bharat RE

RISK ALERT

Newsletter from India's Leading Insurance Broking Company

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SPOTLIGHT

HIGHLIGHTS

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APRIL – SEPTEMBER 2023-24

We have completed six months of the financial year 2023-24 and the first half of the year has been relatively good for the General Insurance industry with a growth of around 15% when compared with the previous half year. The growth in business has been as expected in the Health and Motor verticals, accounting for almost 90% of the growth.

LOOKING AT THE LONG TERM

Swiss Re's estimate of the global general insurance industry for the next 20 years has shown that Property and Liability would be the fastest growing lines of business and that emerging markets like India will lead global growth and constitute 33% share of the market. While the growth and future potential is encouraging, emerging markets, especially India, still have a long way to go with regard to catastrophic events protection, with reinsurer data showing that in the last 20 years insurance covers less than 5% of the economic losses due to CAT events like floods and earthquake in the Asian region while it is a significant 45% in the more developed countries.

CURRENT SCENARIO

Moving away from premium growth, insurance is still looked at only as a cost with low risk awareness, price based distribution channels and a complicated and stressful claims process not providing the confidence that insurance will make a difference between being in business and insolvency.

It is still quite a task to get commercial enterprises to insure. We have had the personal experience of insuring the property of about 2000 tiny enterprises over a five year period with the renewal being a difficult task and at present, able to renew only about 10% of the original number, despite the active support of the trade associations and significant claims paid during the Chennai floods and Gaja cyclone even when the renewal premium was only INR 100 per annum!!

GOING FORWARD

In recent months, the Regulator has been actively pushing for the rates to be market driven against an almost tariffed rate, as they felt that there should be a differential pricing based on risk protection measures, claims ratio, excess / deductibles. While this is, in a larger perspective, the right approach to be taken, it created unviable premium rates due to intense competition when it was implemented earlier in the period 2012-18 and ultimately the reinsurers stepped in the year 2018 and implemented the minimum rates.

From the insured's point of view, it is a double edged sword with the benefit of the premium outgo coming down probably quite significantly, while on the other hand, the claim paying ability of the insurance industry is significantly weakened with the low price, with the result that the main purpose of insurance of "fair and quick claims settlement" in the event of a major loss being severely compromised and claims getting into delays, disputes and denials.

VIJAY T
ACMA, ACS, BL, AIII
CEO & Executive Director

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 organisation an activity that is used only intermittently, guarantees incompetence.

- Peter Drucker

CLAIMS ANATOMY

EXPLOSIVE...... PROBLEMS

There was a major fire accident in a bulk drug unit when the reactor, through which materials were being charged through a manhole, exploded. During this process, static charge was generated and the auto ignition thereof led to the explosion, resulting in the debris of the first floor collapsing into the ground floor. As a precautionary and firefighting measure, water was gushed at high pressure into the entire clean room area to ensure cooling of the area and also to ensure that no other equipment catches fire, so that entry into the room can be made safe.

Apart from significant damages to the buildings and plant and machineries, the entire stock in the clean room (batches waiting for processing kept in polybags and HDPE containers in the entire clean room areas on the ground and first floors) housing the reactors were damaged / washed away. Due to the emergency evacuation, the bottom valves of the reactors were left open and subsequently, on account of firefighting measures where water was sprayed with significant pressure, the materials were washed away.

The loss assessment on building and plant and machinery did not have the challenge of assessment of the damaged items and proceeded smoothly once the main and significant challenge of establishing the adequacy of sum insured was skilfully managed.

- Buildings were significantly damaged, requiring substantial civil works, plastering and roofing repairs and related scaffolding works as damaged materials had to be dismantled and debris cleared.
- The insurance renewal was done about a month before the incident, which included discussions on the adequacy of values and should not have posed any issues. When the asset register was scrutinized in detail, it suddenly appeared that there could be an underinsurance of almost 40%, which would reduce the actual claims settlement on the plant and machinery by more than INR 1 crore.
- The insured was establishing another project within the same premises and had invested substantial capital expenditure for the same, for which a separate insurance cover had been taken. It took several rounds of discussions with the technical and accounting teams to sort out the complications in the assets register which involved project costs and capitalization issues and variations in the accounting methodologies before it could be established to the satisfaction of the loss assessor the values at risk and the adequacy of cover.

The stock assessment posed many issues –

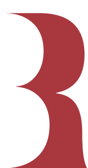
- Material unloading was in progress when the blast occurred due to which the personnel handling the unloading operation had to rush from the clean room area to a safe zone.
- Establishing the quantity through the stock movement and finished goods movement registers was also not possible as the clean room area was also part of the manufacturing process and there was no specific movement register for the clean room to show the extent of material in that block. There was only an overall batch wise inward and outward movement of materials for the entire manufacturing area to show the issuance of raw material to the respective batches.
- Due to the force of the water the materials stored in the bags and drums had split open and were washed away. Even photographic evidence was scanty, as photographs could be taken only after clearance from the safety team, by which time most of the materials were washed off. A significant quantum of material mixed with water flowed into the gutter, as a result of which, establishing the quantity of material lost based on salvage material was not possible.
- The work in process claim was allowed by the Surveyor as, during his visit, he had observed that the stocks that were in process were strewn all around. However, he did not allow for any value for finished stocks as he had not seen the finished stocks and it was difficult to convince him that such a large quantity of finished goods could have been in the process blocks and not moved to the storage area.
- Stocks, being fine powder in nature, were not available as residue / stocks after the explosion and fire. The surveyor started with the presumption that there were no stocks.
- The insured went about establishing the losses in two parts. The first part was establishing the loss from the books of accounts. The quantities of stock available were recorded in the books of

accounts and a comparison of the quantities available before and after the claim event showed that there had been loss of stocks. Secondly, books of accounts were backed up with statutory returns too. However, the surveyor was not totally convinced as he could not establish the quantum of stocks lost from the photos and neither did he have a visibility of the same during his visit immediately after the accident.

- The difficulty was compounded as there was also no movement register of stocks between blocks. The client had some finished stocks stored in the process block, but establishing the quantum in the absence of residue / salvage and inter block movement records, proved difficult.

Detailed physical inspection of the plant by the Surveyor was required to convince him that the normal manufacturing process included purification process which required some of the stocks to be kept in the reactor area and the description of the items in the stock register had to be explained to the Surveyor to his satisfaction.

Detailed plans and storage layout in the process area were also shown to the Surveyor to recreate the stock positions just before the accident.



VENKATESAN K
B.Com, MBA, FIII
Director - Corporate Solutions Group
30 + years in insurance industry – Oriental Insurance Co Ltd, IFFCO TOKIO, SBI General
Involved in providing comprehensive risk management solutions to corporates and customers

BHARAT REVIEW

Every large claim has its set of challenges, both in terms of admissibility and quantum. While loss assessors do have a difficult job in assessing a loss, it sometimes becomes quite difficult to prove and provide evidences to satisfy them. The line between reasonableness and unreasonableness, in many cases is quite blurred, leading to disputes.

The absence of the trust factor between the insured and insurer and the independent loss assessor, many times leads to conflicting positions taken by the concerned parties, ultimately resulting in having to take the dispute to a legal forum.

Fortunately in this case, better sense prevailed and an amicable settlement was reached.

IN THE NEWS

END OF AN ERA

Hyderabad woke up to a part of its history going up in flames as one of India's oldest clubs was destroyed in a massive fire that broke out. Established by the British on April 26, 1878, the 143-year-old Club is said to be among the five oldest clubs of India and was located on a lush green 22-acre campus.

It was a 50,000 square ft. built-up area largely made of wood, so the club did not stand a chance despite fire and police rescue efforts. Within no time, the main heritage building was gutted in flames completely, resulting in the loss of at least INR 35 - 40 crores.

The fire department said that a short-circuit could be the reason behind the fire that started around 2:30 am and was doused by 6 am. No casualties have been reported, officials said. "As many as seven fire tenders took more than four hours to control the flames. Fire department officials said they had to struggle a lot to put out the fire due to the presence of "a lot of combustible material" in the premises. Several gas cylinders are believed to have exploded in the fire.

Source: Media News

LEGAL EAGLE

DOUBLE WHAMMY – THE INSURER'S WAY

A chemical company was engaged in the manufacture of camphor and resin products. The manufacturing activity of the two products were in separate blocks. Due to a short circuit, there was a major fire in the resin plant because of which the power supply to the entire plant was isolated, including the utility area.

Unfortunately, the fire reached the utilities area which was close to the camphor plant and to prevent a major disaster and explosion, the in process material in the reactors of the camphor plant was drained out. The first surveyor visited the plant to assess the loss and he was informed that the restoration of the plant would take more than 9 months and a request for an interim payment to speed up the restoration process was inordinately delayed with two ad hoc payments spread over almost a year.

The insured also requested an extension of time to complete the reinstatement process. More than 18 months after the appointment of the first surveyor, a second surveyor was appointed to assess the business interruption claim, who took a further 14 months to assess the loss.

The insurance company did not settle the claim in full and arbitrarily credited about 50% of the assessed loss to the account of the insured towards full and final settlement and the insured decided to take the issue to a legal forum.

During the legal proceedings, the insurance company filed a return statement that the loss assessment was done in accordance with the terms and conditions of the insurance policy. The insured argued that the surveyor and the insurance company had fixed a notional time period of 253 days as the interruption period citing delays in reinstatement and arbitrarily disallowed the balance number of interruption days. The insured also contended that the indemnity period under the policy was 12 months, and the actual interruption was beyond 12 months and the claim should be assessed for the entire period, as any delay caused in reinstatement was not attributable to the insured.

According to the insured, the so-called delay attributed by the surveyor / insurer was because the reinstatement was not possible as the plinth and foundation of the plant was completely damaged and re-erection of the plant would take substantial time. Disposal of salvage through tendering process took substantial time and the insured had to finally purchase the salvage himself for expediting the claim, which caused a 7-month delay from the date of the accident leaving only 5 months more for reinstatement.

The insured also contended that the loss of gross profit for both the blocks had to be evaluated separately and the surveyor's

assessment which was based on combined gross profit loss estimation was against the terms and conditions of the policy. The insurance company contended that the insured did not maintain segmented accounts for the operations of the distinct plants, although a cost accountant's report showing the profitability of each of their plants was submitted. The cost accountant's report, according to the insurance company, was done only as a one time activity based on arbitrary workings and guess work.

The insurance company also contended that the policy was issued for a consolidated sum insured for all the plants and did not contain department wise sum insured. Interestingly, the surveyor had assessed the loss of gross profit for the damaged plant independently (before changing his stance by issuing an addendum report), which the insurance company contended was an error and the surveyor cannot rewrite the contract for the insurer and the insured.

The reinstatement process, according to the insurance company, was done over a one year period in a staggered manner with purchase orders issued in various months, showing that the insured did not act with due diligence in its efforts to restore the damaged assets and cannot be a ground for claiming a longer indemnity period.

The court perused the various terms of the consequential loss policy, including the alternate basis, departmental and the specification clauses, and concluded that if the business is conducted in departments, the independent results of which are ascertainable, the policy will cover such departmental independent trading results. The determination of gross profit on turnover basis has also been laid down in the terms and conditions of the policy. Thus, the policy issued provides for taking trading results of the department, where the fire had occurred. It is clear that the insured had two independent manufacturing blocks and the fire had occurred in one of the blocks and therefore the loss of profit has to be worked out in respect of the damaged block alone and that too on the basis of the turnover of the damaged block.

The turnover and the gross profit of the other block has no bearing at all and cannot be included or taken into account while computing the loss of profit in the damaged block. The court was in full agreement with the cost and audit report and held that the insurance company was not justified in determining the loss of profit by combining values for both the blocks.

Interestingly, the insured had also filed a separate case for a dispute for the material damage claim. The total claim was for about INR 30 crores. As normally happens in any large claim, multiple iterations of the claim between the surveyors and the insured were done and finally the surveyor issued survey reports assessing the loss at about INR 18 crores. As the insured was challenging the final survey report based on several discrepancies in the report, the insurance company credited and amount of INR 8 crores as full and final settlement over and above INR 2 crores paid as on-account earlier!!

The Court held that the total claim after deduction and excess came to about INR 26 crores and directed the insurance company to pay the balance to the insured.

The Court disagreed with the deductions which were made by the insurance company on the following grounds:

- A substantial portion of the claim was towards the draining out of the work in progress to prevent a much larger loss which the surveyor had allowed as loss minimization expenses. The insurance company argued that the stock was not affected by the fire but due to the shutdown of the common boiler and the damage to the stock in process was attributable to spoilage due to retardation of process, which is a consequential loss and an exclusion under the policy. The insured contended that the loss was a result of fire mitigating process, which was also a contractual obligation as per the terms and conditions of the policy. The insurer added that the description in the policy and the assessment by the surveyor was under work in progress, whereas the material was actually finished goods!!

- The Court agreed with the insured that had they not taken the measures of draining out the material, the fire would have spread causing massive damages and the insurer would have had to pay a much higher compensation.

- The insurer also took a stand that a portion of the claim was not payable as it fell under the electrical exclusion clause of the policy, which again was not the opinion of the surveyor who had assessed the loss. The Court did not see merit in the argument of the insurer.

- Interestingly, the Court also held that the acceptance of the lower settlement by the insured by way of a consent loses its significance for the simple reason that the insurance company did not accept the loss / damage assessed by the surveyor.

The Court directed the insurance company to pay the disputed amount of more than INR 16 crores to the insured.

BHARAT REVIEW

In any large claim, the war of attrition (initially between the insured and the surveyor and during the concluding phases joined by the insurance company) ranges, as the saying goes, from the "bizzare to the ridiculous". Once the dispute is expected to go to Court, the stand on exclusions and quantum of claim has to be seen to be believed!!

As we have been repeatedly emphasizing, the purpose of insurance is defeated if the claims settling process is not quick and reasonable. This is especially true in a large accident when the financials of the insured are strained, and the expectation is that the insurance protection would come to their rescue.

The standardized and simple claim settlement process which has been more or less working well in the Motor and Health channels lulls the corporate enterprise into believing that the same would be possible in the event of a fire or a flood claim.

Having witnessed numerous instances when this belief turns to exhaustion, frustration and despair in the midst of an prolonged claim settling process, the only thing that we can say is the cliched "Buyer Beware".

RISK MANAGEMENT - IN THE NEWS

CYBER RISK AND CORPORATE ATTITUDE

Murder on the Internet - Story of Hosting Company

The demise of a Software as a Service (SAAS) company at the hands of an attacker shows that, in the cloud, off-site backups and separation of services could be key to survival.

This was a company that offered developers source code repositories and project management services. It had been going for seven years, and it had no shortage of customers. But it's all over now -- the company was essentially murdered by an attacker.

The SAAS provider acted as a hosting service where they host millions of lines of code developed by software companies to be released to the principals once they make payment to the software company. They were using the cloud web services of a famous service company on cloud platform. The SAAS provider had a dashboard access to their entire operations, as provided by the Cloud service provider.

SAAS was hit by a DDoS (distributed denial-of-service) attack and the unidentified attacker had also gained access to the cloud service control panel, and demanded payment of a ransom to resolve the DDoS attack. The company then changed its password for the control panel, but the hacker had already created several backup logins, "and upon seeing us make the attempted recovery of the account he proceeded to randomly delete artifacts from the panel," the company stated on its website.

"We finally managed to get our panel access back but not before he had removed all EBS snapshots, S3 buckets, all AMIs, some EBS instances and several machine instances," SAAS stated. "In summary, most of our data, backups, machine configurations and offsite backups were either partially or completely deleted."

However, in a simple way one can view this event as strictly a security failure. The SAAS admin were also guilty of violating the backup administrator's rule of 3-2-1, which requires three copies of any piece of data, on two different media with one offsite. They also did not have multi-factor authentication which could have made it that much hard for anyone to breach. They must have been thinking they are 100% safe since they are entirely on cloud and there is no on-premises risk exposure for their own servers.

Within 12 hours, the SAAS company went from a viable business to devastation!!

Duped Beyond Belief – Story of an EPC Company

What does it take to be duped into paying not just one or two crores to hackers but a whopping INR 130 Crores in three tranches within one day !

A group of Chinese hackers robbed 1.3 billion rupees ($18.45 million) from the Indian unit of a technology driven EPC contractor through an elaborate cyber fraud that included impersonating the Italian engineering firm's chief executive.

The fraud, reportedly an act of Chinese cybercriminals used fraudulent phishing emails, in an attempt to obtain sensitive information such as usernames, passwords and credit card details by sending phony emails.

The EPC company is a subsidiary of a large MNC business conglomerate in Italy. They are in into the business of providing Engineering services.

Chinese fraudsters had originated emails to the CMD of the subsidiary company in India from an email account that appeared similar to the email of the group Chief Executive Officer. They didn't stop there – they also arranged conference calls to discuss a "confidential" acquisition in China instructing the Indian subsidiary's CMD not to discuss with anyone else.

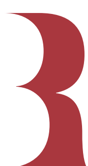
During the conference calls, various people in the hacking group pretended to be the CEO, senior executives of the company and a top lawyer based in Switzerland, and managed to convince the CMD of the Indian subsidiary that funds needed to be transferred from India-based accounts of the company due to regulatory issues in Italy.

Since the discussions involved Group CEO from Italy and detailed instructions were given on a call by their General counsel, the CMD of the Indian subsidiary arranged for transfer of US$ 18.8 Million (> INR 130 Crores) in three tranches - USD 5.6 million, USD 9.4 million and USD 3.6 million - to bank accounts in China and Hong Kong. The hackers withdrew the money in a matter of minutes.

The affected company had launched a forensic investigation into the fraud and had employed legal and security firms to look into the matter. The company has also hired services of a white-collar criminal law and fraud investigating company. Investigations revealed that all those on conference calls had sham identities and the top Swiss lawyer doesn't exist. The bank accounts into which the money was sent were opened using bogus documents. The company has since fired its India chief and the head of accounts and finance.

BHARAT REVIEW

No business should take their cyber risk exposure for granted. They should build adequate safeguards, risk mitigation measures and redundancies to ensure that even if the worst happens, they would be able to be back in business quickly and without much of a financial loss or expense. Ofcourse, a cyber insurance with well designed terms and adequate limits is a must in today's virtually connected business environment.



T. L. ARUNACHALAM
B.A, B.L, AIII
Director & Head - Cyber & Emerging Risks Practice
30+ years of experience in insurance industry, worked with New India Assurance, IFFCO – TOKIO, and comes with international exposure. Specialisation in Marine and Liability insurances, including cyber risks.

SIMPLE POLICIES......... BIG CHALLENGE

Bharat RE has been predominantly a Corporate Broker, and we have always been highlighting the complexities in handling commercial claims. However, issues even in policies that we think are simple like a Motor and Health policies are quite common and the message of "Buyer Beware" is universal.

TRANSPORTED TO.............HELL

The client had driven a Skoda from Delhi to Goa and for the return journey had booked the car with a transporter to be delivered at his residence in Delhi, which normally takes 10-12 days from the date of picking up the car.

Ten days later, as the car was not delivered, the client had called the transporter who stated that there was a delay due to intercity covid restrictions on transportation. Finally, when the car was delivered a month later, the vehicle was received by the domestic help who had informed the owner, who was travelling, that there was no outward damage but informed that the transporter had mentioned that the battery was completely discharged.

When the owner of the car returned, he noticed that the fuel tank was empty and the car had been driven for 335 kms and the warning lights were flashing. The car was taken to an Authorised Service centre, who suggested the callipers to be changed and would inspect the car thoroughly. Until then, it was deemed to be a routine check up.

Subsequently the service centre informed that the car had been involved in an accident and there were several damages to the suspension, braking systems, electronics functioning and the airbags had also been deployed. When the client visited the workshop, they showed him how the car had been repaired cosmetically in an attempt to conceal all external and visible damage and enough repairs to make driving possible. Their estimate of the repairs was around INR 10 lakhs.

On repeated queries to the transporter, he finally admitted that the carrier truck met with an accident in transit and around 7-8 cars were damaged while unloading after the accident to the truck. The cars were then taken to a local mechanic shop to cover up all visible damage.

The client tried to lodge an FIR in the local police station which was declined as it was outside oftheir jurisdiction. So, a complaint was lodged on the transporter which was accepted, and the police officer verified the same with the transporter including that no official recording of the incident had been made at the accident site.

When the claim was intimated to the insurance company, the claim was repudiated on the following grounds

- Delay in intimation of the claim which is a violation of policy term & condition
- The nature and cause of damage is not a covered peril under the motor policy.
- Vehicle damage in custody of transporter during transit is an exclusion as it arises out of contractual liability.
- Also, there is a non-disclosure of material fact and breach of good faith.
- Vehicle was already dismantled / repaired prior to inspection leading to violation of policy contract.

The insured contended that the damages were so well concealed by the transporter that even the authorized service centre was unable to detect the extent of damages in the initial inspection. Once the extent of damages was known the insured had taken all efforts to take up the matter with the transporter and had done so.

When the fact of repair itself was not known to the insured, it is absurd to expect him to intimate the insurer of the accident / repair and provide them with an opportunity to inspect.

The efforts to convince the insurer on the unreasonableness on their stand failed and the claim was not settled and is being pursued legally.

AT THE LAST MINUTE...............

An insured had already utilized a portion of the sum insured for various illness under his health insurance. He was hospitalised again and the balance sum insured was enough to cover less than 50% of his hospital expenses. In the present case, the insured was hospitalised a half an hour before the expiry of the policy.

The insurance company had rightly quoted the terms and conditions of the policy that stated that if the admission period is spread over 2 policy periods, the insured is eligible to claim only the sum insured in the policy which was active on the date of admission.

Fortunately, the insured had renewed his policy before the due date. The standardisation of the health insurance terms and conditions brought in by the Regulator in 2016 clearly provided that if the claim event falls within two periods, the claims shall be paid taking into consideration the available sum insured in the two policy periods, including the deductibles for each policy period. Such eligible claim amount to be payable to the insured shall be reduced to the extent of premium to be received for the renewal/due date of premium of health insurance policy, if not received earlier.

When this was brought in to the notice of the insurance company, and with a little bit of persuasion the insurance company settled the claim.