

Understanding General Average





A great deal can occur during a cargo vessel's voyage, whether on the open sea or passing through straits and coastal areas. An unexpected storm, hidden sandbar, or sudden fire are all obstacles that a cargo ship can encounter without warning. To survive these perils and resume the voyage can take extraordinary efforts by those on board, as well as those that are called in to assist. Parties involved must act quickly and make split-second decisions to save the ship, crew, and cargo aboard. These efforts can often come at a cost. Aside from the cost of lost goods, there are expenses involved in saving the voyage. This is where the concept of General Average comes into play.

What is General Average?

General Average is a principle of maritime law that dates back to the beginning of the first century. It is defined as "a loss that arises from the voluntary sacrifice of part of a ship or cargo to save the residue of the ship or cargo or from extraordinary expenses incurred in protecting the interests involved under pressure of a common risk, and that is shared proportionally by all parties concerned."*

In other words, when a cargo ship encounters trouble and requires extraordinary rescue efforts, the vessel's cargo owners will pay their share of the expenses involved. Shares are based on the value of their goods, as a portion of the total value of the voyage (goods and vessel). If a cargo owner experiences damage to their cargo during the process, then only the percentage of their undamaged cargo is calculated for their share. If a cargo owner experiences a complete loss, then they do not have to participate in the General Average at all, since they no longer have any value on board the vessel (i.e. X % of \$0 = \$0). The expenses of a General Average event typically include the costs associated with rescuing a disabled vessel, such as emergency response, towing, and administrative costs, as well as damages to the vessel itself. If cargo is sacrificed or damaged during the rescue efforts, those losses are also accounted for.

What Happens When a General Average Is Declared?

Once the vessel owner officially declares General Average, a General Average Adjuster is selected to administer the process. The Average Adjuster oversees the process of discharging the vessel while calculating all costs and expenses incurred so that they can be proportionately collected from the cargo owners. A notice is officially given to the cargo owners requesting the following paperwork and security deposit to release their freight:

- **General Average Bond:** This form must be completed by the cargo owner. This states that the cargo owner promises to participate in the General Average process.
- **General Average Guarantee:** This form must be completed by the cargo owner's insurance company and guarantees the payment of the necessary funds. If the cargo owner does not have insurance, then they must place a cash deposit with the Average Adjuster.



What Happens Next?

Once proper documents and securities have been received, freight can be released and the Average Adjuster will begin their General Average calculations to determine each cargo owner's final financial share and remove the balance from their deposit. If the cargo owner's deposit exceeds their proportional cost, then reimbursement is issued. If the deposit was less than the cost, then the cargo owner owes a balance. This process can take several years to complete and without cargo insurance, a cash deposit can be tied up for the entire duration.

Examples of When General Average May Apply

- Example A) A vessel encounters a storm, experiences engine failure, and becomes stranded at sea. To save the vessel, a rescue ship arrives and provides escort to the nearest port of refuge.
- Example B) Fire erupts from a container on a vessel and quickly spreads to other containers and the engine room. The crew quickly acts to extinguish the fire by hosing down the engulfed areas as well as containers in the vicinity. A team of tugs is needed to escort the damaged and disabled vessel to the nearest port for repairs and container discharge.
- Example C) A vessel runs aground on a hidden sandbar while navigating a narrow passage of water. Multiple tugboats are needed to pull and push the vessel, while excavators dig the vessel free.

These scenarios include expenditures to save the voyage and preserve as much of the cargo as possible. The cost of these expenditures, damages, and loss of cargo are proportionately shared among those cargo owners that did not experience a loss.

A General Average event can be overwhelming, especially when your cargo is involved. An effective cargo insurance policy can help get you through the long and tedious process of General Average, and provide adequate financial backing. ECIB is here to help. Our experts have been navigating General Averages for our clients since 1994. To learn more about General Average, or to speak with a cargo insurance expert, reach out to ECIB today by visiting www.ecibglobal.com.