

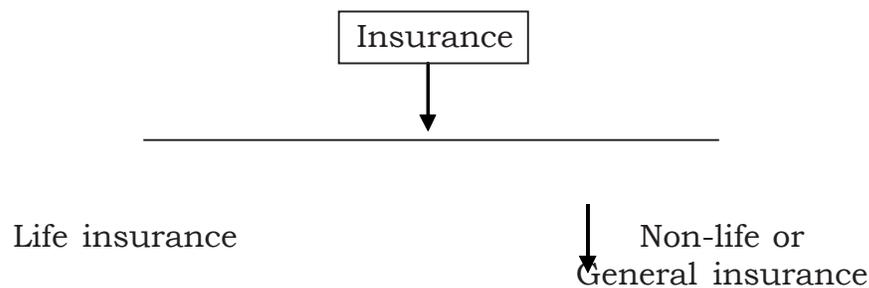
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FIRE INSURANCE

1.0 INTRODUCTION

Insurance sector is divided in two parts as under:



In this module we will explain various insurance policies related to non-life /general insurance. Non-life /general insurance means the insurance of various tangible or non-tangible assets other than human life. Even loss of human life or damage to human body due to accidents are covered by general insurance. Thus, human life relates to life insurance and the belongings i.e. properties of human beings fall under this category.

Though there are various general insurance policies but we will discuss only the following important policies:

1. Fire Insurance
2. Marine Insurance (Transit)
3. Vehicle Insurance
4. Personal Accident Insurance
5. Health Insurance
6. Rural Insurance Policies

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The above said policies are being sold only by general insurance companies and cannot be sold by life insurance companies. This restriction is imposed only in India but not in other parts of the world.

In India also, prior to nationalization, general insurance business was conducted by life insurance companies also but after nationalization in 1972, consequent upon passing of the General Insurance Business Nationalisation Act (GIBNA) General Insurance Corporation of India was formed and was conferred the exclusive power to regulate and conduct the business of General Insurance in India.

Since 1973 the GIC and its four subsidiary companies namely New India Assurance Co. Ltd., National Insurance Co. Ltd., Oriental Insurance Co. Ltd., and United India Insurance Co. Ltd. had been the sole players in the field until the passing of the IRDA Act 1999 which allowed the entry of private players.

Over the past few years a few private players have entered the arena. The new players have entered the General Insurance field but are playing cautiously. These are still early days but the field is wide open, the future is bright and the customer is the one who will be benefited the most by the growing competition. We hope to see international level of service and products in the country soon and a multiple choice to select from.

At the end of this lesson, you will be able to:

- Explain the meaning of fire insurance
- Buy the fire insurance
- Settle the claim under fire insurance
- Know the practice of fire insurance in India.
- Know what is not covered under fire insurance

In the following pages, we shall be discussing the Fire Insurance.

1.1 HISTORY OF FIRE INSURANCE

The development of fire Insurance can be traced back to 1601 A.D. when the Poor Relief Act was passed in England. Vide this act, letters called “briefs” were read from the church asking for collections from the public to help those who suffered losses from fire. There was a great fire in London—a historical disaster—

in which within span of three days from 2nd to 5th Sept.'1666, 80% of the city was destroyed which sowed the seeds of fire Insurance as we know it now.

First, only buildings were insured and the first fire office was established by a builder Nicholas Barbon in 1680. In 1708, Charles Povey founded the Traders Exchange for insuring movable goods, merchandise and stocks against loss or damage and this was the first to insure both the building and its contents.

1.2 MEANING OF FIRE INSURANCE

The term fire in a fire insurance is interpreted in the literal and popular sense. There is fire when something burns. In other words fire means visible flames or actual ignition. Simmering/ smoldering is not considered fire in Fire Insurance. Fire produces heat and light but either of them alone is not fire. Lightening is not a fire but if it ignites something, the damage may be due to fire.

Under section 2(6A) Insurance Act 1938, the fire insurance business is defined as follows: "Fire insurance business means the business of effecting, otherwise than independently to some other class of business, contracts of insurance against loss by or incidental to fire or other occurrence customarily included among the risks insured against in fire insurance policies".

Example: The following are the items which can be burnt/ damaged through fire:

- Buildings
- Electrical installation in buildings
- Contents of buildings such as machinery, plant and equipments, accessories, etc.
- Goods (raw materials, in-process, semi-finished, finished, packing materials, etc.) in factories, godowns etc..
- Goods in the open
- Furniture, fixture and fittings
- Pipelines (including contents) located inside or outside the compound, etc.

The owner of abovementioned properties can insure against fire damage through fire insurance policy which provides



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financial protection for property against loss or damage by fire.

1.3 FEATURES OF FIRE INSURANCE:

(Dear learner, most of the features to be discussed in the following paragraphs of Fire Insurance you must have studied under Principles of General Insurance in other module)

- 1) **Offer & Acceptance :** It is a prerequisite to any contract. Similarly, the property will be insured under fire insurance policy after the offer is accepted by the insurance company. Example: A proposal submitted to the insurance company along with premium on 1/1/2011 but the insurance company accepted the proposal on 15/1/2011. The risk is covered from 15/1/2011 and any loss prior to this date will not be covered under fire insurance.
- 2) **Payment of Premium:** An owner must ensure that the premium is paid well in advance so that the risk can be covered. If the payment is made through cheque and it is dishonored then the coverage of risk will not exist. It is as per section 64VB of Insurance Act 1938. (Details under insurance legislation Module).
- 3) **Contract of Indemnity:** Fire insurance is a contract of indemnity and the insurance company is liable only to the extent of actual loss suffered. If there is no loss, there is no liability even if there is fire. Example: If the property is insured for Rs 20 lakhs under fire insurance and it is damaged by fire to the extent of Rs. 10 lakhs, then the insurance company will not pay more than Rs. 10 lakhs.
- 4) **Utmost Good Faith:** The property owner must disclose all the relevant information to the insurance company while insuring their property. The fire policy shall be voidable in the event of misrepresentation, mis-description or non-disclosure of any material information. Example: The use of building must be disclosed i.e whether the building is used for residential use or manufacturing use, as in both the cases the premium rate will vary.
- 5) **Insurable Interest:** The fire insurance will be valid only if the person who is insuring the property is owner or having insurable interest in that property. Such interest must exist at the time when loss occurs. It is well known that

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insurable interest exists not only with the ownership but also as a tenant or bailee or financier. Banks can also have the insurable interest. Example: Mr. A is the owner of the building. He insured that building and later on sold the building to Mr. B and the fire took place in the building. Mr. B will not get the compensation from the insurance company because he has not taken the insurance policy being a owner of the property. After selling to Mr. B, Mr. A has no insurable interest in the property.

- 6) **Contribution:** If a person insured his property with two insurance companies, then in case of fire loss both the insurance companies will pay the loss to the owner proportionately. Example: A property worth Rs. 50 lakhs was insured with two Insurance companies A and B. In case of loss, both insurance companies will contribute equally.
- 7) **Period of fire Insurance:** The period of insurance is to be defined in the policy. Generally the period of fire insurance will not exceed by one year. The period can be less than one year but not more than one year except for the residential houses which can be insured for the period exceeding one year also.
- 8) **Deliberate Act:** If a property is damaged or loss occurs due to fire because of deliberate act of the owner, then that damage or loss will not be covered under the policy.
- 9) **Claims:** To get the compensation under fire insurance the owner must inform the insurance company immediately so that the insurance company can take necessary steps to determine the loss.

INTEXT QUESTIONS 1.1

1. What is utmost good faith?
 2. What is period of insurance?
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1.4 PROCEDURE TO INSURE THE PROPERTY UNDER FIRE INSURANCE:

For insuring any property under the fire insurance policy, the following is the procedure:

- 1) Filling of proposal form
- 2) Inspection of the property
- 3) Payment of premium
- 4) Issue of Cover note/ Policy document in lieu of acceptance of the proposal.

I) Filling of Proposal Form

The fire proposal includes the following information :

Description of the property. This would include:

- I)
 - (i) Construction of external walls and roof, number of storeys.
 - (ii) Occupation of each portion of the building.
 - (iii) Presence of hazardous goods.
 - (iv) Process of manufacture.
 - (v) The sums proposed for insurance.
 - (vi) The period of insurance.
 - (vii) History of previous losses.
 - (viii) Insurance history - whether previously other insurers had declined the risk, etc.
- II) **Inspection of the property:** In case of property of any business organization, whether manufacturing or other type of organization, a risk inspection report is submitted by the insurer's engineers. The engineers submit in their report the nature of risk involved in the factory/ manufacturing unit.
- III) **Payment of Premium:** Based on the proposal form and the inspection report of the engineers, the insurance company will submit the premium rates to the property owner and if these rates are acceptable to him then he should pay the amount to the insurance company. It is also a legal requirement under section 64VB of Insurance

Act 1938 that the premium is paid in advance in full to the insurance company.

- IV) **Issue of Cover note/ Policy document:** On receipt of a completed proposal form and / or inspection report, the cover note is issued, pending preparation of the policy document. The cover note is an unstamped document issued to provide evidence of cover till the time the policy is issued. The cover note provides insurance against specified perils on the usual terms and conditions of the company's policy.

The printed policy form provides for a schedule in which the individual details of the contract are typed. The items are similar to those in the Cover Note but with more detailed information.

After issuing the policy document, it is likely that there may be some changes in the nature of property or sum insured may increase or decrease. In this case, these changes can be incorporated by way of endorsements which are issued to record changes such as alteration in risk, increase or decrease of sum insured, etc.

1.5 PROCEDURE TO SETTLE THE FIRE INSURANCE CLAIM:

- A) If there are any damage or loss arising due to fire then the policy holder should immediately inform the insurance company in writing and with estimated amount of loss.
- B) **Survey Report:** If the amount of loss is small (i.e. up to Rs. 20,000/-), the insurance company may depute an officer to survey the loss and decide on the settlement of the loss on the basis of the claim form and the officer's report. However, in large losses, an independent surveyor duly licensed by the Government is appointed to give a report on the loss.

The survey report would generally deal with the following matters:

- (i) Cause of loss.



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- (ii) Extent of loss.
 - (iii) Under-Insurance, if any.
 - (iv) Details and value of salvage, and how it has been disposed of or proposed to be disposed of.
 - (v) Details of expenses (e.g. fire brigade expenses).
 - (vi) Compliance with policy conditions and warranties.
 - (vii) Details of other insurance policies on the same property, and the apportionment of the loss and expenses among co-insurers.
- C) **Claim form:** The policy holder will submit the claim form with the following information :
- (i) Name and address of the Insured.
 - (ii) Date of loss, time and place from where the fire started.
 - (iii) Cause of fire.
 - (iv) Details of the property damaged such as description, etc.
 - (v) Value at the time of fire, value of salvage and the amount of loss.
 - (vi) Details of other policies on the same property giving the name of the insurer, policy number and sum insured.
 - (vii) Fire Brigade report details.
 - (viii) F.I.R. at the nearest police station regarding third party liability, if any.
- D) **Settlement of claim:** On the basis of the claim form and the survey report, decision is taken about the settlement or otherwise of the loss.

1.6 PRACTICE OF FIRE INSURANCE IN INDIA

In India, under fire insurance policy, in addition to fire, other perils are also included and the policy is known as **“Standard Fire and Allied Perils Policy”**.

The perils specified in the fire policy are:

- A. **Fire:** It has been explained as above.

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- B. **Lightning:** Any lightning due to cloud burst may damage the property and the same will be covered under the fire policy.
- C. **Explosion / Implosion:** Sudden change in the temperature in any plant & machinery or exposure to atmospheric pressure may result into loss and the same will be covered under fire policy.
- D. **Aircraft Damage:** Any damage to the property due to any droppings by aircraft or by itself will also be covered under the fire policy.
- E. **Riot, Strike and Malicious Damage (RSMD):** Any damage to the property due to public or strike by employees or malicious damage (intentional damage) by any person will be covered under this policy.
- F. **Storm, Cyclone, Typhoon, Tempest, Hurricane, Tornado, Flood and Inundation (STFI):** The property damage due to any of these storms and flood will also be covered under this policy. The meaning of these perils lies in different intensity of the storms. Flood not only means the leakage of water through river but also accumulation of water due to heavy rains in the premises.
- G. **Impact Damage:** Damage to the property due to impact by any Rail / Road vehicle or animal by direct contact, but not belonging to or owned by the Insured or any occupier of the premises or their employees while acting in the course of their employment.
- H. **Subsidence and Landslide including Rock Slide**
Destruction or damage caused by Subsidence of part of the site on which the property stands or Land slide / Rock slide.
- I. **Bursting and/or overflowing of Water Tanks, Apparatus and Pipes:** If due to bursting or overflowing of water from the water tanks installed in the premises of the policyholder any damage or loss to the property of the policyholder is caused, it will be covered under this policy.
- J. **Missile Testing Operations:** Any loss or damage due to missile testing by the Govt. or otherwise will be covered under this policy.



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- K. **Leakage from Automatic Sprinkler Installations :** In most of the organizations as a fire protection measure, automatic sprinkler system is installed. If due to non-usage of the sprinkler system or otherwise it starts leaking and damages the property, then it will be covered under the fire insurance policy.
- L. **Bush Fire:** It means fire spread from the bushes (small fire) but will not include forest fire.

IN TEXT QUESTIONS 1.2

1. What are allied perils in Fire insurance policy?
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1.7 THE FIRE INSURANCE DOES NOT COVER THE FOLLOWING RISKS KNOWN AS GENERAL EXCLUSIONS

- (i) In every claim minimum deduction say Rs 5000/- or Rs 10000/- will be made while settling the claim under this policy. It is to avoid small losses.
- (ii) Loss, destruction or damage caused by war, and kindred perils.
- (iii) Loss, destruction or damage directly or indirectly caused to the insured property by nuclear peril.
- (iv) Loss, destruction or damage caused to the insured property by pollution or contamination.
- (v) Loss, destruction or damage to any electrical and / or electronic machine, apparatus, fixture or fitting (excluding fans and electrical wiring in dwellings) arising from or occasioned by over-running, excessive pressure, short circuiting, arcing, self-heating or leakage of electricity, from whatever cause (lightning included).
- (vi) Loss of earnings, loss by delay, loss of market or other consequential or indirect loss or damage of any kind or disruption whatsoever.
- (vii) Earthquake: It is not covered under the fire policy but by paying additional premium, the earthquake can be covered.

1.8 SPECIAL POLICIES

a) Floater Policy

This policy is issued only for the stocks, not for plant &

machineries. Sometime the stock is kept at various locations and it is very difficult to provide the value of stock at each location. Therefore to cover the risks of stocks at various locations under one sum insured an additional premium can be paid. Example: A person is having two godowns at Delhi and the value of stock is Rs 50 lakhs and he is not having the value at each location then he can insure the stock under floating policy by paying an additional premium.

b) Declaration Policies

This type of policy is useful where there is frequent fluctuations in stocks / stock values and to avoid the under insurance (insurance of lower value) of the stock, Declaration Policy(ies) can be granted subject to the following conditions:

- (a) The minimum sum insured shall be Rs. 1 crore.
- (b) Monthly declarations based on the average of the highest value at risk on each day or highest value on any day of the month shall be submitted by the Insured latest by the last day of the succeeding month. If declarations are not received within the specified period, the full sum insured under the policy shall be deemed to have been declared.
- (c) Reduction in sum insured shall not be allowed under any circumstances.
- (d) Refund of premium on adjustment based on the declarations / cancellations shall not exceed 50% of the total premium.
- (e) The basis of value for declaration shall be the Market Value unless otherwise agreed to between insurer and insured.
- (f) It is not permissible to issue declaration policy in respect of
 - i) Insurance required for a short period
 - ii) Stocks under going process
 - iii) Stocks at Railway sidings

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Example:

Sum insured	:	Rs. 1,00,00,000/- (1 crore)
Rate	:	Rs. 1.00 per mille
Premium	:	Rs. 10,000/-

Monthly Declarations

January	Rs. 58,00,000/-
February	Rs. 56,00,000/-
March	Rs. 46,00,000/-
April	Rs. 30,00,000/-
May	Rs. 30,00,000/-
June	Rs. 30,00,000/-
July	Rs. 30,00,000/-
August	Rs. 40,00,000/-
September	Rs. 40,00,000/-
October	Rs. 40,00,000/-
November	Rs. 40,00,000/-
December	Rs. 40,00,000/-

Total Declarations	<u>Rs. 4,80,00,000/-</u>
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Average sum insured/ month	Rs. 40,00,000/-
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Premium received in Advance	Rs. 10,000/-
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Premium on average sum insured (say)	Rs. 4,000/-
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Excess premium paid	Rs. 6,000/-
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According to rule, refund cannot exceed 50% (i.e.) Rs. 5000/- and not Rs. 6000/-.

c) Floater Declaration Policy

It is combination of the above mentioned policies i.e. stock lying at different locations and the value of stock fluctuating.

1.9 ADDITIONAL TERMS & CONDITIONS

a) Reinstatement Value

This is the fire policy with the reinstatement value clause

attached to it. The clause provides that in the event of loss, the amount payable is the cost of reinstating property of the same kind or type, by new property (i.e.) “New for Old”.

This basis of settlement differs from the basis under the fire policy where the losses are settled on the basis of market value i.e. making deductions for depreciation, etc.

Under reinstatement value policy, it is possible to cover the depreciated value of the building or machinery. The cost of replacement of the damaged property is ascertained by new property of the same kind. If due to technical improvements the new machinery is better than the damaged machinery e.g. output is increased with less consumption of power, the insured is obliged to bear a part of the cost of the new machinery to ensure that he does not derive any undue benefits. Thus, the principle of indemnity is still observed.

The reinstatement value clause incorporates the following special provisions:

- (a) Reinstatement must be carried out by the insured and completed within 12 months after the destruction or damage, or within such extended time as may be allowed by insurers, failing which the loss will be settled on the normal indemnity basis i.e. according to the Fire Policy.
- (b) Until reinstatement is carried out, the liability under the policy remains on the normal indemnity basis. i.e. market value basis.
- (c) Pro-rata Average is applied by comparing the sum insured with the cost of reinstatement of the entire property insured as on date of reinstatement.
- (d) The reinstatement basis of settlement will not apply
 - (i) If the insured fails to intimate to the insurer within 6 months or any extended time his intention to replace the damaged property.
 - (ii) If the insured is unable or unwilling to replace the damaged property. In such cases the loss will be settled on the normal basis of indemnity.
- (e) The work of reinstatement may be carried out upon another site and in any manner required by the insured provided the liability under the policy is not thereby increased.

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These insurances are granted to insureds whose bonafides are satisfactory and, are generally issued only in respect of building, plant *and* machinery in a comparatively new condition.

These insurances are not granted on stocks.

b) Local Authorities Clause

Reinstatement Value Policy may be extended to cover such additional cost of reinstatement of the destroyed or damaged property as may be incurred solely by reason of the necessity to comply with the Building or other Regulations under any Act of Parliament or bye-laws of any Municipal or Local Authority.

c) Agreed Bank Clause

All policies in which a Bank has a partial interest are to be made out in the name of the Bank and Owner or Mortgagor and the Agreed Bank Clause incorporated in the policy.

The salient features of the clause are :

- (a) The claim is payable to the bank whose receipt shall be a complete discharge and binding on all parties insured.
- (b) Any notice under the policy is sufficient if given by or to the bank.
- (c) Any settlement, compromise etc. in relation to dispute if made with the bank shall be valid and binding on all parties insured.
- (d) Any alteration or increase in risk does not invalidate the insurance, provided the bank notifies the same as soon as it comes to its knowledge and pays additional premium.

1.10 SUMMARY

The fire policy does not cover only the loss/damage of fire but also due to other perils like lightning, storms, strike, aircraft damage etc. Therefore the fire policy in India, is known as Standard Fire and Special Perils Policy. Though these risks are covered yet exceptions are always there. For the growth of the Indian economy every business organization should insure its assets.

If the value of stocks is fluctuating substantially during the year then the same should be insured under declaration fire insurance policy. To protect the interest of the financial institutes the agreed bank clause may be included.

In India, the fire insurance premium contributes 30% to 40% of every insurance company.

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1.11 TERMINAL QUESTIONS

- 1) Explain the features of the fire insurance policy.
- 2) Discuss the fire insurance policy in India.
- 3) Explain the various types of fire insurance policies.
- 4) Write short notes on
 - a. Reinstatement Value
 - b. Agreed Bank Clause
 - c. Local Authorities Clause

1.12 OBJECTIVE TYPE QUESTION

1. Under which of the following conditions the fire policy will cease
 - a. Changes in trade or manufacture activities
 - b. Unoccupancy of the building for more than 30 days
 - c. Transfer of insurable interest unless by will or operation of law
 - d. All of the above.
2. In case of a Fire Declaration Policy, if Sum Insured – Rs.1 crore, Rate of premium – Rs.1 per mille, and Average of Monthly Declarations – Rs.60 lakh, calculate Provisional Premium and Refund of Premium.
 - a. Rs.9,000, Rs.5,000
 - b. Rs.10,000, Rs.4,000
 - c. Rs.7,000, Rs.7,000
 - d. Rs.8,000, Rs.6,000
3. The Standard Fire and Special Perils Policy covers works of art for an amount 'not' exceeding Rs. _____.
 - a. 20,000
 - b. 10,000
 - c. 5,000
 - d. 15,000



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4. For insuring full protection of a factory the declaration of SI should be on the following basis.
 - a. Block wise separate amounts on (i) Building (ii) Machinery (iii) Stocks and Stocks in process (iv) Furniture & other contents.
 - b. Block wise separate amounts on (i) Building (ii) Machinery (iii) Stocks
 - c. Total amount for all above as SI
 - d. None of the above.

5. Which of the following perils can be an add-on cover under the Fire policy at extra premium?
 - a. Spontaneous combustion b. Flood
 - b. Impact Damage d. Explosion

6. **Under Fire Declaration policy, the basis of monthly declarations is**
 - A. A: Average of the highest value on each day of the month.**
 - B. B: Highest value on any day of the month**
 - C. C: Value on the last day of the month.**
 - a. B and C b. A and B
 - c. A, B and C d. A and C

7. **Calculate the net premium, if**
 - i. Sum insured : Rs. 500 lakh**
 - ii. Rate of premium : Rs. 2 per mille. Terrorism Rate Rs 0.30 per milli**
 - iii. Discount : 80%**
 - a. Rs. 35000/- b. Rs. 23,000/-
 - c. Rs 1.5 lakhs d. None

8. Which of the following Statements is true?
 - **Statement A : Short period rates are charged when the period of insurance is less than 12 months**
 - **Statement B : Short period rates are charged when the policy is cancelled by the insured**

- a. Only Statement A b. Only Statement B
 c. Both Statements d. Neither of the Statement.
9. In case of Fire and Accident Insurance, Insurable interest must exist
- a. At the time of loss only
 b. At inception of insurance only
 c. Both at inception of insurance and at the time of loss
 d. No insurable interest is required
10. Floater Policy can be given under which situations.
- a) Where sum insured exceeds 2 crores
 b) Where goods are placed at different godowns at different Locations
 c) Where goods are placed at different godowns at different locations in the same compound
 d) Sum insured cannot be ascertained at all locations.
- i) a & b are correct ii) a, b & c are correct
 iii) a, b, c & d are correct iv) None is correct

1.13 ANSWERS TO IN TEXT QUESTIONS

1. Lightning, Explosion / Implosion, Aircraft Damage Riot, Strike and Malicious Damage, Impact Damage, Subsidence and Landslide including Rock slide, Bursting and / or overflowing of Water Tanks, Apparatus and Pipes, Missile Testing Operations, Leakage from Automatic Sprinkler Installations, Bush Fire.

1.14 ANSWERS TO OBJECTIVE TYPE QUESTIONS

- | | | | |
|------|-------|------|------|
| 1. d | 2. b | 3. b | 4. a |
| 5. a | 6. b | 7. a | 8. c |
| 9. c | 10. i | | |

**Notes**