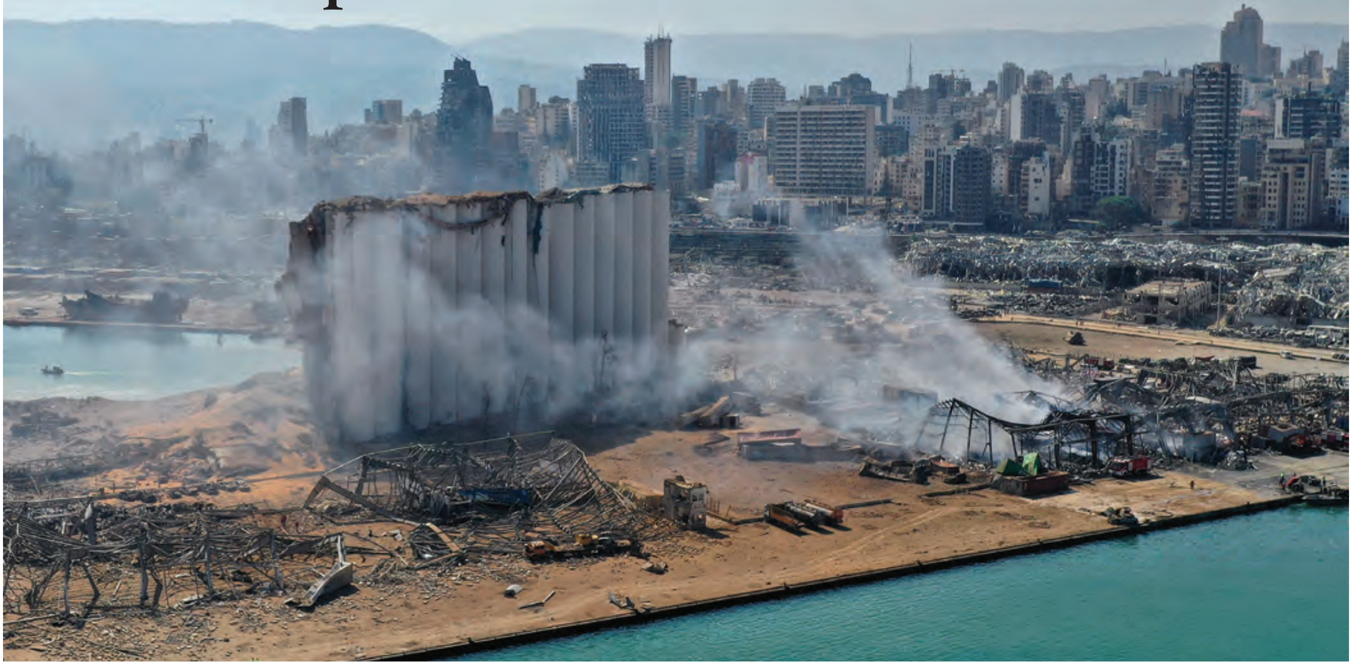
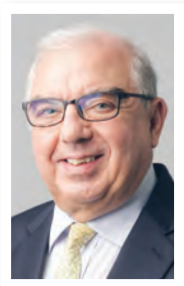
INSIGHTS – CLAIMS

Beirut explosion: Claims considerations



Mr Graham Purdon of **Concordia Consultancy** discusses the insurance and reinsurance implications of the tragic explosion that took place in the port area of the city of Beirut, Lebanon.



A massive explosion rocked Beirut on 4 August, destroying much of the city's port, and damaging buildings and infrastructure across the capital. Reminiscent of the disastrous explosion at the Port of Tianjin in China in 2015, the blast in Beirut struck with the force of a 3.5 magnitude earthquake and was heard and felt as far away as Cyprus, more than 200km away.

The explosion originated in Warehouse 12 of the government-owned Port of Beirut, and was allegedly caused by a fire from welding work. In turn, the fire spread to 2,750 tonnes of ammonium nitrate (equivalent to 1,155 tonnes of TNT) in storage after being confiscated by the Lebanese authorities more than six years earlier.

The resulting explosion produced catastrophic consequences. The stark figures make grim reading:

- More than 190 people were killed;
- 6,500 were injured;
- 25,000 homes rendered uninhabitable;
- 300,000 people homeless; and
- $15bn of property damage.

Global reinsurance brokers Guy Carpenter has stated that property insurance levels are "relatively low in Lebanon".

In Beirut, few homeowners have insurance, producing disputes between landlords and tenants over who should pay for repair work.

Even where cover is in place, some insurers are refusing to deal with claims until the cause of the explosion has been established, just in case the cause is an excluded peril, such as terrorism and political violence. As a CEO of a local insurer put it: "Usually it's MNCs or big Lebanese firms that take this cover."

Braced for losses

Discussion on cause also raises the question of whether recovery rights exist against any negligent third party. Potential recovery targets include the contractors undertaking the welding work allegedly responsible for the initial fire. The contractors, however, are extremely unlikely to have the resources or sufficient liability cover to meet even a small percentage of the losses. The Port of Beirut is also likely to be a recovery target, although, as always, the success of any claim will depend on the supporting evidence.

A little over a month since the August incident, a second fire broke out at the port on 10 September in the duty-free zone in a warehouse allegedly used for the storage of tyres and oil. The fire was nowhere as serious as the early August incident, and was extinguished within 24 hours.

MNCs with property interests and/or operating businesses in Lebanon will become the main claim focus of the insurance market. The local market will face thousands of other claims. The local insurance sector, however, has been struggling for some time due to the financial crisis and banking restrictions. Whether local insurers, some of whom have found it difficult to settle their reinsurance premiums, have the resources to meet such claims remains to be seen.

Policy considerations

The insurance arrangements of MNCs are often more complex than a single standalone policy. The major international brokers are experienced in developing a global insurance programme for those companies with a worldwide network of operating companies.

Typically, such a programme will include a master policy, usually a property damage (PD) and business interruption (BI) all risks insurance, issued in the domicile of the MNC's head office. The PD/BI policy is then augmented by a local policy issued by a registered insurer in each of the countries of the world in which the MNC operates. It is normal for each local policy to be 100% reinsured back to the master policy insurers, and for the programme to incorporate a large deductible.

The master and local covers operate as constituent parts of the global programme, with the existence of each being mentioned in the policies. It is normal for the master policy to be written on a difference in conditions (DIC) and difference in limits (DIL) basis. The intention being to meet only those claims for the shortfall in recovery under the local policy, either because of restricted cover or policy limits being inadequate. The master policy underwriters may also use their own reinsurance arrangements to transfer some of the risk to the international insurance market.

The larger MNCs often establish a captive insurer as part of their risk management programme.

Claims management

Having set out typical insurance arrangements, let's now look at claims management. In the case of the Beirut explosion, let's assume damage to a factory/warehouse complex in the port area, the property of a European-domiciled MNC.

There will be an immediate report to the insurance manager/risk manager at the MNC's head office, and from there a first notice of loss notification to the master policy underwriters.

Under such a programme, it is normal for a single firm of loss adjusters to be nominated on a global basis. Concordia is entrusted with such nominations across a wide range of industries and, in this regard, provides service globally to the international insurance market. The nominated loss adjusters operate under a pre-agreed claims protocol forming part of the insurance programme.

The nominated adjusters will be advised of the loss on a same-day basis, to facilitate immediate investigation of the circumstances giving rise to the loss. One of the initial challenges facing the appointed adjuster is access to the loss location. In the case of Nat CATs such as hurricanes and earthquakes, immediate access may not be possible. In such cases, the adjuster's approach is to make contact with the insured's local staff to obtain preliminary information, and for the adjuster to provide early advice on loss mitigation. At this point, the adjuster will make decisions on the need for specialist consultants, such as forensic accountants (BI and large stock claims), forensic engineers (root cause analysis), loss mitigation contractors, and quantity surveyors (building claims). Any such appointments must be agreed by insurers.

The adjuster will then progress the management of the claim through communication with the insured's insurance manager and local staff at the loss location. Excellent communication amongst the key stakeholders is essential to ensure that the claim progresses well.

Estimate of loss

As in all large losses, the interested insurers (and their reinsurers) look to the appointed adjuster for an early estimate of loss to enable claim reserves to be established. In recommending reserves, the adjuster must first review the heads of claim against the cover and limits of the local policy. Any possible shortfall will result in a reserve being recommended under the master policy.

The loss adjuster will progress the claim to achieve conclusion as quickly as possible by engaging with the insured, locally and at head office, and reporting to, and receiving instructions from, the insurers involved. It is the insured's obligation to produce a quantified claim, with supporting documentation, for consideration under the insurance programme. The MNC may entrust the claims preparation work to their insurance brokers or to a firm of forensic accountants, with whom the loss adjuster will then engage.

The adjuster will collate all claim information, for discussion with the insured or their appointed representatives. Adjustments may be warranted. For example, the local policy may be written on an indemnity basis and the master on a replacement basis. Thus, depreciation adjustments must be agreed with the insured, for transfer to the master policy.

One other area of adjustment, requiring careful consideration and discussions with the insured, relates to the replacement of plant and machinery. Whilst the master policy, if not the local, provides cover on a replacement basis, the settlement amount must be calculated on a like-for-like basis. In the event that replacement plant and equipment involve an enhanced specification (greater capabilities and/or faster performance) over the original, adjustments must be agreed.

In summary, standard adjusting principles are adopted in the management of MNC claims, but challenges arise from the existence of two policies and two insurers. Concordia's experience is that regular dialogue and communication with the interested parties enables issues to be understood and resolved without delay. MNCs expect an excellent claims service under their global insurance programme and the nominated loss adjuster has an important role to play to achieve this.

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