

## **Attachment 2) Abatement FAQ**

### **Q1 What is abatement?**

Abatement is a principle of mutual insurance where a member who has sustained a particularly large and unexpected claim will not have the full extent of that claim taken into account at renewal. Instead, such large and unexpected claims will fall into the “abatement layer” and will be treated as a mutual exposure, with all members contributing.

The new system will make Members’ contributions to claims in the abatement layer more transparent, allowing the Membership easier identification of the costs involved. This will ensure that each Member of the Club will have a clear and easy to understand breakdown of the costs allocated to them. The system will not impose any new burden on the members.

### **Q2 Why is Abatement being introduced?**

Abatement is being introduced as part of a process to bring more transparency to Members. Also part of this process is that the Club will use net loss ratio as a more comprehensive insurance risk index. Net loss ratio has been used by many Clubs in the International Group of P&I Clubs (IG) in recent years. Introducing the net loss ratio and Abatement together will clarify not only the claims trend of individual Members but their contributions to large and unpredictable claims and to the expenses necessarily involved in Club management as well.

The additional advantage of sharing the risk by Abatement is mitigating a sudden deterioration in the loss record of a Member who has sustained a large loss, so that he does not suffer sudden fluctuations in insurance premiums caused by the accident.

### **Q3 What claims are covered by Abatement?**

Abatement applies to the claims involving vessels covered by ocean-going vessel insurance contracts with no limit for claims payment amount (Mutual). There is no limitation on the number of accidents covered by Abatement per policy year, either for the Club as a whole or individual Members. However, Abatement is NOT applicable to the claims such as FD&D, Charter’s Liability Insurance and Naiko Class vessel insurance, ie claims not related to mutual entries / ocean-going vessels insurance.

### **Q4 How does Abatement work?**

All Mutual entry / ocean-going vessels insurance claims from US\$3 million (net of the individual Member’s deductible) per incident up to the Club retention (US\$10 million for 2021) for the policy year the incident occurs will fall into the Abatement Layer and be allocated across all entered vessels.

**Example 1:** Member A has claims totaling (claims paid and payable) US\$7.5million (net of deductible) within a policy year. (The Club retention of IG pool is US\$10 million for the year.)

- Firstly, US\$3 million under the lower limit of Abatement Layer is recorded as a claims payment on the A's loss record.
- The Abatement Layer will apply to the remaining US\$4.5 million.
- US\$3 million of the total claims payment of US\$7.5million is recorded as a claims payment to A on A's loss record, and the remaining US\$4.5 million will be allocated to all entered vessels as Abatement Cost.

**Example 2:** Member B has claims totaling (claims paid and payable) US\$15million (net of deductible) within a policy year. (The Club retention of IG pool is US\$10 million for the year.)

- Firstly, US\$3 million under the lower limit of Abatement Layer is recorded as a claims payment to B on B's loss record.
- The Abatement Layer will apply to the claims payment of US\$7 million above the lower limit of the Abatement Layer and under the Club retention of US\$10 million, and the US\$7 million will be added to the Club's collective Abatement Pool.
- US\$3 million of the total claims payment of US\$15million is recorded on the B's loss record of the year, and US\$7 million is allocated to all entered vessels as the Abatement Cost.
- Part of the US\$5 million covered by the IG pool is indirectly allocated to all entered vessels as the IG pool contribution, not as a claims payment on the B's loss record.

#### **Q05 How will Members contribute to the Abatement Cost incurred by the Club as a whole?**

The Club will base calculation of the Abatement Cost to be contributed to by Members on the paid and payable claims of the completed policy year. For the ongoing year, the average figure for the previous 5 years will provisionally be used, and will be renewed based on the actual figure in subsequent years. 50% of the Abatement Cost will be allocated to all entered vessels based on premiums and tonnage using the apportionment calculation, and will be contributed by the Members.

**Example:** The total Abatement Cost incurred by the Members is US\$20 million in a policy year. The total average entered tonnage of the Club's ocean-going vessels (Mutual) is 100 million GT, and the total premium is US\$150 million. The total average entered tonnage of a Club Member B's ocean-going vessel fleet (Mutual) in the policy year is 200,000 GT and the premium paid is US\$120,000 in total.

The Abatement Cost to Member B is calculated as follows;

- Allocation based on entered tonnage:  $\text{US\$20 million} \times 1/2 \div 100 \text{ million GT} \times 200,000\text{GT} = \text{US\$20,000}$
- Contribution towards premium payments:  $\text{US\$20 million} \times 1/2 \div \text{US\$ 150 million} \times \text{US\$120,000} = \text{US\$8,000}$
- Total contribution:  $\text{US\$28,000} (\text{US\$20,000} + \text{US\$8,000})$