



Reflections on the Contingencies Branch

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"The Contingencies Branch is a group of insurance policies whose aim is to provide the policyholder with cover for potential obligations and claims for compensation or indemnification of a financial nature, entered into on accepting risks not covered by the traditional branches."

Definition

It is not easy to define contingencies insurance with any precision. It is best to begin with a few examples before engaging in conceptual digressions that are difficult to grasp without the benefit of a general understanding of the broad range of products available in the sector.

We give the following examples:

- ▶ Cancellation of a performance due to the non-appearance of the principal artist,
- ▶ overrun on cost of gifts because of the unforeseen success of an advertising campaign,
- ▶ value of prizes awarded to elite sporting figures for breaking a record,
- ▶ reduced performance due to lack of sunshine in solar electric installations,
- ▶ extension of warranties on new vehicles or
- ▶ loss of revenue through failure of satellite communications.

The variety is enormous. In spite of the dissimilarities, however, we can distinguish three characteristics that are common to all these risks:

- ▶ There is a wide range of different insurance products.
- ▶ The aim is to cover financial losses of varying types, whether in the field of

non-recoverable expenses, loss of revenue or in relation to certain established financial undertakings.

- ▶ It is not possible to classify them within the traditional insurance branches (property and casualty, third party Liability, goods in transit, etc.).

We now have the necessary elements to draw up an acceptable definition, as follows:

Group of insurance policies whose aim is to provide the policyholder with cover for potential obligations and claims for compensation or indemnification of a financial nature, entered into on accepting risks not covered by the traditional branches.

Policies that may be considered under contingencies

The list of potential policies continues to grow, the only limitation being the imagination of those involved in the increasingly broad and diverse industrial and service sectors and the need for protection of their liabilities, interests and investments.

With the appropriate reservations, we offer the following list to set out a rough outline of current contents rather than restrict our branch to an exhaustive listing.

1. Conventional products

- a. Cancellation of events due to bad weather, non-appearance of artists and sundry other reasons.



b. Prizes: general public (prize indemnity: competitions and lotteries) and prizes: sport (prize indemnity: contractual bonus).

c. Advertising campaigns: overselling (over-redemption) and advertising campaigns: key persons (death and disgrace).

d. Film-making procedures: production, negatives and cinematographic equipment (film producer's).

2. Travel and tourism sector

a. Cancellation due to socio-political risks, catastrophic climatological events and health scares.

b. Sunshine insurance.

c. Other risks: delays, cost increases, repatriation.

3. Residual value

On leasing or rental contracts.

4. Extended warranties

For motor vehicles, office and home computer systems.

5. Financial institution sector

a. BBB (Banker's Blanket Bond), including electronic fraud, breach of trust by employees and errors and omissions.

b. Credit cards: fraud, misappropriation, theft, loss or misplacement, user's benefits.

c. Stockbroking companies.

6. Technology sector

a. Transmission breakdown, satellite failure.

b. IT: software malfunction and consequences, loss of data, viruses and hackers.

c. E-commerce: intellectual property, illegal traffic, manipulation and spying.

d. Mobile Telephones: damage, loss and theft.

7. Motor vehicle sector

a. Multi-line for industrial vehicles: breakdown of machinery + immobilization + loss of licence.

b. Rallies and exhibitions.

8. Civil liberty sector

a. Kidnapping and ransom.

b. Discrimination in the workplace and sexual harassment.

c. Libel and slander.

9. Guarantees and indemnities sector

a. Costs and expenses due to unforeseen claims (*legal expenses coverage*).

b. Additional expenses due to change of judge (*judge indemnity – Anglo-Saxon market*).

c. Protection against indemnifications filed for a specific amount in a higher court (*judgement preservation coverage*).

Peculiarities

The following are worthy of note:

► Range of cover. We have seen in the definition that policies which do not fall within the traditional branches may be accommodated in contingencies insurance.

Although it is a flexible and multifaceted branch (it remains a catch-all area in which new risks are considered and, where appropriate, accepted), it should not be viewed as "a rubbish dump" by other branches. That which has been deemed unacceptable or uninsurable by others should not be transferred to contingencies.

► Continuous adoption of new products. The ceaseless development, in every sphere and sector, of the most advanced consumer societies every day throws up new insurance requirements to be addressed. This permanent challenge is the branch's chief attraction as well as its principal handicap.

► Tailor-made policies. As a result of the aforementioned points there is frequent use, except in conventional products, of tailor-made policies or cover specially arranged for a specific risk.

In their early years, many of these policies will be subject to a trial period, and undergo modifications until a definitive wording is agreed.

► The perilous drift into high risk operations. Underwriting of contingency policies should be undertaken with great care and foresight. It would not be the first time that highly reputable

Peculiarities

insurance companies have become involved in pure gambling or speculation and have forgotten the industry's basic principles.

A non-life risk is insurable when, apart from representing valid, contingent and lawful business, it is specific and therefore capable of being delimited, analysed, selected and, lastly, assessed for valuation and, where appropriate, transfer to the insurer.

It is not our intention here to restate the general principles of the insurance business, but rather to highlight the true growth area for such a unique branch. It is essential to appraise the risk objectively with the aid of past experience, reliable in-house and third-party statistics, knowledge of the moral standing of the policyholder, proven policy wording, expert advice, etc. If not, we could drift into covering speculative risks, a practice far removed from correct insurance practice.

- ▶ Backing from a specialist reinsurer. From the foregoing it will be noted that the branch requires expert advice which on occasion may be found in the specialist reinsurance market. When starting out in one of these lines of business there will be a need for a specific facultative reinsurance policy, whereby the ceding company will be required to demonstrate the necessary expertise and financial resources and, above all, the underwriting capacity through significant retention limits.

- d. Liability for discharge agreements (*liquidator's indemnity*).
- e. Replacement of parent guarantee: transfer of liability to the insurance policy in the event of sale of subsidiaries (*parent guarantees*).
- f. Contractual third party liability. indemnification to exchange cover through the policy (*escrow replacement*).
- g. Breach of contract due to Force Majeure (*Force Majeure indemnification*).
- h. Indemnification to clients due to business interruption.

10. Sundry

Progressive pollution, multiple birth, loss of permits and licences, loss of documents, temporary loss of employment and salary, aquaculture and return of purchase price of goods (*10 years pay back, buy back guarantee*).

Conventional products

1. Cancellation Policies

These cover the non-recoverable expenses and fixed disbursements incurred by the policyholder in planning, preparing and mounting a performance, conference or any event for a group of persons, should there be a cancellation or postponement for any of the following reasons:

- ▶ Bad weather.
- ▶ Non-appearance of key persons due to death, accident or illness of the aforementioned or their close relatives.
- ▶ Sundry other reasons beyond the con-

trol of the policyholder, such as national mourning, epidemic, fire at headquarters, strike, etc.

Under the heading of "Bad Weather", rates are set based on rainfall and wind tables drawn up by the National Meteorological Institute and similar bodies. Such information is comprehensive and provides details of past weather experience, thereby allowing assessments in accordance with geographical region

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and time of the year.

Under "non-appearance" the report on the health and lifestyle of the insured party, together with scheduled or planned performances (tours) and previous experience, may give an indication of the risk quality.

Indemnification shall cover the following:

- ▶ Cancellations: when in compliance with any existing legal ruling part of the revenue is returned, the amount to be indemnified shall be that relating to insured fixed expenses, after deduction of revenue and subsidies generated by the show or the insured event.
- ▶ Postponements: Only extraordinary expenses, such as accommodation, living expenses, additional advertising costs and similar items, arising as



Examples of conventional products

| Types of Policies | Examples | Comments |
|------------------------------------|--|---|
| Cancellation Policies | Postponement of a bullfight and a rock concert at a village festival due to heavy rain, or cancellation of a medical conference because of an employee strike at the venue. | |
| Prize Policies | A leading financial institution decides to raffle amongst its savings account customers the chance of doubling their balances. | A study of actuarial statistics allows us to calculate the maximum loss in accordance with the number of prizes, the duration of the promotion and the level of customer balances. |
| | A well-known electrical appliance chain offered to return the purchase price to all customers if the Spanish football team had won the European Cup held in Portugal this summer. | Extensive knowledge of Spanish and European football and the individual quality of the relevant players enables us to assess our national team's chances. This time it was easy!. The policyholders are financial and service institutions, manufacturers and distributors, whereas the beneficiaries are the prizewinners. |
| | Bonuses promised by a nation's olympic committee to members of the athletic team who obtained a medal in the Athens olympics, or bonuses to a team of footballers for promotion to the first division. | Under this heading the policyholders are mainly sporting clubs, federations and other sporting bodies and the beneficiaries are sportspersons or sports teams. This section also considers the possibility that commercial sponsors may also figure as policyholders, in their capacity as financiers of different types of sporting events. |
| Policies for Advertising Campaigns | A hole-in-one in a golf tournament organized by a car manufacturer that offers one of its models as a prize. | |
| | A confectionery manufacturer offers a gift to consumers who submit a certain number of coupons, which are obtained on purchase of the products. "Collect 80 points and win a free CD". | Risk assessment is always based on the estimated number of gifts claimed as an indication of the campaign's success. A policy can be arranged to cover any excess over and above that figure, due to the unforeseen success of the campaign. The attraction of the gift on offer, the degree of difficulty in obtaining it and, most of all, past experience will ensure reliable risk assessment. |
| Film-making Procedures Policy | Business promotion by a leading financial institution, based on the public image of a well-known personality. After the campaign has been launched in the media, the individual is accused of tax evasion. | Only in-depth knowledge of the individual's state of health, lifestyle and conduct can give us an idea of the risk. It is a most delicate matter. |
| | Death of the leading actor during filming. It proves necessary to repeat several scenes with a new actor and alter the remainder of the script. | This is a typical non-appearance risk. The risk can only be correctly assessed with up-to-date information on the health and lifestyle of the insured parties. |
| | During the first printing, a roll of negative film is damaged. This necessitates repetition of all the scenes contained on it. | In practice, the risk of damage or loss of back-up tapes is usually limited to a given number of rolls or a stated amount. Information is always sought about the type of film, the name and installation facilities of the developing laboratory in addition to the mode of transport and the distance from the shooting location. |



a result of postponement of the performance or insured event, shall be indemnified.

Typical policyholders in these instances are organizers, promoters and sponsors of shows and events.

2. Prize Policies

The following two types are covered under this heading:

▶ **General public:** This policy aims to cover payment to the policyholder for specific prizes and rewards won by having accomplished or complied with the objectives described in the specifications or regulations of any contest, draw or competition open to the public through any form of mass media, such as press, radio or TV.

▶ **Sport:** This policy covers the policyholder for the value of the agreed prizes or bonuses when an athlete or team reaches or achieves a specific sporting goal or record.

3. Policies for Advertising Campaigns

Two categories with very different aims and objectives come under this heading:

▶ **Over-redemption Policy:** This covers payment to the policyholder of net consolidated losses arising from the excess of prizewinning or promotional awards over and above the number originally envisaged in any given advertising campaign.

Policyholders are mainly manufacturers and distributors of manufactured goods on sale to the public.

▶ **Key Persons Policies:** The purpose here is to indemnify the policyholder for expenses incurred in planning, preparing and developing the media advertising campaigns for one or more celebrities, should the event become non-viable or suffer from a clear fall-off in commercial interest due to the death of the celebrities or should they be prosecuted or involved in a public scandal to the detriment of their good name or reputation.

The sector to be covered under this heading is extensive and may involve any public or private body as well as their advertising agents.

4. Film-making Procedures Policy.

This is a multi-line policy covering expenses disbursed or undertaken by a film producer in connection with the following eventualities:

▶ **Pre-production/Production Risk:** por fallecimiento, enfermedad o accidente corporal de determinadas personas clave (director y actores) que den lugar a la interrupción o suspensión temporal o definitiva de los trabajos de rodaje.

This policy covers the additional expenses incurred by the policyholder in finishing the production, over and above those that would normally have been required.

The expenses already incurred by the producer up until the time of the physical incapacity of the key persons are also included, even though they may prove to have been in vain as a direct result of the changes made to finalize the filming.

▶ **Risk relating to negatives and video tapes:** This covers the insured film producer against financial loss caused by damage to the negatives during processing, storage or while in transit.

Expenses incurred in repairing or cleaning up the damaged tapes and, where applicable, repeat filming of the scenes that proved impossible to recover, are included.

▶ **Risk relating to cinematographic equipment, accessories, props and wardrobe:** this covers disbursements that the insured producer is obliged to make with respect to damage to equipment hired from third parties during the shooting process, as a result of fire, lightning or explosion, burglary or robbery with violence and flaws due to accidental breakage. ■