For Private Circulation Only V1 – I28 – 01 2021

# RISK ALERT

Newsletter from India's Leading Insurance Broking Company

bharat RE™

## HIGHLIGHTS



## IN THE SPOTLIGHT


As we move into the calendar year 2021, the first nine months of the financial year 2020-21 has been challenging, to say the least, dominated exclusively by the Covid 19 pandemic with lockdowns and related human and economic consequences, while we hope the worst is behind us as we get into the fourth quarter.

The insurance industry, also had its challenges with substantial drop in premium especially in the Motor insurance sector, due to negligible sale of vehicles and drop in renewals, during the lockdown, which was to an extent offset by increase in medical insurance premium, especially in the stand alone health sector.

From the commercial insurance point of view, a seemingly innocuous condition in the property insurance policies called the "unoccupancy clause", which states that the insurance coverage will be suspended if the premises covered under the policy is not occupied for a continuous period of 30 days or more, created a lot of panic and confusion among the corporates with the insurers and reinsurers giving complicated and often contradictory clarifications and guidelines from insisting on written approval and endorsements in the policies to prescribing various do's and don'ts on safety and security procedures. The General Insurance Council had to finally clarify that coverage will continue without any requirement for communications and endorsements but still ambiguities continued during the period regarding engineering policies and fire coverage under package policies.

Unnecessary hair splitting by the insurance industry compounded probably by the main reinsurer not taking a clear stand on the issue created anxious moments for the corporates and also undermined the credibility of the insurance industry with the insureds.

The other major point of debate was the coverage for Business Interruption during Covid 19, the Indian policies clearly required Material Damage as a prerequisite to claiming Business Interruption. Policies issued worldwide were not so clear and a flood of lawsuits are in various courts with differing judgements being pronounced. We tend to look at the insurance policy as a kind of a versatile agreement with the insurance company provided by "friendly" relationship managers, giving an impression that every issue can be sorted out to the satisfaction of the insured in the event of a claim. A yearly renewal and probably a long standing relationship with the insurance company again gives a false sense of security to the commercial enterprises that things will be decided in their favour when a claim arises!!

Every major claim (fortunately not very common, but, at the same time can happen to anyone!!) invariably gets into issues from admissibility to interpretation of the policy terms and conditions,leaving the insureds frustrated and fatigued, and exposing the difference between the expectation and reality!!

**Vijay T**
AICWA, 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

# COLLAPSE OF THE CROWN!!

A portion of a crown of a 265 TPD (tonnes per day) furnace for producing packaging glass suddenly collapsed. After normal maintenance repairs of the furnace, it had been heated to $900^0$ C over a period of 9 days. The production process was started with cullet charging over a period of 2 days and temperature was increased to $1500^0$ C when the crown collapsed.

As expected, the loss assessors quoted the workmanship and material defect exclusion in the policy and a Root Cause Analysis (RCA) was inevitable. Investigating the cause of damage, an expert went into the RCA and ruled out:

- Overheating of the super structure of the whole smelter and crown, as the data from Scada showed the temperature was below $1600^0$C, which is normal.
- Possible failure in controlling the expansion of the crown made of silica, as the expert found that the crown movement was properly adjusted by the bolts and performed by experts in the field.
- Poor quality of crown material by testing the silica profiles in a lab in Germany and finding the same within acceptable parameters.
- Poor quality of workmanship as the undamaged portion of the crown did not show any abnormalities in laying of the refractories. An endoscopy report also confirmed the same.

A further study of the Endoscopy report of the damaged portion of the crown refractory showed localised heating indicating excessive fire from the burner. This was possible due to flame from the burner touching the bricks or change in fuel characteristics or change in combustion property.

Change in fuel or combustion property was ruled out by checking the fuel characteristics and the absence of a sudden drop or increase in temperature in furnace negated the possibility of change in combustion property.

The cause was narrowed down to the burner issue and after detailed analysis of the log book etc..it was discovered that an engineering team had fixed a cooling duct problem just before the collapse. They may have accidentally disturbed the burner angle causing the flame to hit the crown resulting in localised heating and collapse. This was further corroborated by the insulation dropping inside the melted glass being noticed in the analysis of the endoscopy report.

The course of repair and replacement was tricky as the silica drip erosion was continuous and it had weakened the entire crown at both the side and front wall areas with the distinct possibility of an abrupt catastrophic failure of the entire furnace.

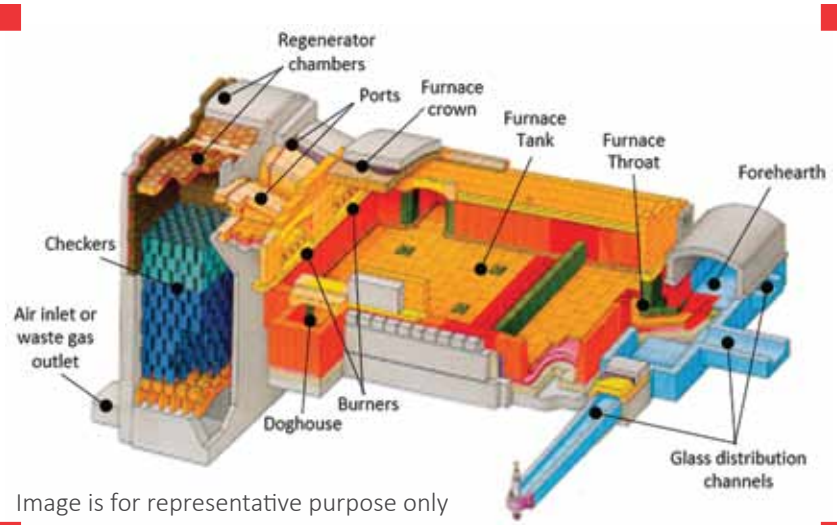
Considering the above, the experts decided to go in for “hot repair” in the running furnace as a temporary measure and then for “cold repair” after the furnace was shut down. The cost of hot repair was about 30% of the cold repair.

The surveyors refused to pay for the first hot repair stating that they cannot pay twice for the same repair. The insured contended that the hot repair was like a temporary first aid andstabilisation, without which there could have been a catastrophic failure of the furnace and the cold repair was the actual repair. Fortunately, an add on cover under the policy recommended by Bharat RE saved the day and the surveyor found it difficult to push this argument beyond a point.

The next contention by the surveyors was by citing another exclusion under the policy which excluded testing risks. They contended that the accident happened after staring up of the plant after maintenance repairs and the furnace was still under the testing phase. The insured showed that the furnace had reached full production temperature 2 days before the accident and raw material feed and output of finished goods were already underway when the accident happened. Also, in an operating furnace, some maintenance repairs or the other are always carried out which cannot be considered as testing.

In a claim situation, nobody gives up easily!! The insured out of necessity and the surveyor / insurance company because it holds the cheque book!! The quantum of repair cost included significant amount of technical supervision fees running into crores, as this is a specialised field with very few manufacturers / repairers available. The cost and number of man days were hotly contested and finally a negotiated settlement after prolonged discussions was agreed.

Apart from the issues on the technical aspects and policy interpretations, another major roadblock on the adequacy of sum insured had to be skilfully navigated to ensure fair claim compensation.

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# BHARAT REview

Any large claim in today's environment becomes a game of chess and the exclusions under the policy are moved by the surveyors leaving it to the insured to counter them.

Interestingly, the initial claim after the first assessment by the insured was about 3% of the final claim settled. Every claim situation has its complexities and involves technical, commercial and insurance issues to be handled.

As we always say, if you are a lawyer, commercial and technical expert and an insurance expert all rolled into one, you, as an insured, can hope to take the claims settlement to its logical conclusion. If not, leave it to us!!

The Claims Team

**Minesh Patel** - B.E (Electrical), AIII (Fire). Sales Engineer and has been in insurance sector for more than 15 years. Specialisation in customizing insurances for Chemical and Engineering industries

**Kishore Hegde** - B.Com, C A., Proficiency in spearheading initiatives encompassing business valuation, financial analysis, taxation, due diligence, regulatory processes & financing. More than two decades in the Financial and service industry

## CLAIMS ANATOMY

# BUSINESS INTERRUPTION – LENGTH……..Y PROBLEM

A sizing machine was damaged in a fire accident. While the Material Damage assessment was relatively straight forward, the Business Interruption claim was tricky, with several factors complicating the assessment.

- The unit had several sizing machines which were not processing the same kind of yarn with some of them processing finer counts and others coarser counts. The sales realization for finer counts was much higher than that for the coarser counts.

- The damaged sizing machine was primarily processing finer counts and accounting for 40% of the capacity of the sizing block. Post the accident, the output in quantity was maintained by both increasing the output to the extent possible from the other machines, and also mainly from the outsourcing of the sizing activity to third parties.

- Even though the output in kgs was maintained, the profit for the company was much lower as the overall realization on the output had come down drastically.

- Apart from the production quantity being maintained, the sizing machine which was damaged was processing about 40% of the capacity of the sizing block. The trends of production in the few months before the accident were showing an upward trend. This increased trend would have had to be factored in while arriving at the loss, if the insured had to be adequately compensated.

- Interestingly, the bottleneck in production was not the capacity of the sizing machines but the availability and management of beams which are loaded on to the sizing machine. Since many of the beams had to be handed over to third parties to produce the sized material, the beams in the factory to carry out the production in the rest of the sizing machines which had not been damaged were not adequate, resulting in the reduced efficiency of the entire sizing department, which also affected the overall realisation.

- The entire beam management system had to be recreated and explained to the loss assessor as, in the current situation, the quantity produced was in fact more than the production before the loss and the loss of one machine theoretically did not hamper the overall capacity.

Most Business Interruption claims involve a lot of subjectivities as the insured and the loss assessor need to arrive at the loss based on historical data, which is then adjusted for trends to arrive at the loss the insured has incurred because of an accident. In this accident, the assessment was further complicated by multiple factors, which had to be looked at in totality to arrive at the actual loss for the insured.

The Claims Team

**C. Ramachandran**
B.E. (Civil), AIII
Technical Director
Risk Engineer in New India - pioneered the corporate consultancy business in the late 70s and early 80s. With specialisation in Engineering, Projects and Textiles.

IN THE NEWS

# LIGHTNING DOES NOT STRIKE TWICE OR DOES IT??

A massive fire gutted an entire manufacturing facility of a sanitary products maker which is an Indian arm of a Japanese conglomerate. The massive fire raged for more than eight hours and destroyed the facility which was spread over three lakhs sq meter and had a market share of almost 35-40% of the Indian market.

The fire is believed to have originated due to a short circuit at one of its storage areas which quickly spread to other areas.

The loss is estimated in excess of INR 1000 crores. Interestingly, the same insured had a massive fire three years back in another location with the loss estimated of around INR 700 crores.

Source: Media / Internet

## BHARAT REview

We understand that the previous claim has not been fully settled and another large claim is sure to test the insured and the insurer to the fullest!!

The objective of insuring the assets of any commercial enterprise ideally should be with an expectation that in the event of an accident threatening the survival of the enterprise, the insurance compensation is received in a timely and reasonable manner.

Regrettably, the intense competition to write business at any cost and the focus of commercial enterprise owners or their finance team on pricing has made the claims process difficult and complicated.

The recent increase in the property insurance pricing, though unwelcome to the insuring corporate world, would in our opinion, significantly improve the loss paying appetite of insurers.

IN THE NEWS

# GAS LEAK IN VIZAG

More than 800 tonnes of Styrene, a gas which is hazardous and can cause respiratory illness and skin irritation, had leaked from a plant recently. The gas leak caused the deaths of as many as 12 people, and hospitalisation of hundreds. The concentration of Styrene in the air was beyond hazardous levels at 461 ppm on the day of the leak, 374 ppm after over 24 hours after the disaster.

The Joint Committee probing the Styrene gas leak pointed out that

- There was only one temperature monitoring guage at the bottom of the tank, and absence of any interlock system arrangement between the temperature monitoring and refrigeration systems, and no external water spray arrangement over the tank in case of temperature increase.
- Water sprinkler system was not automated and manual sprinklers could not be accessed as the controls were in the hazard area, a similar problem was with the alarm

system which was also not automated. The unit could not ccess personal protective equipment which revealed the lack of safety preparedness.

- Chiller system was switched off the previous evening as part of routine maintenance and no temperature or pressure monitoring was done at the middle or top of the tank where space is left for vapourisation, found the committee.

- In addition, the report also pointed out that TBC (Tertiary Butyl Catechol) which is an inhibitor chemical to slow down the reactions, was not topped up since there was no TBC stored at the site.

- Even as basic safety protocols were not followed, the response of the officers and workers present at the factory to the gas leak was also slow. There was a time lapse of almost an hour between the gas detector alarm noted by the control room and to reach the fire hydrant sprinkler valves. The sprinklers could not be activated as they were within the hazardous vapour zone.

It was more than 1.5 hours after the gas leak was detected, that personnel wearing safety SCABA equipment were able to start the sprinkler system. By the time the pumping of emergency chemicals to stabilize the tank started, over 800 tonnes of gas had already leaked.

## IN THE NEWS

# CRASH OF THE CRANE IN VIZAG

A 70 tonnes crane collapsed in Vizag killing 11 persons when it was being taken for a trial run for a distance of 30 meters.

An expert committee that was set up to probe the crane crash has found that structural and design issues are the reasons behind the mishap.

The entire mishap took place in less than 10 seconds, as the link between the gears and disc brake along with the electric hydraulics failed, resulting in breaking of basement bolts and leading to the tilting of the crane. The automatic system which backs up during the technical break down was also said to have failed. The committee has also found that the crane had no proven track record.

The original supplier, who was to operationalise the crane in 2010 backed out from the project. Another agency was entrusted with the operationalisation of the crane only in 2020.

The company did not provide a design manual for the crane, the panel found, and added that four bearings, including central bearings, were damaged, triggering the collapse.

# BHARAT REview

## Do we lack a safety culture?

These recent accidents in Vizag have again shown that the safety and risk management culture in India probably has a long way to go!!

Risk awareness and safety culture has never been a part of our daily routine and without doubt, gets extended to the work environment also. Every accident invariably shows the lack of this and we tend to gloss over the disease by focussing only on the symptoms manifested in an accident and the resultant investigation report.

At the same time, not all accidents happen only because of negligence or absence of safety and risk management protocols not being adhered to, which is why a well designed insurance program is of critical importance.

# LEGAL EAGLE


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The insured was an SME unit engaged in the manufacturing and refining of oil. The raw material for the process used was lubricating oil which was received in barrels and stored in the open yard. Apart from this, oil was also brought in and unloaded into oil pits. The finished product which was refined lubricating oil was either directly loaded into oil tankers or filled in drums and kept in the open. The part of the plant which was in the open was engaged in processes like centrifugation, settling and decantation, dehydration, condensation and treatment of volatile materials. The part of the plant which was in the closed shed was involved in the less hazardous processes like clay treatment and neutralisation, filtration, blending etc.. The shed also included thermic fluid boilers, water softening plants etc..

The assets were insured under two Fire policies. When the Bankers to the insured were changed, the policies were shifted from one insurance company to another. During this process, the insured alleged that an officer of the insurance company brought two proposal forms for Fire insurance and got those signed by the insured, with no details filled in. He also took with him the photocopies of the expiring policies which had been with another insurer and he had also inspected the plant before giving the premium rates. When the policies were issued, the location of the property was mentioned as "factory-cum-godown and office premises", though there was no godown in the factory premises.

The entire factory premises including the assets in the open were completely destroyed in a fire. A surveyor was appointed and during the course of assessment he indicated to the insured that they had been instructed by the insurance company to assess those assets only in the covered shed and not to assess loss to the assets in the open part of the factory premises.

The insured contended that from the very beginning of the policy, they had requested the insurance company to amend the policies by a written communication, wherein they had requested for these changes and had also asked for the name of the Bank that financed the assets to be changed, as it was mentioned incorrectly in the policy.

The matter was taken to the National Commission and the Commission, after considering the matter, took the view that the factory premises included all assets inside and outside the shed areas, by relying on the definition of the factory as given in the Factories Act, 1948. The Commission also observed, as per the guidelines in settling the claims, that 75% of the loss should have been settled. Interestingly, both the insured and the insurance company were not happy with the order – both filed appeals to the Supreme Court. The Supreme Court disposed off both the appeals by a common order.

The main point of dispute was whether, as per the terms of the policy, all the goods which are lying within or outside the shed are covered under the policy or not. The court looked into the definition of factories under various statuettes and opined that the definition has to be construed in the context in which it is used. The Supreme Court, while agreeing that though loosely the expression "factory" may include the whole premises of the factory, the expression "factory – cum – godown" has to be read in the present context with the other conditions that appear in the policy document. The proposal form had a specific question whether the goods are stored in the open or whether there is any kutcha, timber / thatched building to which the answer was negative. Therefore, what was sought to be insured was plant and machinery within closed premises – and it is clear that goods lying outside were not insured. If the intention was to insure the plant and machinery and stock in open, the answer to relevant questions in the proposal would have been given by the insured.

Both the parties have executed the contract and the insured made a disclosure in the negative that no goods are lying in open or kutcha shed. That shows that the goods lying in the covered area were only insured and none else!!

The court observed from earlier decisions that ***"In interpreting documents relating to a contract of insurance, the duty of the court is to interpret the words in which the contract is expressed by the parties, because it is not for the court to make a new contract, however reasonable, if the parties have not made it themselves."*** Also, ***"The insurance policy has to be construed having reference only to the stipulations contained in it and no artificial farfetched meaning could be given to the words appearing in it."***

The court finally stated that the terms of the contract should be construed strictly without altering the nature of the contract as it may affect the interest of the parties, adversely. The court also observed that when the policy was issued, the insured wanted some amendment in the policies including the point that there was no godown in the premises.

The insured contended that they had asked for amendments in the policy which, if implemented, would have covered the assets in the open also, and they had also clarified on the fact that the occupancy description in the

policy was wrong and had asked to be amended. The court viewed the issue as

- When the terms of the contract have been reduced in writing it cannot be changed without the mutual agreement by way of both the parties.

- If the complainant was vigilant and wanted this expression to be deleted he should have prosecuted the matter seriously or repudiated the Policy.

- The only defence pleaded was that they were assured orally but no evidence was led by complainant. On the contrary, suggestion was denied by single witness produced by the Insurance Company before National Forum.

- Therefore, in the present case when the proposal was sought to be amended and it was only agreed to by the Insurance

company to the extent of substituting the Bank and the other amendments were not agreed by the Insurance Company, the complainant had a choice to repudiate the insurance policy or to obtain a proper declaration. But the complainant did not pursue the matter further, it is to be blamed itself for this. the outdated design

## BHARAT REview

Insured tend to take proposal forms and declarations quite lightly, not realising that they form part of the insurance contract. In many cases, inadvertent or casual information in these forms and declarations leads to disputes and denial of claims.

We are quite used to signing blank proposal forms and documents for many of our transactions, and carry the same attitude to insurance also. While this may not be of much significance in other areas, it could make the difference between settlement of a claim or denial, when it comes to an insurance contract.

In the judgement highlighted above, the Apex Court has ruled that an insurance policy is a contract, and after the contract is entered into, no alteration can be made except by mutual consent. They have also clearly stated that contracts have to be interpreted strictly.

*Nowhere is Buyer Beware more relevant than in an insurance contract.*

## 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 policy or an Overseas Medical Policy are quite common and the message of “Buyer Beware” is universal.


A 75 year old individual had taken an Overseas Mediclaim Policy (OMP) with a private insurer. He passed away due to Cardiac Arrest in London. The family incurred an expenditure of more than Rs.3 lakhs towards Ambulance charges, Embalming and also towards repatriation of the remains. Most of the OMP provide cover for repatriation of remains. However this policy provided for this cover only if the expenses were incurred because of an Accident and not an illness!!

When other OMP issued by other insurers were reviewed for the same cover, most of them provided for these expenses, irrespective of whether the death was due to accident or sickness / disease.

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One of our clients had a fire damage total loss claim for a mid-range luxury car with Insured’s declared value (IDV) of Rs.24 Lakhs, as per the policy. The vehicle was insured with one of the large private sector insurers. The insurer made a subjective and partial offer to settle the claim for a much lower value in spite of the fact that the concept of IDV should get the full amount mentioned in the policy for a total loss claim. The Insurer argued that the value of the car based on market price is much lower than the value declared in the policy and they would settle only for the lower value, so that the insured should not make profit out of a loss.

It involved series of discussions and references to Circulars from the regulator to get the insurer to settle at the IDV.

## RISK MANAGEMENT

# DISCLOSE .....TO CLAIM!!

Corporates and business entities have been facing the challenges in keeping abreast of legal changes and also to comply with law. As the law is evolving the pressure for compliance is directly on the people in Management of the organisations.

While realising the legal obligations in terms of compliance with plethora of statutes under which companies operate, CXO-s have also appreciated the role and relevance of Directors and Officers Liability insurance policy which provides indemnity for any legal liability faced by the insured, arising from government, regulators, customers, suppliers, employees etc for a decision by the CXO due to which they feel affected or aggrieved.

The key issue is to capture and report facts and circumstances to the insurance company within time and to the right measure, which has often been overlooked by the policy holder, leading to difficulties in the claims process.

A large textile manufacturer in the West had actually procured D&O Liability insurance for protecting their directors and officers. Surprisingly one day they received a notice from Ministry of Corporate Affairs listing out about 20 violations which were identified during audit of their annual returns submitted a few years ago.

The Insured did not realise that this is a circumstance to be informed to the D&O Insurer. They engaged a consultant and commuted 10 out of the 20 charges and paid a commutation amount of Rs.5 Lakhs.

Meanwhile their D&O was renewed over the next two years and they did not inform this development to their brokers or insurers. They had answered a relevant question about any fact or circumstances that may give rise to a claim with "__".

Two years later they received one more reminder letter from Registrar of Companies (ROC) having jurisdiction seeking their explanation for the balance 10 points which had some serious charges. This time the commutation amount indicated by ROC was Rs.50 Lacs.

The claim was reported to the insurer but after reviewing all documentation, the insurance company decided to reject their claim because this event originated in 2017 and right till 2019 they did not disclose this event to the insurer immediately on receipt of notice from Government and not even in their renewal proposal form submitted on two consecutive renewals.

A company in retail garment sales, had put up their product information online to promote sales. Suddenly one day they received notice from Legal Metrology Dept of state government initiating legal action for not displaying the online price as MRP – Maximum Retail Price. The violation called for a large fine. The insured, who had taken a D&O Liability insurance policy, remembered that this is a circumstance to be reported to the insurer and called their brokers immediately. The insurer admitted this as a valid claim.


**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.

**BHARAT REview**

Keeping the insurer informed of the facts and circumstances that may trigger a claim is an essential requirement of an insurance process, especially for Liability covers.

Not disclosing information, even if inadvertent, will be an issue in claims and renewal processes which is best avoided. Creating awareness of complete disclosure requirements with the finance, legal and operational departments, will ensure real time information flowing to the insurer and preventing issues in the claims process.