

By Joseph S. Harrington, CPCU

INLAND MARINE INSURANCE

*What are the “nonfiled” classes,
and why are they being filed?*

Have you ever encountered a topic of conversation that you are familiar with but don't really understand—and are embarrassed to ask what it really means?

For property/casualty generalists, “inland marine insurance” may be one of those topics.

Inland marine insurance accounts for only about 2% of property/casualty premium in the United States, but is worthy of attention because it accounts for a larger share of industry profit.

According to figures from A.M. Best Co., inland marine insurance had a combined ratio of 97.5% from 1991-2000, compared to 105.2% for personal lines and 109.9% for commercial lines as a whole over the same period.

It's understandable if most property/casualty professionals don't know that, or if they have only the haziest notion of what inland marine insurance is. The “line” is really a series of small lines, called “classes,” with unique characteristics that defy any attempts to establish an easy definition of inland marine insurance as a whole.

Although classified as property insurance, some of the most important inland marine classes provide only liability coverage. Although generally understood to be providing coverage for goods in transit and projects under construction, inland marine insurance includes coverage for some of the largest completed structures in the world.

Filing “nonfiled” classes

Now, a new level of complexity has been added to inland marine: A national advisory organization has begun filing policy forms for many of the traditionally “nonfiled” classes in nearly half the states. Starting in January of this year, the American Association of Insurance Services (AAIS) has filed policy forms provided in its Inland Marine Guide in 23 jurisdictions that have filing requirements for the “nonfiled” classes.

The Guide has long been a standard industry resource for the nonfiled classes. Until now, companies have had to make form filings in certain states on their own, and AAIS

The definition of inland marine insurance, such as it is, rests heavily on perceptions of common practice. To an extent, what inland marine is depends on what its practitioners do.



was required to file some information in selected cases, but there was no systematic filing action.

As befits inland marine insurance, AAIS has established this initiative with conflicting emotions. The decision to initiate a general filing comes in response to direct requests for such action by compliance specialists at AAIS-affiliated companies, and by regulators who no longer want to review multiple company filings of essentially the same forms. Yet the filing action comes after years of resistance to the idea by AAIS and others.

Inland marine specialists have long sought to preserve the unregulated status of coverage for risks they consider too unique to be addressed adequately by filed rates and forms. That is still the official position of AAIS, as well as the Inland Marine Underwriters Association. In support of that position, AAIS is limiting its filing action to only those classes and states where there are explicit filing requirements.

The choice not to initiate a general countrywide filing is conscious and critical. The definition of inland marine insurance, such as it is, rests heavily on perceptions of common practice. To an extent, what inland marine *is* depends on what its practitioners *do*. As this article will explain, certain classes of inland marine are considered “traditionally not subject to filing requirements” by customary practice.

As the successor organization to the former Transportation Insurance Rating Bureau, AAIS has long been a leading organization in inland marine insurance. Its Inland Marine Guide has long been the standard source for forms, rating procedures, underwriting guidelines, and other resources for the nonfiled classes.

The question arises: If AAIS were to file its Guide forms countrywide, would they become “filed” classes by virtue of that step? To avoid such an interpretation, AAIS filed only those forms for those classes required by individual states; some forms were filed in some states but not others.

Still, the AAIS filing action is a milestone in the evolution of inland marine insurance, and a primer on the evolution and current status of the line will be helpful to compliance, marketing, underwriting, and claims professionals who are not inland marine specialists, but find themselves dealing more and more with the line.

Contradictions from the start

To some people, the very phrase “inland marine” is a contradiction in

terms. To literalists, something is either “inland” or it’s “marine” (i.e., waterborne).

The term “inland marine” technically applies to transportation on the nation’s inland waterways (lakes, rivers, and canals), but by the turn of the 20th century, “inland marine” had come to signify insurance for property transported by land.

Today, most waterborne cargo is insured as “ocean” or “wet” marine, which has its own standards of liability, policy forms, and underwriting criteria. Cargo transported by land is typically insured as inland or “dry” marine.

Because of regulatory strictures on “fire” policies in the early 20th century, inland marine insurance expanded rapidly to cover a range of exposures unrelated to transportation, including property at fixed locations. This happened because marine carriers were allowed to write “all-risk” policies that were less regulated than standard fire contracts.

Protests from fire insurers brought about the “Nationwide Marine Definition” in 1933, a definitive statement of the types of property that marine carriers could insure. These were:

- Imports and exports
- Domestic shipments
- Instrumentalities of transportation and communication (bridges, tunnels, transmission towers, and more)
- Specified types of property owned by individuals (jewelry, furs, musical instruments, and more)
- Specified types of property related to a business or occupation (mobile equipment, property under bailment, electronic data processing, and more)

Last modified in 1976, the Nationwide Definition continues to be the principal delineation of inland marine insurance. It has, however, lost its force as a restriction on underwriting authority as the separation between fire, marine, casualty, and surety writers has become blurred.

The Nationwide Definition in effect codified one of the apparent contradictions in inland marine insurance: the inclusion of three important types of liability coverage—bailee, motor truck cargo, and warehouse liability—as inland marine property coverage.

Bailees (such as dry cleaners), motor carriers, and warehouse operators are all in the business of taking custody of the property of others for a limited time. Because the property is outside the control of its

owners, they cannot, as a practical matter, safeguard it from loss or determine whether negligence on the part of the bailee or motor carrier contributed to a loss.

Given that, common law has come to hold bailees strictly liable for loss or damage to the property of others they hold. A similar standard of liability exists for cargo carriers (ocean and motor) and warehouse operators, with certain exceptions.

In essence, bailees, motor carriers, and warehouse operators are bound to safeguard the property of others as if it were their own. Thus, the insurance for such exposures is, for all practical purposes, written as first-party property coverage, with coverage grants, exclusions, and limitations that address property perils rather than negligence.

Unique and changing risks

We must go beyond the Nationwide Definition to arrive at a working understanding of how inland marine insurance contrasts with other property/casualty lines.

For practical purposes in today’s market, inland marine insurance involves coverage for risks that are unique in nature and change frequently. To illustrate, compare inland marine insurance with multi-peril commercial property insurance, the modern-day version of the old “fire” policies.

Standard commercial property policies are written to insure buildings and personal property that are in the same location and essentially same condition over time. A frame structure in an unprotected area with high windstorm exposure remains in that condition day after day. Underwriters should watch for changes in the amount and type of personal property, but the risk exposure remains essentially the same over time.

Inland marine insurance addresses risks for which change is constant. This is clearly seen in the inland marine construction classes—builders risk, contractor’s equipment, and installation floaters—which account for the most premium volume in the line.

A backhoe operating on dry, flat ground one day could be operating on a slippery slope the next. A building under construction is in a different stage of completion at the conclusion of a day’s work than when work started in the morning.

The same character of change applies to other classes of inland

marine insurance, such as accounts receivable and electronic data processing, two forms of intangible coverage that are constantly in flux.

Given all that, it would seem to be a contradiction to include bridges, tunnels, and transmission towers as inland marine risks. They are, after all, large, inert risks that hardly change at all. Yet, as “instrumentalities of transportation and communication,” they are covered by inland marine policies.

Other classes of inland marine insurance provide coverage for valuable personal and commercial property—such as jewelry, furs, tools, and more—that moves about easily, or “floats.” Hence, they are insured by inland marine policies known as “floaters” that typically provide broader coverage than is offered in standard homeowners or commercial property forms, with unregulated rates.

Filed and nonfiled

In addition to the distinction between commercial and personal inland marine classes, there is an added distinction between filed and nonfiled classes. Historically, the distinction arose from market conditions.

Over time, marine insurers were expected to file inland marine forms and rating plans for any classes that encompassed a large number of homogeneous risks for which standardized forms and rating information could be developed.

Among personal inland marine risks, the filed classes include: bicycles, furs, personal effects, cameras, golfers’ equipment, personal property, coin collections, jewelry, silverware, fine arts, musical instruments, and stamp collections.

Among commercial inland marine risks, the filed classes include: accounts receivable, camera and musical instrument dealers, floor plan merchandise, implement dealers, jewelry dealers, musical instruments, negative film, photo equipment, physicians’ and dentists’ equipment, signs, and theatrical property.

The “nonfiled” inland marine classes encompassed those risks deemed too diverse or too subject to change to be adequately addressed through filed forms and rating plans. As long provided in the AAIS Inland Marine Guide, the nonfiled classes encompass a range of classes addressing cargo, construction, electronic data processing, farm, and other risks.

More often than not, the nonfiled status of a class rested on customary

treatment rather than an explicit law or regulation. It is unclear why more and more regulators have, in effect, imposed filing requirements on the nonfiled classes in the past 10 years or so.

In AAIS’s view, there has been no apparent change in the nature of nonfiled risks to make them any more suitable for the strictures of rate and form regulation than previously. Nor has there been much evidence of affirmative decisions by legislatures or insurance commissioners to impose filing requirements on previously nonfiled classes.

Instead, the growth of filing requirements on “nonfiled” classes appears to have arisen from a series of small decisions and interpretations by people within insurance departments. Regulatory staffers appear to be more inclined to believe that all forms and/or rating information must be filed unless explicitly exempted. This mindset has grown even in an era when complete deregulation of commercial insurance is openly discussed.

One can only speculate as to the reason why. It is true that, at a time when state budgets are under intense pressure, there is a financial incentive for insurance departments to require more filings, which generate fee income. There is no definitive evidence demonstrating such a cause and effect, however.

Another explanation may lie in the growing specialization and professionalization of insurance regulation. Like most professionals, insurance regulators have the technology and training to be more productive than their predecessors, and they may feel it their duty to regulate insurance lines unless explicitly directed not to.

Whatever the reasons, the introduction of filing requirements for “nonfiled” classes adds one more layer of complexity to a line already rife with contradictions.

Property/casualty professionals would be well advised not to let confusion about what “inland marine” is keep them from learning about classes of coverage that can improve the margins on their personal and commercial accounts. ■

The author

Joseph S. Harrington, CPCU, is director of Corporate Communications for the American Association of Insurance Services. He can be reached at joeh@aaionline.com