bharat RE™

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RISK ALERT

NEWSLETTER FROM INDIA'S LEADING INSURANCE BROKING HOUSE

Highlights

From the Editor's Desk

We are into the next monsoon season in Chennai, and many commercial enterprises are yet to come out of the financial consequences of the floods last December. The numbers are staggering......

- The Financial losses exceeded Rs. 20,000 crores
- More than 20,000 MSME units suffered losses to a tune of Rs. 14,000 crores
- Production losses exceeded Rs. 10,000 crores
- Repair & Replacement loss – Rs. 2500 crores
- Raw material, tools, infrastructure, and software loss – Rs. 2500 crores
- Number of workers directly / indirectly displaced – 2 lakhs

It should be a matter of grave concern that just 10% of the economic loss is likely to be insured, proving once again that the insurance industry in India does not play an important role in helping the economy bounce back from a catastrophic event like a Flood or an Earthquake. It has been repeatedly proven whether it is the Thane and HUD HUD cyclones, the floods in Uttarkand, Jammu and at Chennai, that the commercial enterprises, irrespective of their size are in majority of the cases, with no insurance and even the small minority who had insured are so badly covered, that in most cases, it is as good as being uninsured.

We have seen a number of cases in the Chennai floods, of enterprises who suffered total losses, being forced to close down their operations without the financial support of insurance. At the same time, an equal number of enterprises with insurance policies in place had to forgo a significant portion of their loss to the fine prints of the wordings of their insurance policy. The added issue of the surveyors / insurers having a deep sense of distrust of the claims preferred by the insureds, further eroded the already low belief that insurance is a vital ingredient of any commercial enterprise's existence.

If the commercial enterprises in India are to be insured in the first place and adequately too, the message needs to be taken to them effectively, continuously and convincingly. This requires properly trained manpower that will be able to effectively and repeatedly communicate the advantages and the implications of having / not having a proper insurance program in place.

Unfortunately, the insurance industry including the intermediaries, have reduced the marketing and selling of commercial insurances to a transaction based model rather than an advisory based model. This has resulted in prioritizing the pricing as the only selling point with the result that the insuring business community has been led to understand that price is everything. The Regulators have also prioritized their objective as protecting the policy holders' rights / interest and have made the job of intermediation / advisors unviable with a host of rules and regulations which are perfect for a well-developed insurance market with high insurance penetration levels, but totally unworkable in an under penetrated and difficult commercial insurance environment.

If the objective is to improve the way insurance is being purchased / organized by the business community, we need to see a paradigm shift in the way we approach commercial insurances!!

Vijay T
AICWA, ACS, BL, AIII
CEO & Executive Director
Bharat RE-Insurance Brokers Pvt Ltd, Chennai

ON OUTSOURCING

"The knowledge needed for any activity has become highly specialized. It is therefore increasingly expensive, and also increasingly difficult, to maintain enough critical mass for every major task within an enterprise. And because knowledge rapidly deteriorates unless it is used constantly, maintaining within an organization an activity that is used only intermittently guarantees incompetence."

- Peter Drucker

ON OUTSOURCING

What Peter Drucker means...
The requirement for "Outsourcing" cannot be more critical than in the insurance and risk management areas. Enterprise Risk Management (ERM) has moved way beyond insurance expertise alone, and today requires skills from other domains – both technical and commercial. It is impossible for an enterprise to have in-house expertise for ERM, and more importantly, keep it updated and useful, especially when the usage can only be in the event of an infrequent major claim.

Case Study

It PAYs............to get into the Details

A 50-MW steam turbine of an East European make, running trouble-free since 2002/03, suffered a breakdown due to which the powergen plant was totally shutdown resulting in power outage and revenue loss for a few weeks. The insurers promptly deputed a competent engineering loss surveyor to investigate the nature and extent of the claim under an all risk policy.

This powergen unit was being operated as a peaking plant with relatively lower operating hours and at partial load cycles. The power plant was operated through a Distributed Control System (DCS) with fully automated ramp-up and ramp-down logics provided by OEMs, ensuring minimal human intervention. The 50 MW direct condensing type 40 stage steam turbine had 62 blades made of corrosion-resistant stainless steel

Close-up View of the Pressure side of the Fractured Turbine Blade

arranged in 3 segments, strung by means of three damping wires made of titanium and connected with sleeves. The turbine rotor was supported on cylindrical bearings designed for critical speeds above 5000 rpm.

The set suddenly experienced high vibrations and tripped due to high vibrations when it was running normally at around 20% of its rated full load. A blade in the last stage suffered rupture by way of damping wire hole plane and a few other blades in the vicinity sustained long cracks. Rubbing marks were observed on the casing in the direction of rotation. Insured's engineers decided to shave off all the blades in the last stage and run the turbine till the spare blades were arranged, to minimize the generation loss. The powergen set could be boxed up and resumption of generation was possible only after 5 weeks of outage.

The claim was basically for the cost of repairs due to the breakdown and Loss of Revenue to the tune of Rs 10 crores.

The damaged blade samples were sent to a private testing lab to carry out metallurgical tests in order to ascertain the cause of blade failure. The lab report noted presence of fretting marks, minor corrosion & erosions of the blade and concluded that the probable cause was due to "corrosion fatigue" on ID side of the damping wire hole of the blade.

Based on above lab findings, the surveyors interpreted the cause of breakdown as part of the policy exclusions. However the Insured felt that the minor corrosion marks on the blade would not cause its rupture and disagreed with surveyors on the rejection of their claim.

After sustained negotiations, it was agreed by the surveyor and insurer that a full-fledged Root Cause Analysis (RCA) exercise involving site visits and technical

Cut-away view of the samples sent for Lab analysis, sheared in way of DW hole towards the leading edge

investigations into turbine history card, operational data , DCS readings, visual examination of turbine parts, non-destructive testing (NDT) and finally detailed lab investigations, including fractography of failed component sample, Scanning Electron Microscopy (SEM) coupled with Energy Dispersive X- ray elemental Analysis (EDX) etc, should be carried out by a competent institution.

The services of a highly reputed Govt of India testing agency/ lab was proposed and accepted by all stakeholders. The RCA report could finally establish with logical analysis and clinching evidence, the most probable cause of blade failure / turbine breakdown was due to fast fracture of the turbine moving blade, as sequenced below:

- The steam turbine got tripped on excessive vibrations when the machine was running at partial load at which low flow conditions would prevail.
- The blades in the last stage of a condensing turbine would undergo combined torsion and bending vibration. Hence the possibility of excessive vibrations to the blades was unlikely unless there was any imbalance in the flow. (It was in the last stage of the turbine that the moving blade suffered a fast fracture).
- Under this running condition, it was likely that eddy currents were induced due to momentary steam condensate hammering.
- Such eddy circulation with negative damping could create a flutter in the blades which would generate self-excited vibrations with uncontrolled amplitudes due to negative damping, which had led to a sudden snapping of the blade damping wire and its sleeve.
- This had caused more imbalance and loss of positive damping in the machine.
- The synergic effect of failure of both damping wire and its sleeve in combination with torsional and bending induced vibration, could have caused the blade to fail in a short period of time (fast fracture), as evidenced by the ridges on the fractured surface.

S. Ramesh

BE (E&E) F.I.I.I. Technical Director, Bharat RE-Insurance Brokers Pvt Ltd, Bengaluru - Formerly with New India Assurance Co. Ltd, Head – Energy with TATA AIG General Insurance Co. Ltd, having more than 4 decades experience in the Insurance, Loss Assessment, Safety Audit and Risk Management disciplines.

Bharat REVIEW

Establishing the cause of loss in many cases requires not only technical expertise, but also a clear understanding of commercial and legal implications as presentation of data collected needs to be done in a clear and cogent manner to ensure that fine prints in the policy are not misinterpreted against the insured. The unviable premium rates have forced the insurance industry to read between the lines and arrive at interpretations which would not be acceptable in a legal forum.

The ineffective legal remedies allow ample opportunity for the underwriters to deny and delay claims without any impact on their credibility and continued acceptability in the market.

In the News

Insurers face $600 mln claim in Brazil dam burst

Insurers covering risks for a Brazilian mine where two dams burst due to flooding killing at least six people and 28 gone missing, could pay up to $600 million in claims. The dam breach was the largest ever spill of its kind, and difficult to determine what caused one dam to fail and another to be "affected".

There were three tailings dams used to store mineral waste and water at the mining operation. One burst, spilling the contents into the collection of waste held back by a second as well as across a rural swath.

The cost to the companies, including for cleanup and rebuilding, could top $1 billion and it is estimated the mine could be closed until about 2019.

The property policy could cover up to $90 million in related claims, and a separate policy for business interruption events could pay as much as $510 million if it is proven that it lost that much in profit.

A separate policy for civil liabilities, which had a coverage of about 70 million reais could be "too small" to pay for extensive environmental damage, apart from the compensation for families of the victims.

The dam burst unleashed 60 million cubic meters of mud and mine waste that devastated a village, killed at least 13 people and polluted a major river valley.

Source – Internet

Three days after an avalanche of mud and mining sludge buried a town

Rs.200 crore claim – DENIED!!

An insurance company had rejected the Rs. 189-cr claim arising out of a fire in a rice mill in 2014.

The rice producer and exporter plans to challenge the rejection of insurance claims made by it for the damage to paddy and rice inventory in a fire in one of its units during June 2014.

The fire damaged paddy worth Rs. 189 crore and the stock was fully insured However, when the insured claimed the payment, the insurer rejected it.

The claim amount was six times its net profit in 2014 - 15 and 63 per cent of its standalone net worth.

The chairman of the rice mill company said the insurer gave no reasons. “We had made a genuine claim, after taking advice from top lawyers and we will file suits against the insurer,” he said.

Source – Internet

Case Study

Swimming.......... between the ....LINES!!

In CAT events like the Chennai floods and previously in the HUD HUD and Thane cyclones, we have had the opportunity of being involved in a large number of claims simultaneously and every time, the extent to which the insurance arrangements are inadequate, is striking.

The Chennai floods is yet another example of Commercial Enterprises paying the price for badly designed insurance policies resulting in severe financial constraints and closure of many units.

It comes as no surprise that the commercial world, especially the small and medium enterprises, are defectively insured when the market's focus, be it insurers, intermediaries and the insured, is only on price, with the result that insurance policies have become commodities to be bought off the shelf from the cheapest vendor, and not as a business protection for the enterprises, which is implemented after review and evaluation, requiring the services of experts.

A manufacturer of agricultural implements with a loss in excess of Rs. 100 lakhs. Issues pertained to damages to floorings and robotic equipment involving months of discussions with the insurance company and surveyors, to resolve.

An under construction commercial complex with a loss in excess of Rs. 300 lakhs. Establishing the loss to the satisfaction of the loss assessor when substantial assets had been washed away was an ultimate test of patience for all concerned.

An electrical panel manufacturing company had a total loss situation as the unit was under 15ft of water for days. After a six months struggle with the surveyors and insurance company, they were able to recover about 30% of their actual loss.

An IT park with 25ft of water, submerging its multiple basements with the entire power infrastructure – including the generators, resulted in the total disruption of the IT services housed in the park. Loss amount was in excess of Rs. 700 lakhs. Obviously, they had issues with compensation from insurers, with about 20% of the claim being disallowed, as movement of assets in the recent past was not reflected by modifications in the insurance cover.

The plant was accessible only after a week. Substantial stocks were washed away and stock in many underground tanks were contaminated. Apart from the normal repair – replacement issues, claims for roads and catalysts had to be seriously debated due to peculiar claims situation caused by the floods.

A company trading in medical devices had their godown completely inundated and the loss was more than Rs.300 lakhs. The claim settlement was an exercise in endurance as issues in underwriting from the insurance company almost resulted in the claim being denied.

Case Study

Claim dissolves – paper by paper!!

Unprecedented floods damaged the plant and machinery and stocks in a paper mill resulting in an estimated loss of about Rs.13 crores.

The insurance company appointed a surveyor, and on his report, offered to settle the claim for about 40% of the amount claimed after a period of around two years. The insured took the dispute to arbitration, where the various points of deduction / disallowance were presented:

- Finished goods for a value of more than Rs. 50 lakhs were disallowed as the surveyor contended that the finished goods were not directly affected by flood water, even though the flood levels were unprecedented in the last 100 years. His contention was that the damage was predominantly due to high moisture levels which resulted in reduction in strength and brightness. Since the claim was due to loss of realization due to altered parameters, the inadmissibility of the claim was attributed to the indirectness of the cause of loss. The insurance company brought out pages of supporting documents regarding the application of proximate cause to show why the damages were not payable.

- More than 600 MT of imported waste paper were being shown as material in transit and not reflected in the computerized system as invoices were not received from the clearing agents. The insured was able to show the physical stock in the factory and other documentary evidences like invoices, payment advices to the bank, material receipt notes etc. to prove the materials were at the site during the flooding. Inspite of this, the surveyor ignored the documentary evidence and chose to deny the amount stating that the materials might have already been consumed in paper production.

- Machinery spares and accessories in excess of Rs. 125 lakhs were damaged. These were both for preventive and scheduled maintenance and were procured well in advance and stocked as the lead time for many of them were more than 6 – 8 weeks as the materials were made to specification and compliance. The surveyor allowed only Rs. 3 lakhs as he considered spares which were consumable in nature only under the assessment and other spares which were not normally required to be kept as spares, was excluded from the claim as he felt that these items were of capital in nature and not forming part of the consumables.

- Some of the raw materials had been stored in the open yard under tarpaulin covers. Although the stocks were exposed to 6 feet of water, the surveyor contended that since the stock was already exposed to the environment including rains for more than 6 months, the damage was not attributable to flood and inundation alone, and made an arbitrary deduction of 50% of the claim, amounting to Rs. 75 lakhs. This again was based on hypothetical possibilities, over riding the consequences of the hard reality of devastating floods being in all probability, the sole cause for the damages.

- Almost Rs. 200 lakhs was disallowed by the surveyor as slow moving items. He also contended that these items were not in economically viable quantities that can be utilized in production and due to efflux of time and the effect of vagaries of nature, the items underwent natural deterioration and were not damaged by the floods. The insured was able to show that the alleged slow moving items were those used only during manufacture of a certain quality of paper. In fact, the market value of the stocks increased because of the increase in price and fluctuation in foreign exchange rates. These raw materials were used when specific orders were received. At the same time, the surveyor accepted that whether an item is moving or non-moving which he defined based on the period of retention in the factory, inundation of water undoubtedly deteriorates the value of the stocks, whether moving or non-moving. The insured explained the storage processes to keep the quality of the materials intact, and that the raw material does not deteriorate in quality due to prolonged storage.

Vinod Reddy

Director – with more than 40 years experience in the insurance industry.

Venugopal Rao

General Manager – with more than 30 years experience in the insurance industry.

Bharat RE-Insurance Brokers Pvt Ltd – Hyderabad

Bharat REVIEW

It is quite common for the insurance industry to put in their best efforts to ensure that claims are reduced to the maximum. The neutrality of the surveyor is only a theoretical belief, as he is appointed by the insurers, and in most cases, would be required to toe their line of thinking. In today's L1 market, almost all claims end up being a war of attrition between the unequal parties and in almost all cases, the insured is forced to give in. The legal system being what it is in our country, the insurance companies have no hesitation in quoting rules and interpreting policy conditions to their advantage, knowing fully well that the insured is unlikely to look at legal options and would probably settle for a small percentage of the actual loss rather than a prolonged litigation.

The Bharat Re team was successful in taking the above dispute involving multiple issues to arbitration, and through the presentation of the facts and interpretation of the policy conditions, was able to get an award from the arbitrator for more than 90% of the disputed amount, resulting in the insured getting an additional Rs.6 crores as compensation.

Case Study

Claim Washed Away too..................

A dealer in chemicals based out of India had a branch in a neighbouring country. They had taken a policy with a local insurer which included coverage for flood.

During the renewal, based on discussions with an executive of a competing insurance company, they shifted their business based on a quotation given by the company which clearly stated that the risk of flood was covered. Subsequently, the policy was issued by the insurance company, and as most corporates do, the insurance document was filed and kept away.

A few months later, they shifted their godown to a new location, which they duly intimated to the insurance company. The insurance company inspected the godown and passed an endorsement in the policy changing the location address. A short while after the endorsement, the area was affected by severe flooding, resulting in a loss of around Rs. 150 lakhs to the stocks, most of which were washed away.

When the claim was preferred with the insurance company, they assessed the loss at Rs. 150 lakhs, but offered a compensation of only Rs. 25 lakhs as ex-gratia, with a covering letter stating that the risk of flood was not covered!!

In panic the insured verified the policy for the first time, and as expected, the risk of flood was excluded under the scope of cover. Apart from that, the policy coverages were so complex that it provided coverage for "cyclone, storm and tempest" as one cover, the risk of flood given as a separate optional cover and "natural perils" which included "Tsunami, Tidal Waves, Volcanic Eruption, Tornadoes due to atmospheric disturbance, Hurricane, Typhoon, Thunderstorm, Hailstorm, Windstorm, Rainstorm due to atmospheric disturbances" as yet another cover.

Each of the covers mentioned above had its own list of exclusions, which again required legal skills to interpret. For example – "loss or damage by rain" was not payable unless the building in which the assets were stored shall "first sustain actual damage". If this was not enough, the "actual damage had to be sustained to the roof or walls".If this again was not enough, this "damage had to be sustained by a direct force of a cyclone, storm or tempest". If that was not ALL, even if it was caused by "cyclone, storm or tempest, damages were excluded if it was linked to a landslide, subsidence or inundation"!! and the list goes on......

If you were fortunate to have the flood cover, don't be too sure as it gives a restrictive definition of "Flood" with its own set of exclusions!!

Claims Team
Bharat RE-Insurance Brokers Pvt Ltd
Chennai

Bharat REVIEW

We are fortunate that at least for the flood coverages, the Indian insurance industry has a built in comprehensive cover without too many hidden traps. At the same time, policy wordings and its interpretations are reaching the heights of ingenuity, that confirming that any risk is covered is certainly not possible. It would be prudent for any commercial enterprise to more than double check the coverages. At the same time, the availability of expertise within the organization to handle the present "reduce the claim to the maximum" mode is debatable!!

Our experience over the years, in handling and resolving hundreds of claims over the years, has shown that handling the insurance program is best left to professionals and even in that case, at the policy design stage itself, and not at the claims stage!!

It's the way you look at it - Half full or half empty!!

A leading coal trading company had taken a credit insurance policy to protect their receivables. The policy was issued to cover the entire turnover of Rs. 190 crores. They had applied for a credit limit for one of their top buyers and the limit of Rs. 35 crores was approved by the insurer.

This buyer defaulted on repayment, and after the policy conditions regarding the waiting period, credit limit exposures etc had been complied with, the claim was made by the company.

During the waiting period, the buyer had paid about Rs. 7.5 crores and the loss was about Rs. 23 crores. After applying the terms and conditions of the policy regarding the premium paid and the maximum liability, the client expected the insurer to compensate him Rs. 12.16 crores. The policy wordings regarding the definitions of "insured debt", "insured losses", "insured percentage" and "net debt" also supported the clients' expectations.

The ingenuity of the insurers in interpreting the policy wordings to ensure the claims settlement are kept to the minimum, was underestimated, as they gave a different interpretation of the policy wordings and brought down the claim amount to less than 35 % of the actual claim..

Jeyaraj Thanghavel
BBM, PGDGM, LLB Head – Credit & Political Risk Insurance, Bharat RE-Insurance Brokers Pvt Ltd, Chennai with 11 years of total work experience in Trade Credit.

Bharat REVIEW

In today's L1 market, policy interpretations are in almost all cases, unreasonable and sometimes, to the extent of being malicious. The amount of time and effort involved in getting legitimate claims has to be seen to be believed!! The race for business pushes down the premium rates and the insured and intermediaries make best use of the situation to claim that they have got "the best rates". The resulting unviability of the entire process shows up in the event of a claim, making the whole purpose of insurance meaningless!!

Fortunately in the above case, the client started receiving payments from the buyer for the outstanding debts and continued to do business with him and the claim was withdrawn. Otherwise, it would have met decades of litigation before one could see the color of money.

bharat RE

In the News

Chennai floods: Auto dealers cash in, charge Rs 11,000 parking fee

Parking charge of Rs. 11,000, repair estimate charge of Rs. 4,500, towing charges of Rs. 7,500, and dealers forcing vehicle owners to go in for a new vehicle were some of the complaints voiced by the owners of vehicles affected by the recent floods in Chennai.

Venting out their anguish in getting their vehicles repaired and insurance claims honoured, vehicle owners complained that the automobile dealers are cashing on their difficulty while car companies are turning a blind eye.

"A dealer quoted a high rate for repairing my friend's car. My friend decided to get the car repaired elsewhere and the dealer charged a parking fee of Rs. 11,000 after reducing from the initial figure of Rs. 16,000," a flood victim said.

"The parking fee is not covered under any insurance policy. Further car dealers are also charging around Rs. 4,000 for preparing the repair estimate," complained another victim.

According to another source, the car dealers were charging anything between Rs. 7,000-Rs. 9,000 as towing charges, whereas insurers reimburse only Rs. 1,500.

According to the General Insurance Council of India, around 50,000 claims have been lodged with the insurers.

Source - Internet

Chennai calamity: Flood-ravaged corporate jets to cost insurers Rs 500 cr

An aerial view of a partially submerged airplane in Chennai

Eight private jets owned by corporate houses were irreparably damaged in the Chennai floods last December, having a combined insured value of around Rs. 500 crores. The jets were submerged for a prolonged period under water and there was water ingress in the entire aircraft including avionics, auxiliary power units and engines

The insurers have been involved in the process of assessing the claims through surveyors and loss assessors. "The damages to the jets and its parts are severe and cannot be restored. Hence, we will have to dismantle and sell parts as scrap, though we will only be able to recover 20-30 per cent of the costs," said the head of a public sector general insurer, which had exposure to these jets.

The Chennai aircraft manufacturers had called for an evaluation of the damaged jets, who ruled the aircrafts were beyond economical repair, as the cost of repair would be higher than the current fair value of these aircraft, sources said.

"Globally, the Chennai floods may not be considered as a big loss in the aviation sector. However, we have never faced this big a hit in this segment, which will directly hurt our books. Some part of it was reflected in the third quarter and some of it will be visible in the fourth quarter," said the general manager of a public general insurance company.

Source - Internet

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