



## FREIGHT FORWARDERS RISK

### A GROWING AND EVOLVING MARKET SEGMENT

#### CONTACT

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#### ABOUT THE AUTHOR

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Many businesses depend on the daily export and import of goods. International shipping can increase the profitability of a business, whether through access to more consumers or the opportunity to purchase goods or raw materials at a lower cost. However, regulations, paperwork, manpower and other factors concerning international trading may be intimidating, and most businesses are not equipped to deal with the intricate logistics of such a task. Businesses can solve this problem by contracting with freight forwarders, who manage the shipments, as well as the hassles associated with the shipping process.

#### SERVICES PROVIDED BY A FREIGHT FORWARDER

Freight forwarders act on behalf of importers, exporters and other freight forwarders to arrange the safe, efficient and cost-effective transportation of goods. Freight forwarders perform a complicated – and ever-evolving – array of services. From an insurance perspective, coverage needs can vary based on the services provided by each freight forwarder and the associated exposure.

Basic services provided by freight forwarders include but are not limited to:

- Quoting and securing freight costs for shippers
- Booking shipments with common carriers
- Preparing all documentation required for export/import
- Using their own trucks or arranging third-party trucks for domestic and foreign inland transit
- Providing “All Risk” coverage to their clients through their insurer for transit and warehousing
- Handling logistics for efficient international trade and resource allocation

Extended (and now common) services include:

- **Customs Brokerage:** Services provided, mostly to importers, include clearing goods through customs, as well as calculating taxes and duties, completing necessary paperwork, communicating with government authorities, and arranging inland transit to the final destination.
- **Non-Vessel Operating Common Carrier (NVOCC):** In the past, there was a distinction between a NVOCC and a freight forwarder, but today, freight forwarders often play the role of a NVOCC (a license is required). In doing so, the freight forwarder will provide a House Bill of Lading to the client and coordinate the efficient and cost-effective transport of the consignor’s goods directly with the ocean and inland carriers. In this role, freight forwarders expose themselves to liabilities carried by common carriers (as well as positive limitations). The freight forwarder becomes the carrier to the shipper and the shipper to the carrier.
- **Indirect Air Carrier:** Some freight forwarders will offer services for international trade via air by providing an Air Waybill and arranging the transportation accordingly with common air carriers.
- **Consolidation:** Freight forwarders receive goods for transport from many clients to many destinations. When there are not enough goods to fill a container, it is a common practice to consolidate merchandise with those of others into one container, especially when the goods are sharing a destination.

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- **Warehousing:** Freight forwarders are expanding their services by providing their clients with storage in owned or leased warehouses or by brokering or negotiating storage in third-party facilities.
- **Distribution Services:** In many cases, shippers work at a very fast pace and deliver goods directly to their client. They contract with freight forwarders to develop their distribution lines and arrange for all goods to be delivered on a door-to-door basis. This operation calls for the freight forwarder to retain custody of the goods (directly or not) for an extended period of time, thus increasing the risk of a loss for which they may be liable.

## RISKS AND EXPOSURE

Accurate analysis of an individual freight forwarder's exposure depends on the services it provides and historical losses. Instead of a Named Perils Covered Policy, Freight Forwarders Legal Liability is a Named **Services** Covered Policy. A freight forwarder arranges all transportation, and even if it is not directly executing the carriage, it can be dragged into a legal dispute if the goods are lost or damaged during transit.

Determining the scope of a freight forwarder's liability in a claim is not an easy task. When goods are damaged in transit and there is no All Risk Cargo Policy or the shipper does not want to file a claim, the shipper will try to recover from all parties involved in the carriage of their goods. There are instances when numerous entities are in possession of goods during transit, including ocean, inland and air carriers, warehousemen and the freight forwarder.

In most cases, ocean, inland and air carriers are protected by conventions which limit their liability to a certain amount of money per package or weight. For example, ocean carriers include in the wording of their Bills of Lading that their liability is limited in accordance with the Carriage of Goods by Sea Act (COGSA) to \$500 per unit. Regarding cargo by air, there are acts like the Warsaw Convention, later amended by the Montreal Convention, stating the liability of the carrier and compensation is based upon the weight of cargo.

In the case where there is an All Risk policy and the insured is covered, the shipper will not hesitate to subrogate if the legal fees are in line with possible recovery. The amount recovered from the carrier may not be enough to cover the losses of the shipper, resulting in the shipper going after the outstanding parties.

## COVERAGES TO ADDRESS FREIGHT FORWARDER'S EXPOSURE

The liability of a freight forwarder is determined by the roles it plays. These roles will determine the scope of coverage and the forms required on the freight forwarder's insurance policy.

Potential roles of freight forwarders include:

- **Carrier/Principal:** If the freight forwarder issues a House Bill of Lading (or Air Waybill) in which it is described as the carrier, then it will act as Principal and the laws, regulations and limitations of a carrier shall apply.
- **Broker/Agent:** If the freight forwarder issues a House Bill of Lading (if any) in which the stated carrier is the common carrier (not the freight forwarder), then the freight forwarder will act as a broker or agent and is usually, but not always, exempt from legal liability.

Freight Forwarders Legal Liability and Carriers Legal Liability policies require the insured to be legally or contractually liable in order to cover both legal representation and losses resulting from court determination of the freight forwarder's legal responsibility. Contractually liable does not mean unfulfillment of contract; rather, it means that the contract states the freight forwarder's liability in case of a loss. These two issues are commonly confused, resulting in the inclusion of Errors & Omissions coverage to fill the gap.

The most common transportation-related liabilities required by freight forwarders, depending on their services, are Carrier Legal Liability and Freight Forwarders Errors & Omissions (E&O).

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Carriers Legal Liability encompasses:

- **Non-Vessel Operating Common Carrier (NVOCC) Legal Liability:** When the freight forwarder issues a Bill of Lading stating that it is the carrier, this coverage provides Legal Liability against loss or damages to such goods and/or merchandise as stated therein, as determined by laws applicable to a common ocean carrier.
- **Indirect Air Carrier Legal Liability:** When the freight forwarder issues an Air Waybill for air shipments stating that it is the carrier, this coverage provides Legal Liability against loss or damages to such goods and/or merchandise as stated therein, as determined by laws applicable to a common air carrier.
- **Motor Truck Cargo Legal Liability (including contingent):** When the freight forwarder issues a Bill of Lading for overland shipments stating that it is the carrier, this coverage provides Legal Liability against loss or damages to such goods and/or merchandise as stated therein, as determined by laws applicable to a Motor Truck Carrier, regardless of whether the insured owns the trucks.
- **Warehouse Legal Liability:** When the freight forwarder accepts goods for warehousing/storage under its own warehouse receipt, this coverage provides Legal Liability against loss or damages to such goods and/or merchandise as stated therein, as determined by laws applicable, whether the insured owns or leases the warehouses.

Freight Forwarders E&O covers the insured's Legal Liability arising out of the breach of any obligation, negligent act, error or omission, including but not limited to incorrect instructions, faulty arrangements or clerical errors of any officer, director or employee of the insured. Coverage extends to whenever or wherever the act was committed or alleged to have been committed within the performance of the insured's business or by others on behalf of the insured in their professional capacity as shipping/forwarding agents, custom house or freight brokers.

All Risk coverages available to freight forwarders include:

- **Shippers Interest:** Coverage that provides the freight forwarder with the capacity to insure goods while on ocean or overland transit on an "All Risk" basis on behalf of their clients, without the need to underwrite each individual case.
- **Warehouse Third-Party:** Warehouse coverage is provided by the freight forwarder to the shipper, who reports and pays the premium to the insurer (at agreed rates) in the same way that it does for Shippers Interest Ocean Cargo/Inland Transit. When a forwarder offers cargo insurance on an "All Risk" policy, they will be required to insure goods under these terms and conditions while in storage.

## CONCLUSION

The amount of freight forwarders operating in the United States has doubled in the past 10 years, and their risk will soon make up a large portion of the transportation insurance market's total premium. In addition, the functions of freight forwarders are evolving to encompass more services. As the role of freight forwarders around the world continues to develop, they are subsequently generating new risks. From an underwriting perspective, the necessity of "fast pace" adaptation and innovative solutions without compromising service and integrity to the insured will continue to be the key differentiator in this market segment.

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