

# CIRCULAR

To the Members

## Revisions of the Insurance Loss Record Index for Ocean-going Vessels

We are notifying you of the revisions to the insurance loss record index for ocean-going vessels that will take effect from the policy year 2022. The purpose of these revisions is to provide more clarity and transparency for our Members, to assist them in achieving a more comparative Loss Record.

The index has been used for the loss records mentioned below (in No 3) in the Club's basic policy for underwriting ocean-going vessels insurance.

1. The Club must underwrite fair, disciplined, and consistent insurance in order to provide Members with sustainable insurance services.
2. Based on the spirit of mutual insurance, Members must share appropriately the insurance claims payments for the entered ships, reinsurance premiums, and expenses required for the management of the Club.
3. The insurance premium for an individual Member must be calculated according to the Member's loss record, which is based on accidents the Member has had in the past, and other factors including deductible amount, reinsurance premium and ship type, to be commensurate with the underwriting risk of the entered ship.
4. Prior to signing a new contract, the Club must make certain that the Member meets the appropriate safety and risk standards for ship operation.

Please take note of the following revisions that will take effect from the beginning of policy year 2022.

### 1. New Loss Record Index

The Club will no longer use the gross loss ratio as an index for calculating the insurance risk of each Member. Although this index shows the claims trend of individual Members, it does not indicate the direct and indirect costs of underwriting and therefore does not indicate the net loss record including the costs.

Instead of the gross loss ratio, the Club will use the net loss ratio as a loss record index. Net loss ratio is used by many of the Clubs in the International Group of P&I Clubs (IG) as it is a more comprehensive risk index. Net loss ratio provides a clearer picture not only of the claims trend of individual Members but of the contribution they should make towards the expenses needed for the management of the Club.

The net loss ratio for a policy year is calculated by the formula below.

$$\text{The net loss ratio} = \frac{(\text{Claims payment} + \text{IG reinsurance premium} + \text{IG pool contribution} + \text{contribution for Abatement})}{\text{Net premium (annual basis)}}$$

(For reference: Previous index) Gross loss ratio =  $\frac{\text{Claims payment}}{\text{Net premium (annual basis)}}$

**Net premium:** Premium paid to the Club during the policy year. Brokerage fee is not included. The figure reflects lay-up refunds, cancellation refunds and changes in the insurance premium amount.

**Claims payment:** Any claims payment covered by Abatement (see "2. Introduction of Abatement" below) and exceeding the Club retention (US\$10 million in the policy year 2021) will be deducted from the total claims payments (paid and payable.)

**IG reinsurance premium:** The IG pool/reinsurance system to prepare for large and unpredictable accidents. All IG Clubs contribute to and share in the payment of claims in the Pool, which is structured in three layers for losses from US\$10 million to US\$100 million. The IG also arranges the reinsurance in the commercial market for claims between US\$100 million and a certain upper limit (US\$3.1 billion in the policy year 2021). See the diagram on our corporate website (<https://www.piclub.or.jp/en/about/ig>).

Current IG reinsurance premium rates allocated according to ship type are shown on the IG's website (<https://www.igpandi.org/article/international-group-pooling-and-gxl-reinsurance-contract-structure-2021-have-now-been-finalised>). All Members contribute to the premium.

**IG pool contributions:** All IG Clubs contribute to the Pool. In order to level the fluctuations in the IG pool contributions paid annually by Members, the Club calculates the contributions due for the year by a 5-year moving average method, using the payments record in the past year. 50% of each calculated amount is allocated to all ocean-going entered ships based on their premiums and entered tonnage. For the ongoing year, the figure of the most recent policy year completed will provisionally be used, and it will be replaced by the actual figure in the subsequent years.

**Abatement Contribution:** See "2. Introduction of Abatement" below.

As for the new loss record based on net loss ratio, see [Attachment 1. New Loss Record Format, and Terms, Definition and Formulas].

## 2. Introduction of Abatement

The Club will introduce a risk sharing system called Abatement as a formal operational rule. In this Abatement system, all Members of the Club will share and contribute towards the insurance claims payments in the Abatement Layer, which is an amount set within the Club for large and unpredictable losses. This system is based on a principle of mutual insurance. While Members have already been contributing towards the payment of large and unpredictable accidents, the Club is making these contributions more transparent.

The advantage of sharing a risk by Abatement is the mitigation of a sudden deterioration in the loss record of an individual Member who sustains a larger than normal loss, as well as avoiding sudden fluctuations in premiums.

All claims payments in excess of US\$3 million per incident (net of the individual Member's deductible) up to the Club retention (currently US\$10 million) for the policy year when the incident occurred will be covered by the Abatement Layer and allocated to all Members of the Club. (The amount allocated is called the Abatement Cost.)

The Club will calculate the Abatement Cost to be contributed by individual Members based on the paid and payable claims for the completed policy year. 50% of the Abatement Cost will be allocated to all fleets using an apportionment calculation based on insurance premium and tonnage. For the ongoing year, the average figure of the previous 5 years will be provisionally used, and will be replaced by the actual figure in subsequent years.

See [Attachment 2. Abatement FAQ] for details of the Abatement system.

### **3. Period covered by Loss Record**

A loss record was previously covering the total of 5.5 years including the 5 policy years most recently completed and a half year of the year. A loss record will now cover the 6 years most recently completed, and the record of the year is indicated separately. If there is a major change in the loss record in the year, it will be taken into consideration.

Yours faithfully,

**The Japan Ship Owners' Mutual Protection & Indemnity Association**

Attachment: 1. New Loss Record Format, and Terms, Definitions and Formulas  
2. Abatement FAQ

**Attachment 1) New Loss Record Format, and Terms, Definitions and Formulas**

#	Policy Year	2015	2016	2017	2018	2019	2020	Sub-Total	2021	Total
a	Pro Rata Number of ships	3	3	3	3	3	3	18	4	22
b	Pro Rata Tonnage	39,654	33,698	36,913	39,395	32,418	39,543	221,621	49,903	271,524
c	Advance Call	305,750	273,305	288,215	268,938	417,573	419,077	1,972,858	293,354	2,266,212
d	Supplementary Call	122,300	109,322	115,286	107,575	167,029	167,631	789,143	0	789,143
e	Release Call	0	0	0	0	0	0	0	0	0
f	Returns	0	0	0	0	0	0	0	0	0
g	Net Premium (c+d+e+f)	428,050	382,627	403,501	376,513	584,602	586,708	2,762,001	293,354	3,055,355
h	Paid Claims	60,741	84,146	117,589	1,500,000	145,285	13,620	1,921,381	5,334	1,926,715
i	Estimated Claims	0	0	0	0	0	55,000	55,000	11,500	66,500
j	Total Claims	60,741	84,146	117,589	1,500,000	145,285	68,620	1,976,381	16,834	1,993,215
k	Gross Loss Ratio (j /g)	14.2%	22.0%	29.1%	398.4%	24.9%	11.7%	71.6%	5.7%	65.2%
l	Pool & IG Reinsurance Recoveries	0	0	0	0	0	0	0	0	0
m	Total Claims net of Pool & IG Reinsurance Recoveries	60,741	84,146	117,589	1,500,000	145,285	68,620	1,976,381	16,834	1,993,215
n	Group R/I Costs	25,407	19,901	18,619	17,870	13,635	16,340	111,772	15,195	126,967
o	IG Pool Costs	19,154	23,545	16,690	20,676	31,308	27,468	138,841	31,600	170,441
p	Total (m+n+o)	105,302	127,592	152,898	1,538,546	190,228	112,428	2,226,994	63,629	2,290,623
q	Loss Ratio (p/g)	24.6%	33.3%	37.9%	408.6%	32.5%	19.2%	80.6%	21.7%	75.0%
r	Abated Claims	0	0	0	0	0	0	0	0	0
s	Total Claims net of Pool Recoveries & Abatement	60,741	84,146	117,589	1,500,000	145,285	68,620	1,976,381	16,834	1,993,215
t	Abatement Costs	27,770	38,642	8,440	18,802	39,228	20,598	153,480	21,034	174,514
u	Total (s+n+o+t)	133,072	166,234	161,338	1,557,348	229,456	133,026	2,380,474	84,663	2,465,137
v	Net Loss Ratio (u/g)	31.1%	43.4%	40.0%	413.6%	39.2%	22.7%	86.2%	28.9%	80.7%

**Terms, Definitions and Formulas**

Terms, Definitions and Formulas	
#	Policy Year covers the most recently completed six policy years, and the ongoing year is displayed separately for reference.
a	Average number of entered ships in the policy year (The figure is proportionate for the period less than 12 months)
b	Average gross tonnage of entered ships in the policy year (The figure is proportionate for the period less than 12 months)
c	Advance Call paid to the Club during the policy year.
d	Supplementary Call paid to the Club during the policy year.
e	Release Call paid to the Club during the policy year.
f	Premium refunded to the members during the policy year.
g	Premium (ETC) paid to the Club during the policy year. Brokerage fees and taxes are NOT included. Reduction in premiums and lay-up refund are NOT included, either.
h	Total claims paid in the policy year
i	Estimated amount payable for the claims already notified to the Club
j	h + i
k	Loss record calculated by GROSS loss ratio, for reference. (j+g) (See Note 1)
l	Insurance claims paid by IG as a pool claims payment for the accidents occurred in the policy year
m	j + l
n	IG reinsurance costs by ship type for the entered ships in the policy year.
o	IG pool contributions for the policy year. The figure of the most recently completed year is provisionally used for the ongoing year, and it will be replaced by the actual figure after the year ended.
p	m+n+o
q	Net loss record excluding abatement cost (p+g) (Note 2)
r	Claims payment covered by abatement if abatement applies to an individual Member's claim during the policy year.
s	m+r
t	Abatement costs to be contributed by the Members in the policy year. The average figure of the most recent five policy years completed is provisionally used for the ongoing year, and it will be replaced by the actual figure after the year ended.
u	s+n+o+t
v	This is the final loss record reflecting the abatement cost. (u+g) (Note 3)

$$\text{(Note 1) (k) Gross Loss Ratio} = \frac{\text{Claims Payment}}{\text{Net Premium(annual basis)}}$$

$$\text{(Note 2) (q) Loss Ratio} = \frac{\text{Claims Payment} + \text{IG reinsurance costs} + \text{IG pool contributions}}{\text{Net Premium(annual basis)}}$$

$$\text{(Note 3) (v) Net Loss Ratio} = \frac{\text{Claims Payment} + \text{IG reinsurance costs} + \text{IG pool contributions} + \text{abatement costs}}{\text{Net Premium(annual basis)}}$$

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