

Status Quo Bias in Ocean Marine Insurance and Implication for Korean Trade

Hongjoo Jung[†]

Business School, Sungkyunkwan University, Republic of Korea

Soyoung Lim[†]

Department of International Trade, Sungkyunkwan University, Republic of Korea

Yoon Lee

Department of International Trade, Sungkyunkwan University, Republic of Korea

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Abstract

Purpose - This research aims to fill the gap between theory of behavioral insurance, particularly the Status Quo Bias (SQB), and practice of the Ocean Marine Insurance (OMI), based on the OMI statistics, international emails, focused group interviews, and survey methods. The OMI, the oldest and most globalized commercial insurance, had been revised in 1963, 1983, and 2009 since 1912 when the Institute Cargo Clauses(FPA) was first developed in the U.K. The SQB has been academically explored mostly in health insurance or in financial services sector, but never in the OMI area which may properly fit analysis of the bias for several reasons. Thanks to available statistics of the OMI in Korea, we can conduct the SQB research for the first time in its kind.

Design/Methodology - We show existence of the SQB in the OMI of Korea, resorting to Korean statistics between 2009 and 2018, email correspondence with a few country experts (in U.K., Germany, and Japan), focused group interview with Korean OMI underwriters, and an in-depth interview with an underwriter, and group survey to 15 OMI insureds (company representatives).

Findings - The result shows that Korean foreign traders rely on the old type (developed in the year 1963) OMI contracts while the other industrialized countries use the newest OMI contract (developed in 2009). We show with simple loss ratio analysis of the contracts over 2009 - 2018 period that the behavior has little to do with rational profit maximization of insurers, as they seem to forgo some more profitable contracts of new clauses by keeping the old clauses. The consistent addiction to old type contracts in the OMI market reveals strong SQB among Korean exporters, importers, bankers or insurers, which is confirmed by a focused group interview with four underwriters, a following in-depth interview and a survey to fifteen insureds.

Originality/value - This research of truly originality has academic value as it comes up with new findings and significant implications for development of trade practice and policy. First of all, this research is based on actual and aggregate statistics which have never been used in any previous Korean research on the OMI. Second, the research shows that all-risk OMI policies provide more values, in terms of coverage given premium, to insureds than partial coverage policies, different from previous argument in Korea. Third, the research presents strong SQB in Korea where foreign trade has played an innovative and significant role in economic growth. And the bias may be attributable to uninformed traders, informed but dull insurers, or conservative bankers. Forth, in order to further develop foreign trade, there should be policy initiative to review current practices of the OMI contracts and to move forward with new contract forms. All of these findings and arguments are new and critical.

Keywords: Behavioral economics, Institute Cargo Clauses, Ocean Marine Insurance, Status Quo Bias

JEL Classifications: F1 Trade, G2 Financial Institutions and Services, G4 Behavioral Finance

[†]The First Author : jungprokorea@gmail.com, Corresponding author: sylim0131@gmail.com

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1. Introduction

Behavioral economics, finance or insurance assumes bounded rationality or irrationality of human being unlike the neoclassical economics which presumes rationality or rational decision-making of both corporations and consumers (Kunreuther et al., 2013; Richter et al., 2014). For example, neoclassical economics assume that corporation and consumer try to maximize their expected profits and utility respectively in a mathematical way (Mankiw, 2020) while behaviouralists say that there are more than that in people's behaviour such as psychological benefits, convenience, altruism and so on. That is, behavioural economics or finance theorists note several anomalies or bias in terms of economic perspective such as endowment bias, frame bias, anchoring bias, status quo bias, overconfidence, and so on (Thaler, 2008).

Insurance is not an exception in this trend toward behavioural economics. Although neoclassical economics or finance has contributed to development of insurance theory, there have been a lot that could not be explained by the neoclassical theory (e.g. expected utility theory). That is to say, traditional neo-classical insurance theory argues that rational human beings purchase insurance at full coverage at actuarially fair premium given no market failure including information asymmetry (Mossin, 1968). However, behavioral insurance can explain a variety of irrational insurance decisions in purchase, supply or regulation, incorporating human psychology.

This research tries to check existence of the Status Quo Bias (SQB hereafter) on the ocean marine insurance market and explain the reasons of the SQB. The SQB describes an emotional bias, a preference for the current state of affairs, or a phenomenon where people stick to pre-existing situation, being reluctant to switch into another situation, even if it gives more profit or utility to move into a new contract. In case of insurance market, the insured or the insurer may adhere to incumbent supplier, customer, contract, or condition. As explained later in this research, health insurance market or automobile insurance market are the well-known examples to display the SQB (see the literature review part below). Using both qualitative observation and quantitative data, for the first time in this kind, we are examining the SQB in the Ocean Marine insurance (OMI hereafter) market which is highly global and liberalized.

The OMI, in particular cargo insurance, is a commercial line insurance used by international traders to overcome maritime risks. The UK has been serving as a leading country in the OMI in terms of business, law, or transaction. As a hub country of the OMI or even of insurance in general, the UK OMI market accounts for 30% of the world. Interestingly, UK has a written law of the MIA (Marine Insurance Act) 1906, although it used to be a common law country relying on case law rather than statute, which implies that the OMI has been taken special care in the country of insurance.

Nevertheless, the UK has traditionally been treating the MIA from the perspective of the insurer rather than from the shipper (traders), as insurance was a new infant industry to protect at the national level in early twentieth century. For this reason, the MIA 1906 had several provisions favoring insurers such as disclosure or warranty which appeared to restrict insureds' rights so severely as to eventually ending up with its revision in the 21st century in the Consumer Insurance Act 2012¹ and the Insurance Act 2015.

Since the UK was the center where modern OMI originated and developed, many representative OMI contracts or clauses were developed or amended there. The MIA 1906 was based on the existence and interpretation of the Lloyd's S.G Policy Form. In this sense, the OMI Terms and Marine Insurance Act are closely linked to each other. OMI contract has been using several clauses such as S. G policy developed by Lloyds in the 18th century.

¹ Many pointed out that there are still problems in non-consumer insurance contracts such as ocean marine insurance because the legal application is limited to consumer insurance contracts. Therefore, the Insurance Act 2015 of the U.K., which applies to all insurance contracts, including non-consumer insurance contracts, was enacted in 2015 and has come into force since 2016. It strengthened consumer rights through two revisions of the law.

In 1963, the **ICC(old clauses)**, jointly enacted by Lloyds and London Insurance Association, were enacted and the new **ICC(new clauses)**, completely reorganized the old one, were developed in 1983 and now the 2009 **ICC**, partially revised, are supposed to be in use globally.

Previous researches on the OMI in Korea mainly compared and analyzed the pros and cons of the OMI clauses (1963, 1982, and 2009). Most studies did not focus on actual usage, and just assumed the insurer or insured will decide the suitable OMI clauses based on rational calculation for cost and benefit. However, motivated by behavioral economic theories, we found the possibility of irrational choices of IMO clauses, so collected the usage data of the OMI contracts to see the trend of usage of each clause. Based on those data, we could capture the reality of the OMI choice, and examine the existence SQB in the Korean OMI market. Furthermore, we could reveal a clue behind the bias by conducting a little survey to the underwriters and insureds.

2. Literature Review

2.1 Behavioral Bias

Behavioral economics, which combines psychological insights into research on economic issues, affects the analysis of consumer behavior, industry, and overall market, and is widely used in fields such as policy development and management. Consumers respond to external demands with given resources in the decision-making process, and Table 1 shows eight typical behavioral biases.

Table 1. Representative behavioral biases related to finance

	Bias	Definition
1	Endowment Effect / Status Quo Bias	A tendency to stay in a state similar to the current state
2	Loss Aversion	Tend to be more sensitive to losses than gains of the same size
3	Overconfidence	A tendency to be overly optimistic or overestimating outcomes that are favorable or satisfactory for you
4	Mental Accounting	A tendency to implicitly allocate money to psychological accounts according to purpose and to think of money differently for each psychological account
5	Framing	A phenomenon in which conclusions vary with the same information depending on how or by whom the information was provided
6	Anchoring	The tendency to anchor and make decisions around the information that matters most
7	Heuristics	A tendency to use experience-based methods such as guesswork or common sense in the problem-solving process
8	Herding	A tendency to imitate decisions made by other people or members of a similar group to reduce exploration cost and complexity

Source : Thaler (2008)

Though behavioral economics focus more on irrational choice of individual, there have been many researches to apply those theories to firms' decision. Inconsistent with existing studies' interpretations, companies sometimes make decisions, such as sticking to existing methods, that do not suit profit maximization. Langevoort (1997) showed that there are irrational corporate decisions that cannot be explained by Agency Theory, Transaction Cost

Theory, and Stake-holder Theory. Also, Campana (2016) and Heaton (2019) have applied behavioral economics to interpret the causes of a firm's wrong choice as self-deception, overconfidence, endowment effect, or as a result of excessive optimism. Thus, according to previous studies, applying behavioral economics theory to companies' decision-making is possible, in some cases it may provide a meaningful explanation.

When it comes to financial consumers, they can be broadly classified into "general financial consumers" or "specialized financial consumers²", as in the 2021 Financial Consumer Protection Act of Korea. As the protection of financial consumers is an increasing demand and trend at home and abroad these days, so Korea also enacted the Financial Consumer Protection Act, which is scheduled to be implemented in 2021. In general, financial consumer protection aims at consumers of household financial insurance, but some corporate financial insurance also has a lot of asymmetric information between consumers and insurers, as we can see later in this research. Nevertheless, corporate consumers may loosely belong to the specialized financial consumers not protected by law or by regulator as much as general financial consumers who are believed not on an equal footing with business counterparty. As small or medium sized enterprise, foreign traders may need public protection, although not so much as individual consumers, as they are not so well informed as large enterprises.

2.2 Status Quo Bias (SQB)

The SQB describes a phenomenon where the characteristics of the initial situation, rather than those of the available alternatives themselves, influence an individual's choice. That is, it is a tendency that people stick to where they have been, even when there are better options to choose. Samuelson and Zeckhauser (1988) wrote a key paper from which discussion of the status quo bias emerges. They examined numerous economic decision-making processes, such as health insurance and pension planning, and find that investors disproportionately and (economically) inappropriately remain as they are, sticking to the SQ arising from cognitive misperceptions, switching costs, or psychological commitment (Krieger and Felder, 2013). Similar to the endowment effect in some sense, the SQB may be explained by prospect theory's concept of loss aversion (Tversky and Kahneman, 1991), the inertia theory, the decision avoidance theory, or by the incomplete preferences theory (Murwirapachena and Dikgang, 2018).

Much of the financial research that emerges from the SQB focuses on three issues: pension and personal financial planning, health decisions, and insurance decisions as follows. First of all, stock market or mutual fund market, the SQB shows up when positive influence of previous growth on current growth with a large number of funds, but also in smaller segments of the industry. As a matter of fact, the greater the number of alternatives, the more pronounced the status quo bias (Kempf and Ruenzi, 2006). Subjects exhibited a robust status quo bias throughout this experiment that is not consistent with standard economic theory (Brown and Kagel, 2009). The magnitude of the status quo bias depends on the nature of the investment opportunity and certain investor characteristic Status quo bias influences their investment decisions (Freiburg and Grichnik, 2013). Second, in case of health insurance and health affairs, the SQB is shown to exist by that premium elasticities are significantly higher for new hires than for incumbent employees (Strombom et al., 2002). And the SQB plays an important role with elderly group more than younger age groups (Becker and Zweifel, 2008). With more choices serving to inhibit switching of health plans, people with longer periods of attachment to a particular health plan were less likely to express an intention to switch plans(endowment effect (Frank and Lamiraud, 2009). The SQB does play a role in consumer choices over health insurance policies, as the bias is an issue particularly among inexperienced consumers (Krieger and Felder, 2013). Patterns of transitions into Medicare Advantage from Traditional Medicare (and vice versa) suggest significant status quo bias in take-up of Medicare Advantage and that this "stickiness" increases with a beneficiary's tenure in Medicare (Sinaiko et al., 2013) or decreases with the number of membership years (Afendulis et al., 2015), and it differs

According to the law, "Specialized financial consumer" means a financial consumer who has the ability ² to take risks in accordance with a financial product contract in light of his or her expertise in financial products or the size of the owner's assets, and falls under any of the following items:

across countries, for example between the Netherlands and Germany (Leukert-Becker and Zweifel, 2014). Other factors to explain the SQB positively are age or morbidity, as well as education or income in opposite direction (Karl et al., 2019). And there are other area to show the SQB such as water sector (Murwirapachena and Dikgang, 2018).

2.3 OMI (Ocean Marine Insurance)

According to the 2019 IUMI (International Union of Marine Insurance) report, more than two-thirds of the world's cargo is shipped by ocean marine transportation³, and Korea is a country of economic success based on foreign trade, of which the volume ranked 9th in the world as of 2019. Thanks to the OMI, that is to say, Korean trade and economic growth skyrocketed since 1960s, along with growing academic research in the OMI area as follows.

First of all, some research were conducted on the factors to determine choice of contract of the OMI. For example, La, Gong-woo (2005) conducted an empirical study on the factors in which a Korean trading company selects insurance conditions when signing an ocean marine insurance contract, such as insurance premium rate, nature/type of cargo, and transport section) influenced the perils covered, the warranty and the covered loss. And Lee Bong-Sang (2008)'s empirical study on the causes and effects of the choice of OMI revealed that there are differences in the selection of ICC (A), (B) and (C) conditions, depending on the size of the import-export enterprise, the transaction period, the degree of use of information, the degree delegation of authority, the work experience of the person in charge, the level of work knowledge of the person in charge, and the degree of emphasis on transaction cost reduction of the import and export enterprise.

There were a couple of comparative research on contract types within the OMI contracts. Oh, Ji-Yang (2010) stated that the old clauses were abolished in the UK after 1983, and that the new clauses were compulsory in the OMI leading country. Emphasizing advantageous value of ICC(A) contract, compared with ICC (B) or ICC (C), he insisted on a unified use system as ICC (A) with disposal of the other contracts, to the benefit of **insureds** free from burden of proof. However, he did not recognize wide use of the old type of contracts in Korea. On the contrary, La, Gong-woo (2013) proposed quite an opposite idea of recommending partial coverage contracts such as ICC (B) or (C) more than 'expensive' ICC (A), based upon a simulation type research. He argued that most of Korean foreign traders mistakenly prefer the old clauses with excessive insurance premiums and complexity of terms and conditions. But his comparison of insurance premium relied on simple their absolute premium (rate) levels, not on relative value measuring both price and coverage together. Jeong, Bun-Do and Yoon, Bong-Joo (2013) and La, Gong-Woo (2014) compared ICC (A), ICC (B), and ICC (C) to show reasonable premium condition and operating expenses in theoretical context without considering loss ratios in whole market. More recently, Koo, Jong-soon (2017) comprehensively analyzed the, terms and conditions used exclusively for container cargo in international transportation.

To wrap up the literature review of the OMI, to our understanding, there has been no research to explicitly compare the usage of the old and new clauses in Korea or elsewhere. That is, it is still necessary to compare cost-effectiveness between old and new contracts, including specific contracts in each groups to see which contract has more value to **insureds** or insurers. And if any anomaly exists in the market, we still have to explore it with survey or interview of the suppliers or consumers of the OMI.

3. Development of the OMI contracts and their usage in foreign countries

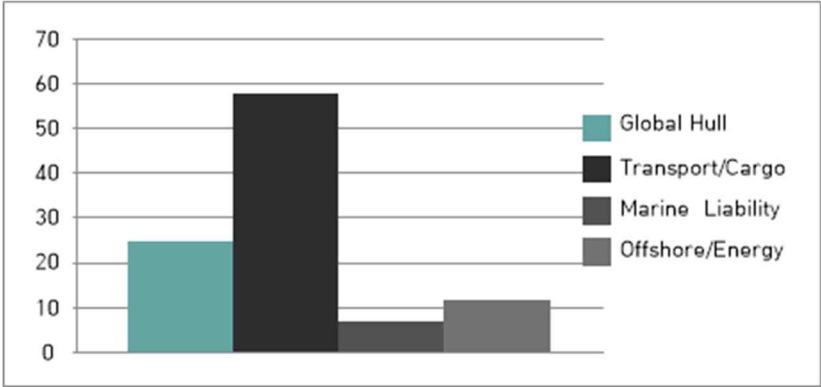
3.1 Overview of global OMI market

Figure 1 and Figure 2 display the size of the OMI market in the year 2019. Cargo

³ According to Clarksons Research, cargo carried is split 71% by sea, 16% by air and 13% by land **base on weight**. IUMI (2019), An analysis of the global marine insurance market 2019, International Union of Marine Insurers, p.9

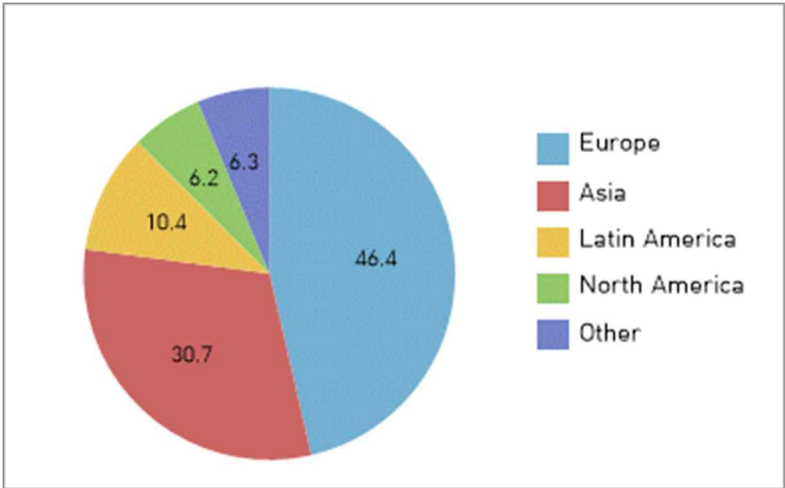
insurance and Europe is the largest line of business and region respectively, followed by hull insurance and Asia. Figure 3 shows loss ratios of cargo insurance from year 2006 to 2018 during which they fluctuate between 55% and 88%, averaging 70%. According to the Institution, the cargo insurance is not so profitable in general but better in Asia than in Europe.

Figure 1. Marine premiums 2018 by line of business



Source : IUMI(2019)

Figure 2. Marine premiums 2018 by region



Source : IUMI(2019)

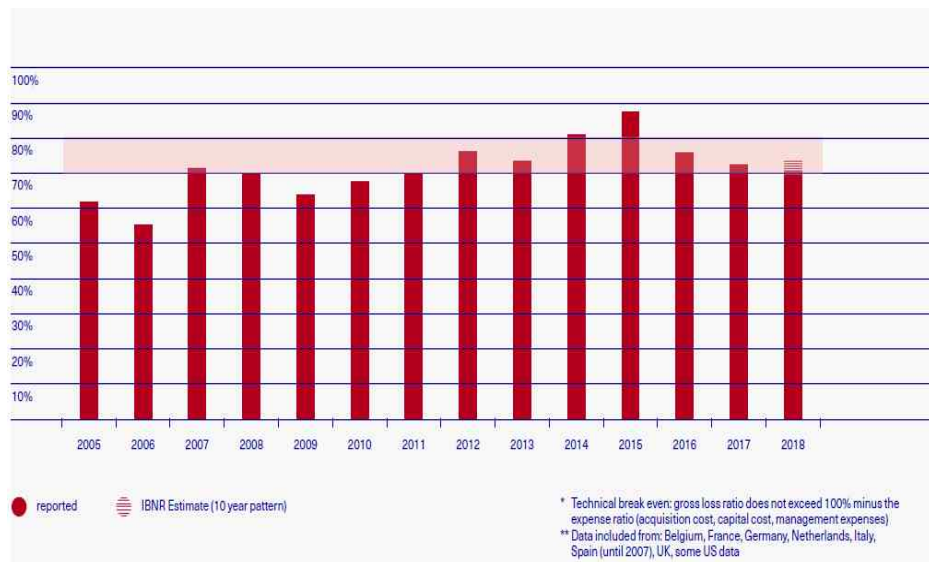
Figure 3. Ultimate total loss ratio of European(some US) cargoes

Figure 3 shows the ultimate total loss ratio of cargo in Europe and some US regions, focusing on insurance premiums, total premiums, payments, and outstanding claims from 2005 to 2018.

3.2 Development of the OMI contracts

The UK is well known to be the global center of the OMI. The oldest commercial insurance has developed in London, with its MIA (Marine Insurance Act) 1906 and several OMI clauses were born there and taken by global traders. In 1779, more specifically, Lloyd's S.G. policy form was adopted as a standard insurance policy form unified at general meeting of Lloyd's. The Lloyd's S.G. policy form was a contract established by accumulated experiences and cases in the OMI and was used as a single unified standard insurance policy form. Various precedents have been accumulated since then, and contractual uncertainty or unclarity could have reduced in the market with increasing usage of the form.

However, due to the industrial revolution and rapid development of the international transportation environment, Lloyd's S.G. policy form has become difficult to meet the demand for intolerable OMI in the 20th century. Accordingly, the necessity of a major revision was discussed, but due to various concerns, Lloyd's S.G. policy form was not revised, while individual agreements between the parties were additionally attached to the standard insurance policy. However, this also caused disputes due to the disagreement between the separate terms and conditions and the scope of compensation. At last, the voice for unification of the terms and conditions was spoken up to an intolerable level.

The Institute of London Underwriters (ILU) is an organization accredited by the British Government for its incorporation by London OMI companies, which began to be established under the British Corporation Act in 1884. The ILU aimed to defend the interests of marine insurers and promote the development of the OMI business through mutual cooperation and joint action. In 1963, the ILU enacted the institute clauses for the first time, attached and supplement then existing Lloyd's S. G. policy form. The linked policy forms to the Lloyd's Policy are called as ICC(A/R), ICC(WA) or ICC(FPA), (what

we call the Old contract here).

As an initiative to make the ICC policies free from and independent of the S.G., Policies, in 1978, the UNCTAD Secretariat highlighted the necessity of establishing a new international standard OMI policy and terms and conditions. In turn, the Joint Hull Committee and the Joint Cargo Committee began to work in 1979 to prepare a new standard insurance policy that replaces Lloyd's S.G. Policy Form. As a result, the Institute Time Clauses-Hulls (ITCH) and the Institute Cargo Clauses (ICC) were promulgated in 1982. As a result, Lloyd's S.G. policy form, used for about 200 years, was discontinued in 1983. The new ICC are distinct from Lloyd's S.G. policy and it is called the MAR form in UK practice. The ICC, established in 1982, is divided into terms A, B, and C as shown in Table 2 according to the scope of the damages to be covered, and in practice it is called the new terms. This is similar to the contents of the coverage with the ICC (A/R), ICC (WA), and ICC (FPA) created by the ILU in 1963.

Table 2. Institute Cargo Clauses 1982

Classification	Contents
ICC(A)	- Similar to 1963 ICC(A/R) -The widest range of insurance coverage as all risks are covered by insurance
ICC(B)	-Similar to 1963 ICC (WA) -The scope of insurance coverage is narrower than the ICC(A) terms due to the With Average condition, and the insurance coverage is wider than the ICC(C) terms
ICC(C)	-Similar to 1963 ICC (FPA) -The narrowest insurance coverage under the condition of Free from Particular Average

After twenty years of the change of ICC policies, strong demand for another change came up with the unfortunate breakout of terrorism in the United States in 2001, continuing trend of containerization, and other environmental change in international mode of transportation. To cope with these changes, the **Joint Cargo Committee (JCC)** of the British Insurance Market initiated a revision of the 1982 ICC on January 1, 2009, to modernize the words used in the terms and conditions, and interpretation of the contents of compensation, to protect the interests of the insured more by reducing the disclaimer and extending the insurance period. Details of revision are as in Table 3.

Table 3. Comparison of ICC 1982 and ICC 2009

Article	1982	2009	Reason for modification
ICC (A)	goods, cargo underwriters expect as provided	subject matter insured Insurers expect as excluded	Modernize the words Modernize the words Clearly indicate that the articles mentioned are exclusions
	Liftvan	Delete the word	Delete ambiguous terms
	Servants	Employees	Modernize the words
	proximately	Delete the word	Reduce confusion and conflict
	Brief description of losses, damages and	Details of loss, damage, and costs for bankruptcy ⁵	Reduction of the insured's immunity when the carrier goes bankrupt(good faith insured protection)

⁵ 4.6 loss damage or expense caused by insolvency or financial default of the owners managers charterers or

	costs for bankruptcy ⁴		
4. 7	arising from	directly or indirectly caused by or arising from	Expansion of exclusions due to terrorist attack or atomic attack
	weapon of war	any weapon or device	
8. 1	on delivery	on completion of	
10	held covered ⁶	must be notified ⁷	Delete ambiguous terms and clarify
15	This insurance shall not inure	This insurance	Modified in simple expression

Source ; Richards Hogg Lindley(2009), Institute Cargo Clauses 2009 – A Comparison of the 1982 and 2009 Clauses with additional commentary

In practice, the ICC 1963, ICC 1982, ICC 2009 could be used freely, but there is not much data for actual usage ratio. According to IUMI (International Union of Marine Insurance), there is no data of the OMI transaction with respect to contract form. We only could get the following expert opinion from IUMI.

Dear Professor Jung, I just received the following response from our British member, the Lloyd's Market Association: Speaking from the UK perspective, there are no statistics for this, only a common knowledge of use in practice. Underwriters are free to use whatever wording they like as long as it's not illegal or clearly wrong by reason of obsolescence. The ICC2009 clauses are in general use in the UK. It is thought there was no use of the 1963 wording after 1982 in the UK, and very little if any use of 1982 after the 2009 release. However, usage is never mandated. I hope this is helpful and will revert when I hear from our German member association. Best wishes, Hendrike Hendrike Kühl Policy Director IUMI International Union of Marine Insurance⁸

That is, the UK OMI focuses on the 2009 form (so to speak, the newest one) with a few exceptions of 1982 form and very few 1963 forms, in spite of any legal requirement to use the new one or the newest one, seemingly based on market principle taken by the Anglo-Saxon tradition. As the origin of the OMI law, principle or business, the UK may have no reason to stick to the old type contracts, once they have endeavored to develop the newest contract form.

Following information is to show that Germany is similar to the UK in its usage of the newest OMI contracts. The IUMI officer contacted Germany representative (German Insurance Association, GDV) to get replies to the same question as to the U.K. That is, German OMI usually takes the German domestic form of contracts except required by the UCP 600, the letters of credit, in order to avoid any legal conflicts arising from the English

operators of the vessel where, at the time of loading of the subject-matter insured on board the vessel, the Assured are aware, or in the ordinary course of business should be aware, that such insolvency or financial default could prevent the normal prosecution of the voyage. This exclusion shall not apply where the contract of insurance has been assigned to the party claiming hereunder who has bought or agreed to buy the subject-matter insured in good faith under a binding contract.

⁴ 4.6 loss damage or expense arising from insolvency or financial default of the owners managers charterers or operators of the vessel.

⁶ held covered at a premium and on conditions to be arranged subject to prompt notice being given to the Underwriters

⁷ this must be notified promptly to insurers for rates and terms to be agreed. Should a loss occur prior to such agreement being obtained cover may be provided but only if cover would have been available at a reasonable commercial market rate on reasonable market terms.

⁸ E-mail from Hendrike Kühl hendrike.kuehl@iumi.com (05 October 2020 18:33)

law. Otherwise, the Germany OMI uses the 2009 version, the newest contract. This is also reasonable situation.

*Dear Professor Jung, Herewith the response from our German member GDV. Sorry. We do not have any stats or counts for this. In general, German insurers far overwhelmingly prefer German standard conditions in insurance contracts avoiding English law and practice as stipulated in the Institute clauses. As far as I understand the 2009 version will be applied to insurance certificates when ICC A is required by ERA 600. I hope this is helpful at all. Best wishes, Hendrike Hendrike Kühl Policy Director*⁹

According to Satoshi Nakaide (2019, 2020), Japan also is similar to the UK. In Japan, the MAR Form (2009 contract) has become popular since 2009 when Japanese non-life insurers decided to promote the newest policy for **insureds** based on their judgement of mutual benefits from their usage of the contracts.¹⁰

4. Usage of the OMI contracts in Korea

4.1 Data and basic questions

Fortunately in Korea, unlike the UK, Germany, Japan, we could obtain historical data of the OMI contracts at the Korea Insurance Development Institute (the KIDI hereafter). The data includes information on the number of contracts, total premium, average premium per contract, the number of accident claims, total loss payment, and loss ratio over ten year period (2009 – 2018) from which we can answer the following questions for the first time ever:

A. How many contracts were concluded in each year? Among the old (1963), new (1982), and newest (2009) contracts? (Interestingly, a short answer is that old one (1963) dominates the Korean market, very differently from the other countries mentioned before)

B. Among those contracts, which one is more beneficial (profitable) to the OMI insurers? In that sense, the insurers are rational or biased toward the status quo? How about the value of contract to **insureds**?

C. Are there any trend in the ten year data in terms of behavior of **insureds** or insurers? Or any trend across differing forms of contracts?

4.2 Usage Analysis

4.2.1 General Trend

The old form contract is more extensively used than the new one or the newest one.

The Table 4 to the Table 7 summarize the domestic utilization data of the old and new clauses for the 10 years from 2009 provided by the KIDI. As can be seen from the Tables, the old contract form (of 1963) is widely used and popular in Korea more than the new ones (of 1982) or the newest one (of 2009) which is not used at all.

All-risk type contract is more popular than partial coverage ones.

⁹ E-mail from Hendrike Kühl hendrike.kuehl@iumi.com (06 October 2020 2:17)

¹⁰ 中出 哲「海上保険」有斐閣、2019年 114頁 日本では、貨物海上保険の領域では、1982年のMARフォームと協会貨物約款ができてからも約20年以上は、ロイズS. G. 保険証券様式に協会貨物約款を加える方式が利用されてきた。しかし、2009年の協会貨物約款改定以降は、しだいに新書式による引受けが広がり、現在では、信用状で指定がある場合などの例外を除くと、ほぼMARフォームと協会貨物約款2009年改定版に基づく新書式が利用されている。そのため、以下では、新書式に基づく方式を対象としてその内容を解説する。

As to coverage levels, the ICC(A/R) of 1963 and the ICC(A) of 1982 contract, so called all-risk coverage, are more popular than their alternative contracts such as the ICC(WA), ICC(FPA), ICC(B) or ICC(C) with partial coverage. The popularity of the all-risk type contracts have been usually attributable to convenience of wider coverage, affordable price, and little burden of proof (La Gong-Woo, 2013).

All-risk type contract is more valuable to insureds in terms of loss ratios, and also to the insurers in terms of the ratios' stability¹¹. Thus, it is not a valid argument in fact that partial coverage contracts are more valuable for insureds, which was argued before.

That the loss ratios of ICC(A/R) or ICC(A) terms are high and stable, in particular, means that, unlike the claims of existing domestic studies, ICC (FPA), ICC (WA), ICC (B) and ICC (C) contracts are sure to be more expensive than the all-risk type policies. In terms of loss ratio volatility, on the other hands, ICC(A/R) and ICC(A) contracts are more stable than the, others. Therefore, ICC(A/R) or ICC(A) contracts may be considered as more desirable for both the insured who can benefit from higher loss ratio and insurer who can enjoy more stable loss ratios, different from La Gong-woo (2013).

As average ICC (A) is around 10% more expensive than an ICC (A/R) while the former has higher loss ratio than the latter. Other things being equal, this means that the former contracts are more valuable than the latter in terms of coverage and value.

According to the statistics from 2009 to 2018, ICC(A) contract is about 10% more expensive on average than ICC(A/R) contracts in terms of average premium of contract, but the loss ratio of the former is 3% higher and its accident rate is 0.04% higher than the latter. As a result, we may say that the new contract provides wider coverage at lower premium rate than its old counterparty.

Table 4. Comparison of domestic utilization of ICC(A) and ICC(A/R)

	Number of Contracts		Premium Income (million won)		Average loss ratio (%)		Loss frequency(%)	
	ICC(A)	ICC(A/R)	ICC(A)	ICC(A/R)	ICC(A)	ICC(A/R)	ICC(A)	ICC(A/R)
2009	252,816	1,033,238	42,388	140,044	20.0	48.2	0.4501	0.6641
2010	288,405	1,213,504	53,403	157,531	43.7	91.5	0.3616	0.5845
2011	378,141	1,335,724	56,630	160,083	20.2	49.5	0.2544	0.5631
2012	418,227	1,284,394	61,508	151,938	27.7	57.1	0.3505	0.5821
2013	468,082	1,284,297	50,824	139,218	123.9	24.3	0.7591	0.5178
2014	499,800	1,328,509	52,371	134,541	310.8	25.9	0.8197	0.4172
2015	522,555	1,315,150	49,987	119,668	-	90.3	0.5402	0.4904
2016	553,965	1,343,175	43,062	110,294	65.8	107.9	0.6565	0.4132
2017	500,019	958,581	56,184	103,356	50.2	72.4	0.6458	0.4517
2018	571,577	1,665,120	57,413	121,886	43.0	93.6	0.3887	0.3722
Total	4,453,587	1,276,169 ₂	52,3770	1,338,560	67.9	64.3	0.5427	0.4990

Source : KIDI General Insurance Team, (Note some values are missing for unidentifiable reasons)

Table 5. Comparison of domestic utilization of ICC(B) and ICC(WA)

¹¹ The frequency of the OMI accidents by each contract is at a very low level of 0.04~0.5%, and their loss ratios are between 10% and 70% over years, substantially lower than the IUMI ratios that we have seen before, which implies high profitability of Korean OMI insurers in the world.

	Number of Contracts		Premium Income (million won)		Average loss ratio (%)		Loss frequency (%)	
	ICC(B)	ICC(WA)	ICC(B)	ICC(WA)	ICC(B)	ICC(WA)	ICC(B)	ICC(WA)
2009	8,203	11,860	4,142	382	61.9	-	2.7673	0.0169
2010	7,873	11,094	4,347	358	1.4	-	1.5623	0.0631
2011	8,927	9,803	4,340	594	57.1	6.5	1.1874	-
2012	8,791	8,237	4,062	319	26.3	124.2	1.4333	0.0607
2013	8,887	6,662	3,177	288	36.8	83.2	1.1702	0.0300
2014	9,146	6,170	2,936	251	3.1	-	0.6998	0.0972
2015	10,399	5,569	2,652	163	88.7	64.2	0.9712	0.0898
2016	9,981	3,591	2,277	112	33.7	23.3	0.9618	0.0557
2017	7,853	3,241	2,586	119	69.7	-	0.8150	0.0933
2018	7,068	2,686	2,658	80	84.3	39.9	0.5659	0.0745
Total	87,128	68,886	33,176	2,665	44.1	20.6	1.2063	0.0494

Source : KIDI General Insurance Team, (Note some values are missing for unidentifiable reasons)

Table 6. Comparison of domestic utilization of ICC(C) and ICC(FPA)

	Number of Contracts		Premium Income (million won)		Average loss ratio (%)		Loss frequency (%)	
	ICC(C)	ICC(FPA)	ICC(C)	ICC(FPA)	ICC(C)	ICC(FPA)	ICC(C)	ICC(FPA)
2009	6,302	38,215	714	4,816	7.5	24.9	0.0793	0.1047
2010	9,858	37,564	956	5,085	9.0	173.1	0.0101	0.2263
2011	12,720	33,794	1,412	4,790	9.3	373.4	0.0865	0.6540
2012	12,126	31,946	1,177	5,472	31.7	71.4	0.0907	0.1252
2013	13,189	32,067	1,028	4,278	-	-	0.0303	0.1060
2014	12,056	32,968	651	3,743	20.1	-	0.0332	0.0607
2015	9,268	33,836	432	2,798	34.9	118.2	0.0755	0.1123
2016	9,632	33,729	421	2,453	-	-	0.0104	0.0415
2017	8,033	25,532	415	2,845	17.5	63.1	0.0249	0.0470
2018	7,062	22,463	355	2,661	41.5	8.0	0.0425	0.0312
Total	100,249	322,114	7,531	38,940	14.5	72.6	0.0489	0.1586

Source : KIDI General Insurance Team, (Note some values are missing for unidentifiable reasons)

Table 7. Comparison of domestic utilization of ICC(Air) and ICC(A/R Air)

	Number of Contracts		Premium Income (million won)		Average loss ratio (%)		Loss frequency (%)	
	ICC(Air)	ICC(A/R Air)	ICC(Air)	ICC(A/R Air)	ICC(Air)	ICC(A/R Air)	ICC(Air)	ICC(A/R Air)
2009	93,985	375,580	4,679	12,160	36.8	20.3	0.1043	0.1401
2010	180,825	321,203	6,166	12,688	9.7	39.0	0.0791	0.1432
2011	213,407	322,257	6,595	14,274	37.1	69.4	0.0768	0.2079

2012	217,318	317,637	6,277	10,044	12.9	70.5	0.0594	0.2594
2013	240,728	313,202	6,820	8,113	14.8	46.3	0.0552	0.2439
2014	259,859	326,395	6,640	7,450	50.5	79.1	0.0562	0.2711
2015	263,774	346,385	8,759	5,961	19.5	61.2	0.0891	0.2116
2016	286,902	385,411	7,096	8,031	4.4	108.3	0.0491	0.1450
2017	259,699	393,283	6,568	12,123	15.3	34.7	0.0385	0.0742
2018	281,979	242,902	7,213	4,384	68.5	50.0	0.0997	0.1284
Total	2,298,294	3,344,255	66,815	95,227	26.2	54.4	0.0683	0.1802

Source : KIDI General Insurance Team, (Note some values are missing for unidentified reason)

Table 8. Comparison of the old clauses and the new ones over the 10 years

	New Clauses	Old Clauses	Average in 10 years	Notes
Average insurance premium per policy	0.117606	(>) 0.104889	old one cheaper	The larger the premium is, the more the coverage is (in general).
Accident frequency	0.5427	(>) 0.499	old one lower	The coverage of the new clauses seems to be wider.
Loss ratio	67.9	(>) 64.3	old one lower	More cost-effectiveness of new clauses for the insured

Source : Author's own calculation

Table 8 shows that the new contract is more expensive in absolute price on average but provides more benefit (i.e. higher loss ratio) than the old contract. The judgement favoring the new contract is supported by the higher accident frequency.

The data analysis above shows that Korean OMI market undergoes a strong status quo bias toward the old OMI contracts, while the newest contract (of 2009) is never used. Comparison of both types of contract reveals that the old one offers smaller coverage and lower absolute premium rate with lower loss frequency or loss ratio, which means that the old one is more beneficial to insurer than the insureds in general. Nevertheless, this finding may not be interpreted as profit maximizing behavior, as old contract with partial coverage is less profitable than the corresponding new one. Therefore, the only consistent interpretation of the phenomenon could be the status quo bias toward old contract in all types of contracts.

The following section aims to answer the consequential questions why we see the SQB in the OMI market.

5. Interview with OMI Underwriters and Insured Survey

5.1. Focused Group Interview (FGI) with the OMI underwriters

Although previous research on behavioral finance explains what drives the SQB in general, we conduct a Focused Group Interview in a written form with four major OMI underwriters in Korea¹² via the KIDI in order to answer the following questions by the

¹² Although four underwriters seem to be fewer than an acceptable sample size, they may be said to represent Korean OMI insurers fairly well because they represent the Samsung, the Hyundai, the KB, and the Meritz non-life insurance companies covering 60% of total premium written in non-life insurance of Korea. Furthermore, Korean non-life insurers hire only a few OMI underwriters who work for the profession for years. That is, we may say that total population of the OMI underwriters may number some tens at the most, and obviously their replies are as professional as can be imagined. Please refer to Insurance Statistics Yearbook (2019), Korea Insurance Development Institute, p.326, published in October 2020.

practitioners.

- 1) Why the old clauses are more accepted than the new ones ?
- 2) If there is any difference between Korea and other countries in the choice of OMI clauses ?
- 3) Why all risk type contracts are more popular than partial coverage ?

5.1.1. why the old clauses are more accepted than the new ones ?

A	OMI insureds prefer the old clauses (1963 version) while feeling unfamiliar or uncomfortable with the new clauses (1982 version). This current situation will never change unless the old clauses disappear.
B	In case of umbrella (e.g. large sized) insureds, they stick to the old ones while feeling no major difference between the old and new clauses. Particular (e.g. small sized) insureds, however, do not know that the new ICC (A) covers all-risk. Moreover, when issuing L/C, banks require to include the ICC (A/R) conditions only, without knowing that either ICC (A/R) or ICC (A) is acceptable. Third, none prefers to change the OMI coverage.
C	When signing an OMI contract, various clauses are offered to insureds together with expected premium, who cannot tell the difference among them. And very few read and compare all the English clauses before making a decision. In addition, insurance is often sold not bought in trade practice by insurers which just want to follow the requirement written by the bank's L/C department. For insureds, only the feeling matters that the cargo can be secured for full-coverage notwithstanding any possible difference between options.
D	There may be some differences in choosing clauses, without any particular trending.

5.1.2. Difference between Korea and other countries in the choice of OMI clauses

A	Agree. There are some differences between Korea and other countries.
B	While foreign insureds do not know the difference well, their insurers prefer the new clauses with clearer coverage than the alternative.
C	Although varied by country, it is well-known that most countries except Korea mainly use the 2009 ICC, as the foreign insurers explain the difference and recommend the new one to the uninformed stakeholders such as banks or traders in the insurance market with information asymmetry.
D	The purposes of transformation of the old clauses into the new clauses are to 1) improve readability by deviating from obsolete and difficult expressions, and 2) to resolve disputes caused by various coverage or exemptions. The ICC 2009 were also seldom used in Korea.

5.1.3 Why all risk type contracts are more popular than partial coverage

A	ICC (A/R) is preferred because the difference in insurance premiums is not that large, with other things being virtually equal.
B	Insurance premiums for cargo insurance are cheap, so the difference of premium between ICC (A/R) or ICC (A) and the others ICC (WA), ICC (FPA), ICC (B) and ICC (C) is not so significant
D	ICC (A/R) and ICC (A) offers a comprehensive or virtually full coverage, indemnifying all loss or damage except for a few risks specified, while the other clauses cover less obviously. Naturally insureds choose the wider coverage even if paying a bit more insurance premiums.

The responses of underwriters of the OMI reveal that they recognize the both difference

between the overseas market and the Korean one in terms of the SQB and advantage of new clauses over the old clauses. Seemingly they may pass part of responsibility to insureds or to banks issuing L/Cs.¹³

5.2 Supplementary in-depth interview with an underwriter

After the FGI with the OMI underwriters, we conducted an in-depth interview in November 2020 with the underwriter of the company C who offered a highly dedicated reply with expertise of both domestic and foreign OMI market. According to him, he confirmed that the ICC 2009 is generally used in most of foreign countries. And Korean insurers present the SQB by hesitating to deviate from existing contract forms, as they are largely indifferent to profit, terms or conditions as they focus mainly on their size or market share. In case of Korea, he said, not only insurance companies but also other stakeholders have a low care or little understanding of the OMI clauses. In particular, the OMI is perceived as simply required for trade practice rather than as necessary to cover transportation risk for the trade per se. He also added that many foreign traders use the old clauses because domestic banks usually require ICC (A/R) conditions when issuing L/C probably without knowing that the new ICC(A) play a similar or better role than its old counterpart.

5.3 Insured Survey

For the sake of completeness of this research, survey to insureds was conducted between July 1st and July 14th of 2020 with those who are working for Korean trading companies and are in charge of purchasing the OMI policies the Ace non-life insurance company of Korea. In spite of the support of a managing director (Mr. Choi, Eunseok) for the survey, we managed to receive just 15 respondents with the following results.

Among the total 15 respondents, 8 responded that they subscribed the old clauses ICC (A/R) and 6 responded to use the new clauses ICC (A). As to the question why you chose to subscribe the contract, 8 responded with the answer ‘as a custom (Status Quo)’ and 6 with ‘as advised by my insurer’, 1 with ‘for wide coverage), presenting the SQB or incomplete information among the insureds. While average duration of the existing contract form is shown to be 3.9 years, the insureds appear to stick to current contract for the time being because of convenience (5.4/7.0), no stress (4.7/7.0), tradition (5.3/7.0), custom (5.1/7.0), showing the SQB as well.

6. Conclusion and Implications

This research aims to fill the gap between theory of behavioral insurance, particularly the status Quo Bias, and practice of the Ocean Marine Insurance (OMI) by using data, emails, interview, and survey methods. It is well known that the OMI has undergone revamp of its standard form of contracts in 1982 and in 2009 to complement the old Lloyd’s S.G. policy for more clarity, stability or balance. Using both qualitative observation and quantitative data, for the first time ever in its kind, this research compares popular contract types of the OMI between Korea and a few industrialized countries (e.g. UK, Germany, and Japan) in terms of status quo bias, trade development, and even consumer protection.

Surprisingly, however, the result shows that Korean foreign traders rely on the old type (born in the year 1963) OMI contracts while the other countries use the newest OMI contract (developed in 2009). It is shown with simple loss ratio analysis of the contracts over 2009 – 2018 period that the behavior has little to do with rational profit maximization of insurers, as some new contract can provide more average profits than the old contract. The consistent addiction to old type contracts in Korean OMI market reveals strong status quo bias of Korean exporters, importers, bankers or insurers which is confirmed by a focused group interview with four underwriters, a following in-depth interview and a survey to fifteen insureds. **For international comparison, we conducted a few email correspondences with experts in the U.K.,**

¹³ According to Satoshi Nakaide, Japanese insurers began to actively recommended the newest clauses of 2009 to their customers in 2009 with the belief that they will be better off with the new contracts.

Germany, and Japan where any data of the OMI contract type are not available. In spite of data unavailability of the foreign countries, this research ends up with new finding and significant implications for development of trade practice and policy.

This research of truly originality has both academic and practical value as it comes up with new findings and significant implications for development of trade practice and policy. First of all, this research is based on actual and official statistics which have never been used in all the previous Korean research on the OMI. As most of the researches about OMI focused on legal or contractual issues, approaches from actual usage would provide a broader perspective on this field. Second, the research shows that all risk OMI policies provide more values, in terms of coverage given premium, to insureds than partial coverage policies, different from previous research argument in Korea. Therefore, not only insurance coverage, but also cost and value side of the OMI should be considered when insured choose OMI contract. Third, the research presents strong SQB in Korea. As KIDI data showed, insured and insurer prefer ICC 1963 than new ones regardless of price and loss ratio. The bias may be attributable to uninformed traders (insured), informed but dull insurers, or conservative bankers.

Some scholars argue that coverage of ICC 1963 is wider than the new ones, so the insured might prefer ICC 1963. However, according to our results, the average loss ratio of the ICC (A) is a little bit higher than that of the ICC (A/R), which otherwise should be have been lower simply with narrow coverage. We could assume This evidence enables authors to argue that benefit from clearer and modernized clauses that might prevent the conflict would be higher than dominate wider coverage, if any, of the 1963 clauses in some aspects.

Thus, in order to further develop foreign trade, there should be policy initiative to review current practices of the OMI contracts and to move forward with new contract forms. According to previous studies, SQB diminished as individuals gain experience and information (Shapira and Venezia, 2008; List and Haigh, 2005), so the government the insured, the insurer or financial supervision agency could diminish those SQB by revealing obtaining more information such as comparing the cost and benefit, loss ratio data or by requiring description obligation duty of explanation to the insurer about comparing each ICC type (p.16). The Financial Supervision Service or academic seminar may also encourage banks and insurers to review the current practices leading to the SQB.

Unfortunately, there is no data about ICC 2009 usage in Korea, so we could not compare it with ICC 1963 and 1982. Also, international comparison in our study was limited to developed country. Hopefully further research can be continued with formal survey with more sample size and wider range in order to explore the structure of the SQB in the OMI in more depth or detail.

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