Tricky Matters

Contents

Introduction

This book highlights a range of cover issues that may present problems when an insurance claim is made. All the examples have arisen in actual claims – the issues raised are practical and topical.

The content will appeal to a range of insurance professionals, including underwriters, account executives and those involved in business development – many of the examples can assist when prospecting.

We hope that the examples are thought-provoking while being easy to dip into. For more detailed technical discussion, please feel free to call me in the first instance and I will put you in touch with the appropriate vrs Vericlaim expert.

Damian Glynn
vrs Vericlaim UK Ltd
Birmingham Office
T: 0121 200 8680

January 2011

IT Maintenance Agreements

Many businesses have maintenance programmes in place with their IT suppliers, who will commonly also supply their hardware.

If a claim is submitted following theft (which might have involved dozens of pieces of kit) insurers will want to use preferred suppliers. The maintenance provider may disown equipment sourced and configured by others – there may be difficulties with the maintenance agreement going forwards.

Why not agree, before any loss is suffered, that the customer's usual IT provider will be used, subject to the business paying the normal prices charged when insurance is not involved?

Re-instatement

Re-instatement does not have to take place in exactly the same form or even on the same site.

It does have to take place within a reasonable period, and many UK policies require re-instatement in this country.

Why not take advantage of a disaster to expand or re-focus a business?

To avoid unnecessary complication, settle the Business Interruption claim early if time is being taken to consider the longer term – a lack of discussion with loss adjusters may raise concern that there is failure to mitigate loss, and this can raise policy issues.

Running the Claim

When an insured event occurs, it is natural for the directors of a business to devote resource to the claim.

However, it is easy to lose perspective – running the claim may take over from running the business. Even running today's business may not be enough – R&D and tomorrow's business may be just as vital.

Most businesses that become insolvent after an accident do so after expiry of the Maximum Indemnity Period. It will help to have a project manager running the claim, leaving the directors to run the business (and mitigate the loss).

Has a director recently retired who can be earmarked in advance to fulfill this role (with the cost being dealt with as an Increased Cost of Working)?

Plant – Indemnity Cover

It is common for some businesses to buy second hand plant. The amounts paid are frequently then used as the basis for a re-instatement sum insured.

The replacement cost as new might be significantly higher than the second hand value and under-insurance may arise.

This is not just a material damage issue.

If under-insurance does arise, and there is delay in finding an appropriate second hand asset (as opposed to buying a new one, if that is faster) any increased BI loss may not be covered by the policy.

This problem can also arise if plant is insured on an indemnity basis and a second hand replacement cannot be found. Any exacerbation of a BI claim may not be covered.

Customers' Goods

Customers' Goods claims can be difficult. Just because a business has insured those goods does not mean that they have to claim for them, or to pay the customer for them in the absence of any negligence on their part.

Where does the sum insured come from?

Customers are unlikely to have given indicative valuations pre-incident. A separate limit of indemnity, rather than a sum insured subject to average will avoid under-insurance complications in the event of a claim.

Declaration Linked Policies

It is difficult to see why a business would want to buy a non-Declaration Linked policy, given the modest (if any) premium implication.

A Declaration Linked policy does not allow for any proportionate reduction if the sum insured is too low. This might lead to BI sums insured not fully reflecting the value at risk.

Legal opinion suggests that a significant under-declaration can constitute a breach of Utmost Good Faith and make the policy (including the MD) voidable. There have been differing views as to whether such significant under-declarations need to be deliberate or not.

Why not obtain copies of a client's profit and loss account every two to three years to sanity check the declared amount?

Books and Records

Books and Records are frequently under-insured. Following smoke spread, it can cost £1200 to decontaminate one filing cabinet drawer full of papers. For a large office, the value at risk can rapidly challenge the whole contents sum insured, particularly when the clerical time to recreate electronic records is included.

Solicitors, accountants, and other professionals can also have expensive collections of technical reference works purchased over a number of years.

It might be better to insure books and records as a separate item subject to a limit of indemnity (not subject to average).

Listed Properties

The sum insured on a listed building needs to be at least 125% of that for an unlisted property. All manner of unforeseen additional costs can arise, particularly for grade 1 or 2* properties.

Given the need to liaise with heritage bodies and others during re-instatement, any business conducted from the premises will suffer extended periods of interruption – a Maximum Indemnity Period of two or three years is advisable.

Maximum Indemnity Period

Many policies are still issued with a 12 month Maximum Indemnity Period.

This is likely to be too short. Allowing for planning complications, etc, buildings can easily take 10 months to re-instate. Only two months then remain to build turnover back to its pre-incident level.

Reliance on key assets, customers or suppliers can all result in extended periods of loss.

Historically, the business interruption risk could be assessed with reference to a company's own assets. Today the assets of partners in the supply chain can be at least as relevant. The fragility of the supply chain supports longer Maximum Indemnity Periods.

Remote Archives

Many businesses use off-site archive stores. These are usually for documents or other assets not in current use.

Contents covers are frequently extended to cover assets at such locations.

Bear in mind, however, that there will not be any business interruption cover if those locations burn down, unless the definition of Premises has been extended to include them.

This can be particularly relevant where off-site stores are used for temporary safekeeping, and the assets involved have an ongoing use to the business.

Component Sets

It is not uncommon for a business to have a number of component stores at different locations.

If a warehouse burns down, the damage to the component stock therein, and the business interruption loss relating to the whole product would be dealt with by Insurers.

However, if the destroyed components represented one half of matching sets, and the corresponding parts intended to be assembled with them were not damaged, no payment would be made for the latter.

The cost of producing the undamaged parts may have been wasted, but that would not be a loss that the policy would respond to.

Defining Gross Profit

It might be imprudent to deduct from Revenue as many uninsured working expenses as many businesses select. Even Purchases might not reduce in line with turnover.

A business may have legally contracted to buy crops in advance even of planting from a farmer. If that business suffers a fire, it will still have to pay for its raw materials.

Other businesses may utilize raw materials in restricted supply, and may need to continue to buy them after a fire as a commercial necessity to maintain supply lines for the future.

Costs do not always behave post fire as anticipated. As a matter of prudence, acknowledging the commercial reality of potentially higher premiums, the fewer expenses that are uninsured, the better.

Increased Costs

The ideal business interruption loss is one made up of Increased costs only, with no Gross Profit loss.

That is better for Insurers and for the Insured business. The loss has been mitigated and the customer base retained.

Some well meaning businesses do not spend enough money on increased costs, trying to keep quantum as low as possible. Unfortunately, unnecessarily large Gross Profit losses can accrue.

Spend a little to save a lot, or spend a lot to save a fortune.

Stock Valuation

Not many business are asked how they define the cost of stock in their accounts in advance of a claim. There are three categories of cost that might be included:

Raw Material costs accrue to remanufacture stock forming part of the insurable amount.

Variable costs often form part of the cost of stock but these costs may also be insured as part of the BI Gross Profit. If a BI claim will definitely be made following stock damage, for example for fresh foodstuffs to be sold the next day, it may be unnecessary to insure such costs as stock.

Fixed costs will not be normally increased if a number of widgets are remanufactured post incident. Premium may be made in respect of fixed costs with no likelihood of a claim for that cost being paid.

Asbestos

Asbestos is an identified problem with regards buildings, and sums insured are frequently increased to reflect the higher disposal costs which may arise post incident.

However, the corresponding impact on stock and contents might be overlooked. The asbestos in a building is likely to cross contaminate all of the assets therein. The sums insured for debris removal might be insufficient to recognise that.

Obsolete Assets

Many business retain assets that might not be in everyday operational use. However, unless explicitly excluded, they still need to be included in a value at risk calculation.

Such assets include:

- Masters and moulds in the ceramics industry / dies and tooling for manufacturers
- Wardrobe collections for theatre companies / Image libraries for photographers / researchers.
- Conveyancing files for solicitors
- Historical financial documentation for VAT
- Quality control records for HSE, and particularly in the aviation industry
- Recipe details for manufacturers / Design records for currently unfashionable products.

If these assets are obsolete, a clear statement to that effect pre claim can avoid misunderstandings.

Security Requirements

Security requirements endorsed or warranted on a policy require ongoing review.

Windows or doors might be replaced and locks thereon inadvertently downgraded.

The status of the local police force's attitude to intruder alarms has caused difficulty in the past. Forces have on occasion downgraded responses for a whole area, and have written to businesses advising them to tell their insurers. Where such businesses fail to do so, this may constitute a breach of policy conditions.

Multi-million pound claims have been repudiated on this basis.

Keyman Insurance

Keyman insurance policies provide for lump sums on the death or incapacity of key individuals in the senior management team.

However, these are not business interruption covers. The loss of key team members after a fire, whether through stress, the desire to work, or for any other reason, may exacerbate a BI loss. If the additional element of loss caused by their absence (as opposed to that deriving from Damage) can be measured, it may not be payable by the Insurance policy.

There appear to be expectation issues with regards keyman insurance that might be managed better pre-incident.

vrs Vericlaim office locations

London
Suite 306
1 Alie Street
London
E1 8DE
T: +44 (0)20 7709 4040
london@vrsvericlaim.co.uk

Birmingham
1 Cornwall Street
Birmingham
B3 2DX
T: +44 (0)121 200 8680
birmingham@vrsvericlaim.co.uk

Manchester
Nelson House
Park Road
Timperley
WA14 5BZ
T: +44 (0)161 905 8510
manchester@vrsvericlaim.co.uk

Leeds
Suite A, Hall Mews
Clifford Road
Boston Spa
LS23 6DT
T: +44 (0)1937 846 270
leeds@vrsvericlaim.co.uk

Glasgow
Suite 5, West Wing
Buchanan Business Centre
Cumbernauld Road
Stepps
Glasgow
G33 6HZ
T: +44 (0)141 779 5230
glasgow@vrsvericlaim.co.uk

vrs Vericlaim UK Ltd
Suite 306
1 Alie Street
London E1 8DE
T: +44 (0)20 7709 4040
SSteel@vrsvericlaim.co.uk
www.vrsvericlaim.co.uk

vrs»vericlaim