods due to be shipped on those Hanjin vessels that are now barred from entry have begun to build up in ports. The owners of the goods have consequently been exposed to financial risks following the failure of the ship operator, as contractually agreed delivery dates would be missed, goods would need to be stored, and extra expenses incurred as alternative routes for delivery would need to be arranged.

The time of year also presents additional challenges, as August to October is generally the busiest time of the year for the shipping industry, as companies stock up for the holiday season.

WHO IS LIKELY TO BE AFFECTED?

Due to the inherent interdependency in the industry, the impact is likely to be far-reaching. Below, we examine those who are likely to immediately feel the effects:

CHARTERPARTIES

Firstly, of the vessels operated by Hanjin, the majority were not in fact owned, but chartered by the company, with Hanjin paying the owners a daily charter hire amount for the use of the vessels, as is common under bareboat, demise, or time charterparty agreements. It is often difficult to tell, simply by looking at a vessel, as to whether it is owned or chartered, as one of the terms common to such charterparty agreements is that the charterer can have the vessel painted into its own colors. As a result of the recent developments, the owners of those ships operated by Hanjin may stop receiving the charter hire amounts, and would therefore seek to terminate the charterparty



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agreement and re-take possession of their vessels, with a view to chartering them out to another charterer.

With a considerable number of vessels likely to be affected in this way, the market for hire rates for such vessels may be reduced due to increased competition. As a result, owners may face a reduction in income when they do find a new charterer, or, failing that, be forced to have the vessels laid up and suffer a complete loss of earnings.

TERMINALS AND PORTS

Terminals and ports to which the Hanjin vessels were scheduled to visit may need to protect their own financial position, knowing that the payment of port fees, tug and pilot services are at risk if they do permit the vessels to come into their facilities. They could be at risk of not getting paid for these vessels entering the port.

For those vessels owned by Hanjin, as well as being barred from port entry, they may have been subject to mortgages from banks, which could seize vessels under the terms of the finance agreements once Hanjin goes into default on those loan agreements.

FREIGHT FORWARDERS

Freight forwarders could be put in a difficult position if they have taken goods into their care (or have contractually agreed to do so), as those contracts may impose financial penalties if the goods are not delivered to the right place at the right time. If the freight forwarder has scheduled to have the goods loaded onto a vessel that does not arrive, they will have to find an alternative, which could prove expensive, particularly as many freight forwarders will also be looking to find alternatives. This is unless the freight forwarders have arranged to be contractually held not liable by the owners of the

goods in their freight forwarder agreements, in the event of the financial insolvency or default of the scheduled carrier. However, few freight forwarders are likely to have considered this.

All this could lead to ports becoming rapidly inundated with containers which are unable to be shipped quickly. Available space to store these containers could soon become exhausted; therefore, the ports and terminals may have to close their gates to Hanjin-scheduled containers.

This will then have an adverse effect on independent truck companies, rail freight companies, and hauliers, as they will be refused entry to ports and will have to find a means of storing these containers, with the added financial burden of not being paid for having failed to deliver the boxes to the port. In order to avoid entering financial difficulties themselves, such companies may have to refuse to load boxes scheduled to be carried on Hanjin vessels. While this would reduce the problem of storage, it would also reduce their income. In addition, since many trucking companies work on very tight financial margins, the financial insolvency of Hanjin could lead to the financial default of others all along the supply chain.

CREWS

The crews on Hanjin-operated vessels may find themselves at risk of not being paid, or receiving reduced pay, and being left stranded at various ports around the world. While this may be lessened in some jurisdictions, especially following the implementation of the Maritime Labour Convention (MLC 2006), the likelihood of full pay is threatened. Hanjin's port agents around the world may also face a loss of income if their agency fees are unpaid.

ALLIANCE PARTNERS

The CKYHE alliance partners of Hanjin may also face logistical problems, if they had relied on Hanjin vessels to provide a service for their own customers (that is, under a “box swapping” arrangement). Similarly, some of those partners (for example, Evergreen) are already refusing to carry Hanjin boxes on their own vessels, which merely adds to the woes of Hanjin customers. However, while many of the boxes may be emblazoned with Hanjin’s color and logo, many are leased by the company, not owned. The box owners will want to claim back their property if Hanjin fails to pay the required lease amounts.

The various companies that supply to Hanjin-operated vessels, such as oil (bunker) providers and food and equipment suppliers could face challenges and financial loss as a result of this insolvency.

CARGO OWNERS

The cargo owners entrusted to the care of Hanjin or other service providers who have loaded onto, or were near to loading onto, a Hanjin vessel, are perhaps most at risk of a financial loss following the shipping company’s failure.

OTHER CONSIDERATIONS – SUPPLY CHAIN INTERRUPTION AND DELAY

From what has already been detailed, it is clear that end users of goods or components could suffer delay or a loss of supplies. In either case, the disruption could be significant and have knock-on effects as facilities become clogged and competition for alternative capacity intensifies. The potential disruption should be evaluated and planning put in place prior to the full effects being felt.

INSURANCE COVERAGE ISSUES

Unsurprisingly, there is now considerable concern throughout the industry as to whether or not companies are insured against this scenario, and certainly whether additionally incurred forwarding costs are covered. Unfortunately, there is no simple answer that fits all cases, as marine cargo insurance policies are written on a wide variety of terms and conditions, for which there are going to be very different answers on a “case-by-case” basis. Many policies have additional conditions imposed by insurers beyond those laid down in the standard market “Institute” sets of clauses.

Attention has been drawn to one particular exclusion commonly found in marine cargo insurance policies, namely the “Insolvency of Carrier exclusion” (Clause 4.6 of the Institute Cargo Clauses A, B, and C).

Despite that exclusion, for cover to continue against the perils otherwise covered under the insurance, the shipper must not have been aware, at the time of loading the goods on the vessel, that the carrier was in such a parlous financial state that could prevent the voyage from taking place.

However, one further concession under the Institute Cargo Clauses in 2009 was for the buyers of goods (presumably under a cost, insurance, and freight (CIF) type of contract of sale, and where the goods have already been loaded on the vessel at the time of purchase) to be exempt from this exclusion. In order to have a valid claim, any loss or damage would need to have been proximately caused by a peril otherwise covered under the terms of the policy. The Institute Cargo Clauses go into further detail in Clause 9, titled Termination of Contract of Carriage, on what

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We expect that the wider ramifications of such an important company failure are only beginning to unfold.

happens if, during the period covered by the contract of carriage (normally from when the goods have been loaded on the vessel), the carrier becomes insolvent.

Clause 12, titled Forwarding Charges, explains how expenses incurred should be handled. However, we must emphasize that the standard Institute clauses are often just the initial basis of insurance cover provided, and numerous amendments, additions, and alterations to the terms and conditions will apply on a case-by-case basis.

For those that are unsure about, or have questions regarding, their coverage, we would advise you to consult your broker at the earliest opportunity.

WHAT RISKS SHOULD BUYERS OF GOODS NOW CONSIDER?

Potential buyers of goods may now find themselves being offered attractive bargains. However, buyers (or consignees) need to exercise considerable care when being offered goods that are already on ships (commonly under CIF type of contracts), as they may, unwittingly, be buying into this problem, if those goods are actually being carried on Hanjin-operated vessels. Before purchasing such goods, careful examination of the bill of lading (BoL) is strongly advised to see who the carrier is, in addition to scrutiny of the terms of the insurance that is offered to cover the goods on the vessel under

such CIF contracts, by the seller. It should be noted that insurance cover deemed to be “adequate” in the mind of the seller, may not be so for the buyer.

WHAT NEXT?

Over the past few days, there have been reports of financial injections into Hanjin Shipping to save the company. While this may happen, there is the strong possibility that, despite all efforts, the company will still fall into bankruptcy. In addition to the survival issues for Hanjin, there is no “one-size-fits-all” answer to the numerous insurance questions arising from this turn of events from cargo interests and others. Marsh will continue to monitor the situation and will look to assist clients on various insurance matters arising as this develops.

FOR MORE INFORMATION PLEASE CONTACT YOUR LOCAL MARSH REPRESENTATIVE OR:

MARCUS BAKER

+44 (0)20 7357 1780
marcus.baker@marsh.com

STEVE HARRIS

+44 (0)1603 207 324
stephen.j.harris@marsh.com

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