Erroneous Coverage: A Great Risk

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One of the principal risks for policy holders of insurance and reinsurance contracts is the eventual lack of clarity and scope of some of the specific clauses of coverage.

In the case of Insurance, the insurer's good faith is confirmed precisely by the publication of clear and unequivocal clauses which permit the insured party to adequately understand the scope of the coverage he has acquired. Lack of clarity in the terms of a clause could lead to a dispute with the insured as to the settlement of a claim, and should this go to court, judgement would undoubtedly be against the insurer.

In regards to reinsurance, a confusing clause or one that is not self-explantory could in a particular incident expose any insurance company to grave financial impact (while the scope is being disputed between the reinsurer and the insurer) or even worse, a grave economic impact (in the case where the reinsurer refuses to pay for the incident as he considers the clause in question not to be applicable). Both of these situations could have very negative impact on the insurer.

This danger could re if the particular clauses being used were free translations of the English language clauses.In the translation there is a risk that the spirit and scope of the original coverage are lost, or the legal consequences of a particular market are not adequately considered. The translations of the so called "world wide policies" of insureds having risks located in many different countries are particulary dangerous.

At this point it is worth mentioning the "Language Clause" by which (and although the insured party may have received a brief in his native language) it is stipulated that "for all effects the present contract shall be subject to the conditions of the "Master Programme in the English language...". This clause is not generally known by the insured parties.

It is also possible that insurer and insured bilaterally agree to clauses which establish scope over matters which by their very nature can escape the apparent intentions of the parties, consequently leading to prolonged judicial processes. An example of this is what is commouly known in Chile as the "Z Clause", by which in a "fronting" operation the policy contains a clause which states that in case of loss the Company will pay only when it receives the corresponding funds from the reinsurer, making an exception to the general rule that a Company cannot avoid payment of loss on the pretext that it has not received the corresponding payment from the reinsurer.

We should note that there are coverages which due to their complexity do not permit their scope to be gauged simply by reading the text, or where the text contains wording which difficult to interpret. A clear example of this is the "Claims Cooperation Clause" through which there is an intention to establish cooperation between the ceding company and the reinsurer in the settlement of a particular claim. As the scope of the word "cooperation" is not clearly defined, in a great many cases long litigation results between the parties which can prolong the settlement process... leading to consequent damage to the insured.

In contrast with this clause, we believe that the "Control of Claims" clause does not present any difficulties in clearly defining the scope of the reinsurer: it establishes the period to inform the reinsurer of the inccident, allowing him to appoint an assessor/adjuster, if he deems this appropriote, and prevent the Company from paying any amount to the insured without prior consent by the reinsurer.

Other complex clauses include those which cover political risks such as civil unrest, insurrections or popular disorders, which could cause difficulties in the interpretation of the insured event as to the time and geographic scope of the coverage.

As always and, particulary in relation to the insured, taking adequate time to assure things are done properly will bring about the desired results and eliminate drawn out discussions which definitely do not enhance the image of the insurance business, always criticized over the lack of clarity in coverages. This demonstrates that the complete text of clauses must be incorporated into the policies, thus avoiding the common and poor practice of simply referring to them by just their titles, or, even worse, by using abreviations or acronyms commonly used by insurers but absolutely meaningless to the insured.

For example, a common practice in maritime policies is to express "subject to ship Classification Clause" and no more (the insured has no idea of who does the classifying, nor does he know before hand what surcharge must be paid, and often, he does not even know the name of the ship when it starts its voyage), or subject to the "Contamination Clause" or "Excludes inexplicable Losses " or "Covers 30 days stay in customs with guaraneed existence of minimun security conditions".

So, we have a number of particular conditions whose undefined scope can complicate loss and, in short, at the very least seriously compromise the insurer's prestige.

Thus it is quite evident that all of these aspects should be attended to with particular care as in case of a major loss, the solvency of at least one of the parties involved may be seriously damaged. Therefore, the insured should make sure that the insurer, lets him know the insurance or reinsurance terms, for which he must dedicate sufficient time and effort to the study and analyse these; as each time a coverage is sought "for yesterday", the risk of error increases.