INSURANCE EXAM · IC-57

IC-57 Fire and Consequential Loss

Revision book

11	2	232
chapters	master tables	numbered sections

FREE SAMPLE: Chapter 1 of 11

CHAPTER 1

Basic principles and the fire policy

1.1 Definition and features
1.2 Valid contract (Indian Contract Act 1872)
1.3 Utmost good faith
1.4 Indemnity and valuation
1.5 Sum insured
1.6 Insurable interest
1.7 Other principles
1.8 Old fire tariff (AIFT)
1.9 Fire policy form

MUST KNOW

1. Insurance Act 1938, S.2 defines fire insurance business.
2. **Policy:** usually **1 year**; longer only for residential houses.
3. Insurer pays actual loss only, within the sum insured.
4. **Perils:** social, natural, miscellaneous. Loss of profit = separate CL (Fire) policy.
5. **Disclosure:** ends at conclusion in common law; the alteration condition continues it.
6. Book value is never the basis; RIV has no depreciation deduction.
7. **Insurable interest:** at start, during policy and at loss. Policy is personal.
8. Contribution and subrogation are corollaries of indemnity.
9. AIFT rating part withdrawn **1 Jan 2007**; wordings continued; 8 sections.

1.1 Definition and features

- **S.2 Insurance Act 1938:** loss by or incidental to fire or other customary occurrence.
- Contract of good faith; period **1 year** max (houses can exceed); renewable.
- **Subject matter:** moveable and immovable property with money value, inside or in the open.
- **Perils:** social (riot, strike), natural (storm, flood), miscellaneous (aircraft, vehicle impact).
- Material damage only; consequential loss (loss of profit) = separate policy (ch 9 and 10).

TRAP

No loss = no liability, even if a fire occurred.

1.2 Valid contract (Indian Contract Act 1872)

- Offer and acceptance; consideration; agreement; competent parties; legality.
- **Consideration:** insured gives premium; insurer gives promise to pay.
- **Not competent:** minor, insane, under alcohol or drugs.
- Against public policy or law = not enforceable.

1.3 Utmost good faith

- Duty to disclose material facts; breach = void or voidable.
- **Two aspects:** disclosure; preserving the property and status quo.
- Material fact = affects acceptance, declining or premium.
- Insured must tell known material facts even if not asked.
- **Common law:** duty ends when contract concluded. The alteration condition: report material alteration during policy.
- **Proposal declaration:** becomes basis of contract; statements become warranties, literally true.
- Insurer survey = deemed knowledge; no penalty unless insured deliberately misled the surveyor.
- **Act as if uninsured:** prevent fire, fight it, salvage.

1.4 Indemnity and valuation

- **Indemnity:** same money position as before loss; no profit. Payment, reinstatement or replacement.
- Sum insured = upper limit, not the measure of indemnity.

Basis	Meaning
Market value	Present cost of similar less real depreciation (age, usage, wear); = actual cash value
Book value	Original cost less accounting depreciation; never right basis
Reinstatement value (RIV)	New for old; no depreciation deducted
Agreed value	Valuation certificate; art, manuscripts, obsolete machinery, heritage buildings

Property	Basis
Buildings, plant, furniture, electrical installation	Market value or RIV
Household effects, shop contents	Market value
Raw material	Market (replacement) value
Semi-finished goods	Raw material + expenses so far
Finished goods	Raw material + all overheads; never selling price

TRAP

RIV (insured's choice) is not the reinstatement condition (insurer's choice to reinstate).

1.5 Sum insured

- Fixed by the insured; maximum liability; premium base; should equal real value.
- **Over-insurance:** no benefit. Under-insurance: pro-rata average.

FORMULA AND WORKED SUM

- Claim = loss x SI / value. Example: 4 x 18 / 24 = Rs 3 lakh.

1.6 Insurable interest

- Physical object; subject matter; legal relationship; pecuniary interest.
- Gives legal validity; separates insurance from a wager.

- **Bank:** loan + interest outstanding; joint names with Agreed Bank Clause; insure full value, not just loan.
- Must exist at start, throughout and at loss.

> **TRAP**
> **Personal contract:** no automatic transfer on sale; needs endorsement.

1.7 Other principles

- **Proximate cause:** active, efficient, dominant cause; immediate, not remote.
- **Contribution:** same property, many policies; rateable share; corollary of indemnity.
- **Subrogation:** recovery rights pass to insurer after paying; corollary of indemnity.

1.8 Old fire tariff (AIFT)

> **TODAY'S RULE**
> Tariffs withdrawn **1 Jan 2007** (TAC circular **4 Dec 2006**). Insurers set own rates and file with IRDAI. SFSP wording continued; AIFT only a reference.
>
> **From 1 Apr 2021:** Bharat Griha Raksha (homes), Bharat Sookshma Udyam Suraksha (up to **Rs 5 cr**), Bharat Laghu Udyam Suraksha (**Rs 5 cr** to **Rs 50 cr**). Insurers may file own products since **2022**.

- Old tariff binding (S.64UC(4),(5)); made by Tariff Advisory Committee, Part IIB.

Section	Subject
I	General rules
II	Standard fire and special perils policy
III	Dwellings, offices, hotels, shops
IV	Industrial and manufacturing risks
V	Utilities outside industrial risks
VI	Storage risks outside industrial compound
VII	Tank farms, gas holders
VIII	Add-on covers

- **Annexure:** specimen clauses.

1.9 Fire policy form

- Operative clause; general exclusions; general conditions.
- **Operative clause:** preamble, limitation of sum insured, perils covered.
- **Preamble:** pays value at destruction or damage amount, or reinstates or replaces at its option.
- **Limit:** never above sum insured per item or total.

CHAPTER 1 (CONTD.)

The perils covered, exclusions and conditions

1.1 Fire peril
1.2 Lightning, explosion, aircraft
1.3 Riot, strike, malicious and terrorism
1.4 STFI
1.5 Other perils
1.6 General exclusions (13)
1.7 Conditions (15 in all; seven here)

MUST KNOW

1. Fire = accidental actual ignition. Excluded: own fermentation, spontaneous combustion, heating or drying process, burning by public authority order.
2. **"Its own":** neighbouring property damaged by spread is paid; only the first item is excluded.
3. Lightning is covered with or without fire. Terrorism is excluded unless the inclusion clause is bought (extra premium).
4. STFI covered; earthquake and volcanic eruption excluded. Heavy clay = greatest subsidence risk.
5. **Old tariff excess:** **5%** of lightning / STFI / subsidence claims, minimum **Rs 10,000**.
6. Fees **3%** and debris **1%** of the claim; consequential loss excluded; machinery away up to **60 days**.
7. **Building falls:** cover ends in **7 days**. Unoccupied more than **30 days**: cover ceases.
8. Claim statement in **15 days**; liability ends **12 months** after loss; suit within 12 calendar months of disclaimer.
9. **Cancellation:** insured gets short period scale; insurer gives **15 days**' notice, pro rata refund.
10. Right of entry does not admit liability; no abandonment to the insurer.

1.1 Fire peril

- **Fire:** actual ignition or burning, accidental or fortuitous as far as the insured is concerned.
- **Excluded:** its own fermentation, natural heating or spontaneous combustion; heating or drying process; burning by order of a public authority.
- **Examples:** hay and coal in bulk; sugar over-heated in refining = not payable.
- **Haystack:** first stack excluded; stacks burned by spread are paid.
- Spontaneous combustion can be bought as an add-on (Chapter 2).
- **Also paid after a fire:** smoke, scorching, falling walls; fire-brigade water and blowing up; weather damage to goods removed to reduce loss.

TRAP

"Its own" = only the item that heated itself. Do not exclude the whole loss.

1.2 Lightning, explosion, aircraft

- **Lightning:** all damage, fire or no fire.
- **Explosion:** sudden violent burst with loud sound; "concussion damage" = broken machinery, shattered glass, splintered timber.
- **Implosion:** bursting inward / collapse from outside pressure.
- **Excluded:** own explosion of boilers (not domestic), economisers, steam vessels, centrifugal machinery. Cover = engineering policy.
- **Aircraft:** aircraft, aerial or space devices (balloons, rockets, satellites), articles dropped. Pressure waves excluded (low-flying rattle, supersonic boom).

1.3 Riot, strike, malicious and terrorism

- **Covered:** direct visible physical damage by external violent means.

Excluded head	Meaning
Stoppage	Cessation of work or process, omissions
Government order	Confiscation, commandeering, requisition, destruction
Unlawful occupation	Dispossession, blocked access
Burglary / theft	House breaking, larceny, attempts

- **Terrorism exclusion warranty:** any act of terrorism, whatever other cause contributes; also action to control or suppress it.
- **Act of terrorism:** force, violence or threat; political, religious, ideological aims; UAPA Amendment Act **2008**.
- **Inclusion clause:** extra premium; pays above any government compensation scheme.
- **Military Authority:** armed forces, paramilitary, police, any authority for law and order.

1.4 STFI

- Popular meanings; earthquake, volcanic eruption, convulsions of nature excluded.
- **Earthquake cover added:** delete "excluding earthquake" words.
- Storm = severe air disturbance (heavy rain, hail, wind, snow). Flood = water escaping its normal confines (level rise or barrier breakdown).

1.5 Other perils

Peril	Excluded / note
Impact	Own vehicle or animal of insured, occupier, employees (add-on)
Subsidence, landslide, rockslide	New-structure settling, made-up ground, erosion, defective design, demolition / excavation
Bursting of tanks, pipes	Water tanks, apparatus, pipes
Missile testing	By Government of India
Sprinkler leakage	Repairs, installation work, known defects
Bush fire	Forest fire (add-on)

- **Sub-soils:** gravel, heavy clay, sandy, silt. Heavy clay greatest risk.

1.6 General exclusions (13)

- **1 Excess (old tariff):** **5%** each claim for lightning / STFI / subsidence, minimum **Rs 10,000**; other perils with SI up to INR **10 cr** per location (from **1 Apr 2011**); per event per insured.

FORMULA AND WORKED SUM

- **Rs 8,00,000 lightning:** excess 40,000; pays 7,60,000. Rs 1,50,000: 5% = 7,500, so excess 10,000; pays 1,40,000.

- 2 War, civil war. 3 Nuclear. 4 Pollution (except pollution from an insured peril, or a peril from pollution).
- **5 Unless declared:** bullion, unset stones; curios and art above **Rs 10,000**; manuscripts, plans, securities, documents; stamps, coins, notes, cheques; books of accounts; computer records; explosives.
- 6 Cold storage temperature change (power failure = add-on). 7 Electrical risks (fans and wiring in dwellings excepted); spread fire is paid.
- 8 Fees **3%** and debris **1%** of claim; fees on adjusted loss; claim preparation costs not included.

FORMULA AND WORKED SUM

- **Adjusted loss Rs 20,00,000:** fees 60,000 + debris 20,000 = 80,000.

- 9 Consequential loss (separate policy). 10 Spoilage from process stoppage. 11 Theft after a peril (except RSMD). 12 Earthquake. 13 Removal elsewhere; machinery up to **60 days**.

TODAY'S RULE

Tariffs were withdrawn from **1 Jan 2007**; the excess figures are old tariff practice, used as a guide. Each insurer files its own terms with IRDAI.

1.7 Conditions (15 in all; seven here)

Condition	Point
i	Voidable for misrepresentation or non-disclosure (good faith)
ii	Cover ceases **7 days** after a building falls (unless an insured peril); notice in **7 days** may allow continuation
iii	Material alteration: risk raised; unoccupied over **30 days**; transfer of interest (exceptions: will / law; endorsement)
iv	Marine clause: fire policy pays only the excess over marine
v	Insured cancels: short period scale. Company: **15 days**' notice, pro rata
vi	Claim duty, then limitation
vii	Right of entry

- **vi duty:** immediate notice; written claim in **15 days**; proof at insured's expense; declaration on oath (rarely used). Condition precedent.
- **vi limitation:** **12 months** from loss (unless action / arbitration pending); suit within 12 calendar months of disclaimer or time barred.
- **vii:** enter, take possession, salvage, sell; no admission of liability; non-co-operation forfeits; no abandonment (right of marine policy).

TODAY'S RULE

Surveys now: surveyor appointed in **24 hours**; survey compulsory above **Rs 1 lakh** (non-motor); report in **15 days**; insurer decides in **7 days** of report (IRDAI PPI Regulations **2024**; Master Circular **5 Sep 2024**).

TRAP

7 days (building fall) / **15 days** (claim and notice) / **30 days** (unoccupied) / **60 days** (machinery) / **12 months** (limitation).

CHAPTER 1 (CONTD.)

Conditions, average and the Bharat policies

1.1 Conditions: fraud to continuation
1.2 Average and contribution sums
1.3 Arbitration details
1.4 Standard fire products from 2021
1.5 In-built covers (Sookshma and Laghu)
1.6 Summary points

MUST KNOW

1. **Fraud:** 4 cases forfeit all benefits (fraud claim, false declaration, fraudulent means by insured or his agent, wilful loss or connivance).
2. **Average:** Claim = Loss x SI / Value, item by item; equal totals do not save an under-insured item.
3. **Contribution:** share = loss x own SI / total of all SIs.
4. **Arbitration:** amount only, never if liability is denied; **30 days**, then panel of 3; Act of **1996**; award is condition precedent.
5. Extra premium from loss date to expiry is deducted from the claim; cover continues in full.
6. **2021 products:** BSUS up to **Rs 5 cr**, BLUS over **5 cr** to **50 cr**, BGR homes; compulsory from **1 Apr 2021**.
7. Bharat adds tsunami, forest and jungle fire, theft within **7 days**; aircraft damage inside impact.
8. **SI basis:** reinstatement, market or agreed value (not cost, nominal or rateable value).

1.1 Conditions: fraud to continuation

- **Fraud:** fraudulent claim; false declaration; fraudulent means by insured or anyone for him; loss by wilful act or connivance of insured.
- Fraud avoids the policy under common law; condition is for emphasis.
- **Reinstatement:** insurer may pay value or damage, or reinstate or replace.
- Reinstatement need not be exact or complete; limit = pre-fire condition within SI.
- Insured gives plans and details at his own expense; insurer's steps are without prejudice.
- **If law stops rebuilding:** pay only what lawful reinstatement would cost (indemnity basis).
- Rarely used; guards against inflated claims.
- **Average:** insured is his own insurer for the difference; each item separate.
- **Contribution:** same property, similar peril; rateable proportion = own SI / total SI.
- **Subrogation:** insurer holds insured's rights even before paying; help at insurer's expense.
- **Arbitration:** quantum only; sole arbitrator in writing; else 3 arbitrators after **30 days**.
- **Notices:** written or printed.
- **Continuation:** full SI maintained; pro-rata premium from loss date to expiry deducted from the claim.
- If insured at once chooses not to reinstate, SI reduced by the loss.
- **Fire form:** operative clause, general exclusions, general conditions; about 13 exclusions, 15 conditions.

TRAP

- Learn the conditions by name, not by number.
- Arbitration is refused if the insurer disputes liability.
- Subrogation help costs the insurer, not the insured.

1.2 Average and contribution sums

FORMULA AND WORKED SUM

- **Rs 30,000 SI, Rs 40,000 value, Rs 16,000 loss:** 16,000 x 30,000 / 40,000 = Rs 12,000.
- Building 1,00,000/1,00,000; machinery 3,00,000/2,00,000; stocks 5,00,000/6,00,000, loss 60,000: pay 60,000 x 5/6 = Rs 50,000.
- **Value 1,00,000, SI 75,000, loss 35,000:** 35,000 x 75,000 / 1,00,000 = Rs 26,250 (Rs 46,667 is the upside-down trap).
- **Policies Rs 6 lakh and Rs 4 lakh, loss Rs 5 lakh:** A pays 3 lakh, B pays 2 lakh.

TRAP

Equal total SI and total value does not stop average on one item.

1.3 Arbitration details

- **Law:** Arbitration and Conciliation Act **1996**.
- Award is a condition precedent to any suit on the policy.
- **Reasons:** quick, cheaper than court, private (no bad publicity).

1.4 Standard fire products from 2021

Peril	SFSP	Bharat (BLUS, BSUS, BGR)
Fire	Yes	Also own fermentation, natural heating, spontaneous combustion
Aircraft damage	Separate	Clubbed into impact
Storm etc.	Yes	Tsunami added
Impact	Yes	Any external physical object (vehicle, tree, aircraft, wall)
Bush fire	Yes	Forest and jungle fire added
Earthquake, volcanic eruption	Add-on	In-built
Terrorism	Add-on	In-built
Theft (within 7 days)	No	Yes

TRAP

Aircraft damage is not a separate peril in the Bharat policies.

1.5 In-built covers (Sookshma and Laghu)

Cover	Limit
Additions, alterations, extensions (not stocks)	**15%** of SI for the item
Stocks temporarily removed (fabrication, processing, finishing)	**10%** of value
Money	**Rs 50,000**
Documents (deeds, books, plans, securities)	**Rs 50,000**
Computer programmes and data	**Rs 5 lakh**
Personal effects of staff, directors, visitors	**Rs 15,000** each, **20 persons**
Start-up expenses	Laghu **Rs 5 lakh**; Sookshma **Rs 1 lakh**
Professional fees	up to **5%**
Debris removal	up to **2%**

- **Also in-built:** municipal regulation costs, terrorism, earthquake.
- **Floater cover for stocks:** Sookshma only.

1.6 Summary points

- **Principles:** utmost good faith, indemnity, insurable interest, proximate cause, contribution, subrogation.
- **Corollaries of indemnity:** subrogation and contribution.
- Insurable interest gives legal validity; separates insurance from a wager.
- **Cold storage stock:** generally excluded; add-on by endorsement possible.
- **Contract law:** Indian Contract Act **1872**.