

Principles and Practice of General Insurance



Committee on Insurance and Pension
The Institute of Chartered Accountants of India
New Delhi

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This book is also a Study Material for Paper-2 of the DIRM Course of the Institute of Chartered Accountants of India, covering General Insurance portion of the syllabus. For Life Insurance portion (of Paper 2), the members may refer the book entitled 'Principles and Practice of Life Insurance'

FOREWORD

A successful insurance sector is fundamental to every modern economy since it encourages the savings habit as well as provides a safety net to rural and urban enterprises and productive individuals. The global and national insurance sector provides enough role to play by the members – both in practice and in service – of the Institute in view of their established brand in India as Complete Business Solutions Provider. With an objective to develop the width and depth of the professional reach, members of the Institute are being groomed to enter the insurance field with appreciable level of technical and practical acumen for which our profession is known for during all these years.

The fact that the Government of India has duly recognised our Institute by nominating the President in office as a member in the Insurance Regulatory and Development Authority of India clearly vindicates the emerging importance of our profession in this most dynamic field. Multi-pronged strategies are being adopted by the Institute such as the introduction of Post Qualification Course in Insurance and Risk Management (DIRM) to facilitate the members and students to acquire the technical and practical knowledge in the field of insurance.

The Committee on Insurance and Pension which administers the DIRM course has completely revised the DIRM Study Materials as a measure to provide the latest possible technical inputs for the members who are pursuing that Course. The material has brought out to enable other members of the Institute – who are not pursuing the DIRM course – to develop expertise on the key areas of insurance and pension fields.

I appreciate the efforts put in by Chairman, CA. Pankaj Jain and other members of the Committee. I wish that the members at large should make use of this material to the maximum possible extent in the overall interest of the stakeholders of our profession.

(Ved Jain)
President

PREFACE

With the appreciable level of contribution by insurance funds to financial savings and the GDP of India, development of insurance is necessary to support continued economic transformation of our country. Insurance is very necessary to protect enterprises against various risks.

It is our sincere belief that to enable the members of the Institute to play an appreciable level of role in the insurance and pension sectors, they need to be provided with a general framework for thinking about the effects of risk and a broad knowledge of risk management and insurance. They need to be aware of the many public policy issues related to risk, including legal liability and economic security issues apart from strong conceptual foundation for understanding institutional details.

I wish to take the pleasant privilege of presenting before the members of the Institute the revised study materials for the Institute's Post Qualification Course on Insurance and Risk Management (DIRM). The study materials have been grouped and brought out in such a way that members of the Institute - apart from those who have registered for the DIRM course - could peruse these publications to acquire strong technical foundation in the areas of insurance and risk management.

I wish to express my heartiest gratitude to the President of the Institute CA.Ved Jain and Vice President CA.Uttam Prakash Agarwal for their constant motivation to enable the Committee to move forward on its various endeavours. I wish to place on record my sincere thanks to the members of the Committee and Special Invitees on the Committee for their guidance and involvement in bringing out this publication. We are grateful to Mrs. V. Jayalakshmi of International Institute for Insurance and Finance, Hyderabad for preparing the basic draft of this material and Shri R. Parthasarthy of Chennai for reviewing the materials.

It is my sincere hope that the members of the Institute would find the contents of the book professionally enriching. With humility I invite your constructive comments to further improve the contents of the book.

(CA.Pankaj Jain)

Chairman,
Committee on Insurance and Pension

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CHAPTER – 1

INTRODUCTION TO GENERAL INSURANCE

OUTLINE OF THE CHAPTER

- Introduction
- History of General Insurance
- The Insurance Market
- Insurance Intermediaries
- Insurance Intermediaries in Overseas Markets
- Tariff Advisory Committee (TAC)
- Loss Prevention Association of India (LPA)
- Questions

LEARNING OBJECTIVES

- To study the historical evolution of the general insurance markets in India
- To understand the role of all players in the insurance markets
- To study the function of the Tariff Advisory Committee
- To evaluate the implications of Detariff regulations of IRDA
- To examine the services rendered by the Loss Prevention Association of India

INTRODUCTION

Man has always been in search of security and protection from the beginning of civilization. At the same time “Risk” is inevitable in life and any business activity. Again risk is closely connected with “ownership”. It is the owners who want to save themselves from risk and it is out of this desire, the concept of insurance has originated.

The aim and objective of insurance is to protect the owner from financial losses that he suffers for the risks that he has taken. The basis of insurance is sharing of losses of a few amongst many. Insurance provides financial stability and security to both individuals and organizations by this distribution of losses of a few among many by building up a fund over a period of time.

HISTORY OF GENERAL INSURANCE

Globally, the history of general insurance can be traced back to the early civilization. As the incidence of losses increased with the advancement of civilization, slowly the idea and concept of loss pooling and loss sharing started taking roots. Historical facts show that the Aryans through their cooperatives practiced the loss of profits insurances. The Mediterranean merchants also practised insurances from as early as the 4th century BC through the issue of bottomry bonds, which is an advance of money in a ship during the period of voyage, repayable on the arrival of the ship. The Code of Manu also indicates the practice of marine insurance by Indian with their counter parts in SriLanka, Egypt and Greece.

Marine insurance is the oldest type of insurance originating in England, as early as in the 12th century. The earliest transaction of insurance as practised today can be traced back to the 14th century AD in Italy.

General insurance as a whole, developed with the industrial revolution in the West and with the consequent growth of seafaring trade and commerce in the seventh century. In India too, evidence of insurance in some form can be traced as early as from the Aryan period. The British and some of the other foreign insurance companies through their agencies transacted insurance business in India. The first general insurance company in India was the Triton Insurance company Ltd., established in Calcutta in 1850 AD, with the British holding major share. The first general insurance company by Indian promoters was the Indian Mercantile Insurance company Ltd. started in Bombay in 1906-07. Following the First World War, several foreign insurance companies started insurance business in India, capturing about 40 percent of the insurance market in India at the time of Independence.

Insurance business in India is governed by the Insurance Act of 1938, which was amended later in 1969. However, in 1971, the government by an ordinance nationalized the general insurance business, under the General insurance Nationalization Act, 1972 to ensure orderly and healthy growth of the business. The then existing 107 companies were brought under the aegis of General Insurance Corporation (GIC) of India. The GIC was thus entrusted with the responsibility of superintending, controlling, and ensuring smooth and healthy conduct of the general insurance business in India along with its four subsidiaries in all the zones in India.

THE INSURANCE MARKET IN INDIA

A contract of insurance can be defined as a contract whereby one person, called the 'insurer' undertakes in return for a consideration, called the 'premium', to pay to another person called 'assured', a sum of money or its equivalent on the happening of a specified event. The happening of the specified event must involve some loss to the assured or at least should expose him to adversity, which in insurance parlance is called 'risk'. The underlying concept of insurance is to transfer the loss suffered by an individual to a willing and capable professional.



Providers

The Insurance market comprises the insurers, the buyers, and the intermediaries who mediate between the two parties and are rewarded for their efforts by the insurer. The insurance market in India hitherto consisted of the General Insurance Corporation of India (GIC) and its four subsidiaries namely:

- National Insurance Co. Ltd. with Head Office in Kolkata.
- United India Insurance Co. Ltd. with Head Office in Chennai.
- The New India Assurance Co. Ltd. with Head Office in Mumbai.
- The Oriental Insurance Co. Ltd. with Head Office in New Delhi

The GIC was formed on 1st January, 1973, under the Insurance Act, 1938 in accordance with the provisions of the General Insurance Business (Nationalization) Act, 1972. All the existing companies carrying on general insurance business in India were merged under Section 16 of the Nationalization Act, and notified by the government on 31.12.1972. Thus, from 1.1.1973, the four subsidiaries of GIC as mentioned above started insurance operations.

A brief review of the four public sector companies as subsidiaries of GIC under the nationalization program in chronological order is examined in the following paragraphs.

National Insurance Company is one of the four public sector companies. Since its incorporation in the year 1906 headquartered in Kolkata, the company had been carrying out general insurance business under private management until 1972, the year of its nationalisation. In the same year, 21 foreign and 11 Indian Insurance Companies were amalgamated with National Insurance Company Limited, as a subsidiary company of General Insurance Corporation of India.

The New India Assurance Company was incorporated on 23rd July, 1919 and commenced business from 14th October, 1919 with head office in Mumbai. In 1972, the year of its nationalisation, Government of India took over the management of the company along with all other non-life insurers in the country. New India Assurance (NIA) was subsequently reconstituted taking over 23 companies under the Scheme of Merger, following the nationalization of General Insurance Business in 1973.

United India Insurance Company Limited was incorporated as a Company on 18th February 1938 with its head office in Chennai, with 12 Indian Insurance Companies, 4 Cooperative Insurance Societies and Indian operations of 5 Foreign Insurers, besides General Insurance operations of southern region of Life Insurance Corporation of India were merged with United India Insurance Company Limited.

The Oriental Fire & General Insurance Co. Ltd., with its head office in New Delhi was incorporated in the year 1947 as a subsidiary of Oriental Government Security Life Assurance Co. Ltd. In 1956, Oriental became a subsidiary of the Life Insurance

Corporation of India until 13th May 1971, when the Government of India (GOI) took over the management of all general insurance companies in India.

This was followed by the nationalisation of general insurance business with effect from 1st January 1973 and the Oriental Fire and General insurance company came under the General Insurance Corporation of India as one of the four subsidiaries. It commenced its operations from 1st January 1975.

Later on in 2002, with the passage of Insurance amendment Bill (2002), all the four Public sector companies were delinked from GIC and are functioning as independent companies since then.

Following convergence of the financial services and financial institutions, the Indian government also initiated reforms based on the recommendations made in the Report of the Malhotra Committee, set up in 1993. As a result, the insurance sector was opened up to private participation to make the sector efficient, vibrant, and competitive.

At present, the Insurance Regulatory and Development Authority (IRDA), is the statutory body entrusted with the responsibility of regulation of operations of the insurance companies as well ensuring orderly development and growth of the insurance business in India. The primary concern of the IRDA is the protection of the policyholder's interest.

Following are the Life and General insurance companies operating their business. (Position as of 18th October 2008)

INSURANCE COMPANIES OPERATING IN INDIA

LIFE INSURERS	
PUBLIC SECTOR	PRIVATE SECTOR
1. Life Insurance Corporation of India (LIC)	1. Bajaj Allianz Life Insurance Co. Ltd. 2. Birla Sun Life Insurance Co. Ltd. (BSLI) 3. HDFC Standard Life Insurance Co. Ltd. (HDFC STD LIFE) 4. ICICI Prudential Life Insurance Co.Ltd. (ICICI PRU) 5. ING Vysa Life Insurance Co.Ltd. (ING VYSYA) 6. Max New York Life Insurance Co. Ltd. (MNYL) 7. MetLife India Insurance Co.Ltd. (METLIFE) 8. Kotak Mahindra Old Mutual Life Insurance Co. Ltd. 9. SBI Life Insurance Co. Ltd. (SBI LIFE) 10. TATA AIG Life Insurance Co. Ltd. (TATA AIG)



	<ol style="list-style-type: none"> 11. Reliance Life Insurance Co. Ltd. 12. Aviva Life Insurance Co. Ltd. (AVIVA) 13. Sahara India Life Insurance Co. Ltd. (SAHARA LIFE) 14. Shriram Life Insurance Co. Ltd. 15. Bharti AXA Life Insurance Company Ltd. 16. Future Generali India Life Insurance Company Limited 17. IDBI Fortis Life Insurance Company Ltd. 18. Canara HSBC Oriental Bank of Commerce Life Insurance Company Ltd. 19. AEGON Religare Life Insurance Company 20. DLF Pramerica Life Insurance Co. Ltd.
NON-LIFE INSURERS	
PUBLIC SECTOR	PRIVATE SECTOR
<ol style="list-style-type: none"> 1. The New India Assurance Co. Ltd 2. National Insurance Co. Ltd. 3. The Oriental Insurance Co. Ltd. 4. United India Insurance Co. Ltd. 5. Export Credit Guarantee Corporation Ltd. 6. Agriculture Insurance Company of India (AIC) 	<ol style="list-style-type: none"> 1. Bajaj Allianz General Insurance Co. Ltd. (BAJAJ ALLIANZ) 2. ICICI Lombard General Insurance Co. Ltd. (ICICI LOMBARD) 3. IFFCO Tokio General Insurance Co. Ltd. (IFFCO TOKIO) 4. Reliance General Insurance Co. LTD. (RELIANCE) 5. Royal Sundaram Alliance Insurance Co. Ltd. (ROYAL SANDARAM) 6. TATA AIG General Insurance Co. Ltd. (TATA AIG) 7. Cholamandalam MS General Insurance Co. Ltd. (CHOLAMANDALAM) 8. HDFC ERGO General Insurance Co. Ltd. (HDFC CHUBB) 9. Star Health and Allied Insurance Company Limited 10. Apollo DKV Insurance Company Limited 11. Future Generali India Insurance Company Limited 12. Universal Sompo General Insurance Company Ltd. 13. Shriram General Insurance Company Ltd. 14. Bharti AXA General Insurance Company Ltd.
RE-INSURER: General Insurance Corporation of India (GIC)	

Buyers

The buyers in the insurance market are the general public, traders, exporters, importers, industrial and commercial organizations, clubs, associations, hospitals, schools, etc. The intermediaries are the agents, and now-a-days new channels include brokers, corporate agents and financial institutions like banks (Bancassurance), micro-finance institutions etc. All the intermediaries are to be duly licensed by the Insurance Regulatory and Development Authority (IRDA).

INSURANCE INTERMEDIARIES

Insurance companies sell their products mainly through the following:

- i. Agents (who are the representatives of the Insurer)
- ii. Independent Intermediaries (who are the representatives of the Buyer)
- iii. Direct Sales including through 'online' and 'Referrals'.

Agents

In Insurance industry the term "Agent" is ordinarily applied to a person engaged by the insurer to procure new business. An Agent can work for one life insurer and/or one non-life insurer and in addition to this, to one 'exclusive health insurer'.

Insurance agents are intermediaries whose activities include soliciting, procuring, and servicing the general insurance market. An agent must fulfill the statutory requirements of his competence prescribed by the regulator and for which he has to pass the stipulated examination to satisfy the regulator after undergoing specified number of hours of training at accredited institutions (online / off-line). Upon the successful completion of the examination, all the agents in the insurance business are given license granted as provided under Insurance Regulatory and Development Authority (Licensing of Insurance Agents) Regulations, 2000, as amended upto date. Application for the same are to be made in prescribed form. The contract of agency between the company and agent defines the authority and responsibility and sets forth the agreement of the parties with respect to commissions and other details of the relationship. Agency license can also be granted to cooperative societies, panchayats, corporate entities, and banks. Renewal of license should be done in time by paying the prescribed fees.

However, no license can be granted, if the individual suffers from any of the following disqualification:

- if the person is a minor.
- if found to be of unsound mind by a competent court.
- if found guilty of or connived at any fraud, dishonesty or misrepresentation against any insured or insurer.



The appointment of agents is governed by Insurance Regulatory and Development Authority (Licensing of Insurance Agents) Regulations, 2000. The IRDA has prescribed both qualifications and disqualification for a person to be given a licence under section 42 of the Insurance Act.

A person must

- a) Be at least of 18 years of age.
- b) Have passed at least 12th standard or equivalent examination appointed if he/she resides in a place having a population of five thousand or more as per the last census, or 10th standard otherwise.
- c) Have undergone a training program of 50 hours in Life or General insurance business or any other pre-recruitment examination recognized by IRDA. (However there are reduction in the required hours based on insurance qualifications, etc. of the applicant for Agency.)
- d) For a composite agency, a person should have completed 75 hours of training in Life and General insurance business spread over 6 to 8 weeks.

An agency licence is usually given for 3 years, which may be either renewed or cancelled later. But before renewal of the licence, it is a prerequisite that the agent should have undergone 25 hours of practical training in Life and General Insurance business or at least 50 hours practical training in subject for a composite agency renewal. The agent is expected to procure a minimum premium amount depending upon the company rules and targets.

The agent is paid commission as remuneration for discharge of all his functions, the commission rates are subject to the guide lines issued from time to time by the IRDA.

Corporate Agents

The IRDA has also allowed Corporate Agents to act as insurance intermediaries to sell insurance products. As per the Act, a *Corporate Agent* means any person specified in clause (k) of the Act, and licensed to act as such, while a *Composite Corporate Agent* means a Corporate Agent who holds a licence to act as an insurance agent for a life insurer and a general insurer.

Qualifications

- The corporate agent should ensure that depending upon the nature of the entity, the Partnership Deed, Memorandum of Association or any other document evidencing the constitution of the entity shall contain as one of its main objects soliciting or procuring insurance business as a Corporate Agent.
- The corporate insurance executive shall possess the minimum qualification of a pass in 12th Standard or equivalent examination conducted by any recognised Board/Institution, where the applicant resides in a place with a population of five thousand or more as per the last census, and a pass in 10th Standard or equivalent examination from a recognised Board/Institution if the applicant resides in any other place.
- Should have completed from an approved institution, at least, fifty hours' practical training which may be spread over one to two weeks, in either life or general insurance business, as the case may be.
- Or shall have completed from an approved institution, at least, seventy five hours' practical training both in life and general insurance business, where such an applicant is seeking licence for the first time to act as a composite corporate agent.

The applicant seeking the Corporate Agency from the authority or any other corporate insurance executive of the applicant should be a professional as mentioned below:

- (a) an Associate/Fellow of the Insurance Institute of India, Mumbai;
- (b) an Associate/Fellow of the Institute of Chartered Accountants of India, New Delhi;
- (c) an Associate/Fellow of the Institute of Costs and Works Accountants of India, Calcutta;
- (d) an Associate/Fellow of the Institute of Company Secretaries of India, New Delhi;
- (e) an Associate/Fellow of the Actuarial Society of India, Mumbai;
- (f) a Master of Business Administration of any Institution/ University recognised by any State Government or the Central Government; or
- (g) possessing Certified Associateship of Indian Institute of Bankers (CAIIB); or
- (h) possessing any professional qualification in marketing from any Institution/ University recognised by any State Government or the Central Government;
- (i) (from 1.4.2009, it is compulsory that a Broker should have the Designated Person with qualification of AIII / FIII).



Besides individuals, some of the companies are making use of banks, building societies and others as agents to increase the new business volumes. Further, tied agency has also become a popular channel of distribution where in the tied agents are representatives of the company drawing commissions as remuneration.

Banks, under the contract of “bancassurance” which is the strategic alliance between an insurance company and the bank, where in the banks use their resources and client base to augment sales of insurance policies. This arrangement provides mutual benefit to the bank as well as the insurance company and more importantly value addition to the customer, who can derive insurance services also from his bank counter.

Independent Intermediaries (Brokers)

Brokerage has also become a very popular distribution channel for marketing Life and General insurance business. Also known as Independent financial advisors (IFAs), these advisors have become the popular source of procurement of business in the advanced markets. Brokers canvas the business and place the same with insurers either on standard or negotiated terms. They are also authorized to negotiate with insurers for tailor-made policies to cater to the customer’s specific needs. A broker usually does business with more than one company and in return gets commission. However, he does not charge anything from the client. He is bound by the IRDA Regulations to give best advice to his client and acts on behalf of the advice seekers. Basically, a Broker is the representative of the insurance buyer.

A broker is a through professional who is registered and licensed to offer his professional advice to the clients. IRDA has prescribed guidelines for Brokerage registrations under INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY (INSURANCE BROKERS) REGULATIONS, 2002. An insurance broker is an individual / firm / Company / Co-op. Society who advises policyholders on insurance matters and places business with the insurers. A high standard of professional skill and conduct is expected of a broker. Moreover, if he fails to maintain the required standard he may be liable for damages to his principal.

Although brokers are agents of the proposer, they are usually paid by the insurers with whom they place business.

In India, there are many licensed brokers who are engaged in procuring business in the domestic markets and also in international exchange of reinsurance business. Besides, these brokers also provide risk management consultancy services.

Agency and brokerage systems are most common and contribute maximum share of insurance business in the developing and developed countries.

IRDA Regulations limits on payment of Commission or brokerage on general insurance business

The IRDA under Section 14 of the Insurance Regulatory and Development Authority Act, 1999 and in terms of the provisions of Sections 40(1), 40A(3) and Section 42E of the Insurance Act, 1938, has laid down the percentage of premium that can be paid by way of **commission or brokerage** on a general insurance policy not exceeding the percentages of premiums set out below.

The IRDA also specifies that no brokerage can be paid in respect of an insurance where agency commission is payable and likewise, no agency commission can be paid in respect of an insurance where brokerage is payable.

The following are the current rates of commission as recommended by IRDA:

AGENCY COMMISSION STRUCTURE

Class of business	Agency commission (% of premium)	Brokerage commission (% of Premium)
1. Fire, engineering insurances	10%	12.5%
i. Individuals		
ii. Corporate clients (including PSUs) whose paid up capital is:		
a) Upto Rs.15 crores	10%	12.5%
b) Between Rs.15 crs & 25 crs	6.25%	7.25%
c) Over Rs.25 crores	5%	6.25%
iii. Risks qualifying as large risks under para 19(v) of File & Use Guidelines	5%	6.25%
2. Motor insurance business (other than third party)*, WC/ EL and statutory PL Business	10%	10%
3. Marine Hull insurance	10%	12.5%
4. Marine Cargo business	15%	17.5%
5. All other business	15%	17.5%



Please Note

- No commission shall be paid on motor third party insurance.
- Evidence of paid up capital can be taken from the latest Balance Sheet which is in public domain as per the requirements of the Companies Act, 1956. In case of a balance sheet which is 2 years prior to the relevant year of placing insurance, an auditor's certificate must be produced.
- In case of sole proprietorship and partnership firms a certificate from a Chartered Accountant to the client should be acceptable.
- In respect of branches in India of a foreign company reference should be made to the paid up capital of the company in the country in which it is incorporated converting it into Indian Rupees at the current exchange rate on the date of insurance.
- No payment of any kind, including "administration or servicing charges" is permitted to be made to the agent or the broker in respect of the business in respect of which he is paid agency commission or brokerage.
- These rates supersede all existing directions on the subject and shall take effect in respect of insurances or renewals commencing on or after 1st January, 2007.

Development Officers (DO)

This arrangement is in vogue in Public Sector Insurers, both in Life and Non-Life. This is purely an internal arrangement in organizing the marketing force of an Insurer. They are not covered under any Regulation of IRDA or other Statutes. They are governed by the service conditions of his/her employer only. Functionally, Development officer is a link between the branch manager in an insurance company and the agent. In particular, the Development Officer is a field worker and plays an important role in the promotion of insurance business and in increasing the sales of insurance policies. The development staff procures the General insurance business in India either directly or through agents. The development staff is usually full-time employees of the insurance companies. They are also required to procure the targeted business in the classes of business deemed as non-traditional classes.

Some of the main functions or duties of the Development officer as envisaged in the act include:

- Soliciting, negotiating, procuring, or effectuating an insurance contract or a renewal of an insurance contract
- Disseminating information relating to coverage or rates
- Forwarding an insurance application
- Servicing or delivering an insurance policy or contract

- Inspecting a risk
- Setting a rate
- Investigating or assessing a claim
- Transacting a matter after the effectuation of the contract
- Representing or assisting an insurer or other person in any other manner in the transaction of insurance with respect to a subject matter of insurance.

Some of the other general functions include:

- assist their agents in matters connected with procurement of new business
- make various plans for the development of insurance
- conduct research for the development of insurance business
- recruit, train, guide, and motivate agents for procuring business
- develop general insurance business in the area under their jurisdiction
- make rules for appointment, transfers, and promotions of various cadres of agents
- arrange training programs for agents
- review system of accounts from time to time
- to prepare and issue cover notes and kutcha (temporary) receipts for the business written.

Thus, the development officer acts as a vital link for the company. The insurance company monitors the activities of these officers through the integrated and monthly reports prepared by them. The reports show the work done by the officer, number of new policies issued, business procured, premium collected and the difficulties faced by them. Inefficient and non-performing officers are given training and motivation to perform better.

Direct Sales

The direct Sales force (DSA) refers to sales activity procured by the staff of the company itself has become a popular channel of distribution of insurance products now-days. The main advantage in this channel is that commissions need not be paid to the salaried staff. Generally this advantage of the commission savings is passed on to the consumers by way of premium discount by the life insurance companies. Nowadays, sales through internet or online sales is picking up particularly in case of retail insurance of Motor and Health. Payments are made through credit cards / internet banking. Receipts are generated online but the policies are dispatched by the Insurer subsequently. Referrals also contribute to direct sales and this mode is also picking up faster. Referrals provide the database already available with them, such as banks,



associations, etc. Referrals are not paid any commission but are compensated by way of fees, whether the individuals referred by the referrals ultimately buy insurance or not.

INSURANCE INTERMEDIARIES IN OVERSEAS MARKETS

The insurance intermediaries in the U.K. comprise part-time agents such as solicitors, accountants, bank managers, building societies, and estate agents who introduce their own clients to an insurance company. It is the brokers, who are full-time specialists, who are regarded as professionals with expert knowledge of insurance. Besides arranging for insurance, these brokers also offer risk management services, such as risk analysis, loss prevention advice, adequate insurance programming and placement of insurance with companies or at Lloyds of London (a corporate or individual underwriters who accept marine insurance business on their own behalf) at best possible rates. These brokers are required to be registered with the Brokers Registration Council (Registration) Act, 1977.

The U.S. insurance intermediaries are composed of three categories, such as Independent agents, who represent a number of companies, Exclusive agents, who work for a single company, and the General Agent, who in turn hire and train full-time agents to procure business under his direction and supervision. These General agents are empowered to accept and underwrite risks on behalf of the insurance companies and also issue policies.

In Japan, the agents are individuals, partnerships or corporate bodies who procure majority of the insurance business except marine. Marine insurance is sold directly through the staff of the insurance companies (direct distribution). Besides, the usual agents, there are also *canvassers* who sell monthly payment insurance schemes such as the householders and storekeepers policy, dwelling/ apartment fire insurance policy.

REFORMS IN THE INSURANCE SECTOR

The New Economic Policy initiated in the early 90s, threw open the banking and the mutual fund segments of the financial system to private participation. As a consequence of this endeavor, a great need was felt for the opening up of the insurance sector too, as insurance is also an integral part of the financial system. Therefore, Government of India appointed a Committee on Reforms in the Insurance Sector in 1993. The committee (known as Malhotra Committee) recommended the opening up of insurance sector to competition stating that introduction of competition will result in better customer service and the Committee recommended the following steps to be taken immediately for more equitable product pricing:

- a) Claims costs should be controlled by improved application of loss control and risk management techniques;
- b) Concerted efforts should be made to comprehensively review and reduce management expense ratios;

- c) Motor premium rates should be raised in light of persistently growing adverse motor claims experience;
- d) More frequent reviews of rates in all classes of business in light of changing experience in various classes of risks. For this purpose, the companies need to set up R&D Cells and upgrade statistical information and technology support to their present product pricing mechanisms.

One of the main objectives for recommendation for the opening up of the sector was to provide the consumer of insurance services wider choice so that he can get the benefits of competition in terms of range of insurance products, lower price of insurance covers and better customer service. The Malhotra Committee in its Report also recommended for opening of the insurance sector to private players with an independent regulator towards development of a competitive market.

Consequently, on April 19, 2000 Insurance Regulatory and Development Authority bill was passed creating IRDA to protect the interest of the policyholders, to regulate, promote and ensure orderly growth of the insurance industry and amended the Insurance Act, LIC Act and General Insurance Business Nationalisation Act thereby ending an era of exclusive privilege of the state owned companies from doing insurance business in India. New private players thereafter were licenced to enter the market and it was expected that with their innovative approaches and better use of distribution channels and technology, they would make a mark along with established public sector companies in the Indian Insurance Market for better service and faster growth.

The era of tariffs

The price of an insurance product is generally linked to the scope of the cover. The tariff mechanism provides floor rates for various insurance products based on estimates of average of all losses across insurance companies, average administrative costs including commissions and average expected profit.

In India, the Tariff Advisory Committee (TAC) established under the Insurance Act, 1938 was vested with the functions of administering the rates, terms, advantages and conditions in the general insurance business which are under tariff. The major classes of general insurance business under tariff regime as in 2006 before detariffing of the market were Fire, Petrochemicals, Engineering and Motor. Upto 1972, some data was being received at TAC from the insurers. After nationalization in 1972, the data flow reduced. Further, there was no system of dissemination of data to the public. Even the four public sector insurers were not able to publish consolidated data on each class of insurance. Thus, **scientific rating became a casualty**. As a result pricing of different classification of risks was done in an ad-hoc manner. This resulted in cross subsidization among different class of risks and also within a class the better risks subsidizing the loss making risks.



Apart from this, the insurer in a regulated market did not have the flexibility in pricing or innovation of products as they had to adhere to the terms and conditions of the tariff in letter and spirit. With the standardization of covers, freezing of rates, terms and conditions, there was little choice available to the insuring public in terms of products and prices. Thus, while the parameters or risk factors fixed in the tariff were adhered to for rating purposes, new and emerging risk factors could not be dove-tailed into the tariff for want of data on those factors. On the customers' side, there was a perception that the better risks were being charged as much premium if not more than those for the high risk ones. In short there was no distinction between good risks and bad risks as the same rate applied to all.

Post IRDA Act, 1999

The IRDA Act was enacted with the objective to protect the interests of insurance policy holders and to regulate, promote and ensure orderly growth of the insurance industry. Even after the opening up of the sector, although benefits of liberalization could be seen with increase in volumes of premium, there was little innovation in the tariff driven General Insurance business. Even after the opening up of the insurance sector, the general insurance business was predominantly governed by the tariffs prescribed by TAC. Considering prevalence of such tariffs against the principles of competition, there was a constant demand from insurers and other industry experts to abolish the tariffs. However, the authority felt that sudden removal of tariffs could result in unhealthy price-wars thereby affecting the solvency of the company itself. In other words, need for sustainable growth on scientific lines and enhanced customer satisfaction was the need of the hour. Hence the IRDA decided to initiate the process of detariff in a phased manner slowly as noted in the following paragraphs.

Motor Insurance: The Loss making portfolio in a regulated set up

Generally the countries with a tariff regime and with a controlled market tend to have higher premium than those of the free market. In India, however the situation is different. The motor premium rates were among the lowest in the world. The average motor premium ranges from 2 to 3 per cent of the value of the vehicle as compared to 8 per cent in western countries. The reason is due to the absence of data in the Indian market to support a justifiable pricing mechanism. The older insurers, who had a market share of more than 80 per cent were unable to generate adequate database to enable scientific calculations for risk assessment and rating of different groups of vehicles. Therefore, underwriting in the transport sector was perceived to be a losing proposition, with claims well over 120 per cent of the gross premium income. The net result was that the administered pricing became flawed in the absence of data. For the same reason, the commercial vehicle operators, users, lobbyists, Government or the Courts could not be convinced to approve increase in rates even in the wake of deterioration of claims experience of the insurers.

Traditionally, the following lines of business were governed by tariffs prescribed by Tariff Advisory Committee (TAC):

S. NO.	Department	Policy
1.	Fire	All India Fire Tariff Industrial All Risks Tariff CL (Fire) Tariff Petrochemical Tariff
2.	* Marine Hull	* Tariff for Ocean-Going vessels * Tariff for Dredgers * Tariff for Fishing Vessels/Trawlers * Tariff for Sailing Vessels * Tariff for Jetties / Cranes / Pontoons Insurance * Tariff for Builders. Risk Insurance * Tariff for Ship Repairers. Liability * Tariff for Charterers. Liability * Tariff for Ship Breaking Insurance
3.	**Marine Cargo	**Tariff for Marine Cargo
4.	Engineering	Erection All Risks/Storage-cum-Erection Tariff Contractors. All Risk Insurance Tariff Machinery Breakdown Tariff Boiler Pressure Plant Tariff Civil Engineering Completed Risk Tariff Contractors. Plant and Machinery Tariff Electronic Equipment Insurance Tariff Deterioration of Stocks (Potatoes) Tariff Loss of Profits (MB & BLOP)*** Tariff
5.	All India Motor Tariff	Act Policy Private Car Package Policy Motorized Two Wheelers. Package Policy Commercial Vehicle Package Policy Motor Trade Package Road & Transit Risks only Policy Motor Trade Internal Risks only Policy
<p>* Detariffed w.e.f. 1st April, 2005 ** Detariffed w.e.f. 1st April, 2004 *** MB: Machinery Breakdown; BLOP: Business Loss of Profit</p>		



Evolution of De-tariffing Concept

As discussed earlier, in a competitive market, the products need to be priced equitably based on their individual risk experience which was not practiced due to tariff restrictions. It was alleged that tariffs were rigid based on out-dated statistical data, and that premium rates were not revised in response to the market dynamics. It resulted in heavy cross subsidy of premium for those lines of business which had persistent high claims ratio, for e.g. Motor Third Party. Further, the private players refrained from underwriting the loss making areas such as stand alone liability policy and on the other, they clamoured for detariffing of motor portfolio. They also had in place sophisticated IT set ups and systems capable of statistical analysis of various risk factors over and above the ones prescribed by the motor tariff. The awareness among customers in the wake of liberalization also resulted in a movement towards risk based rating rather than a rigid tariff structure. Representations were received too by the IRDA that insurers were not willing to offer Mandatory Third Party Liability cover and that there were loading the own damage policies.

The Authority therefore considered moving to a tariff free regime in a phased manner. It constituted a Committee under the Chairmanship of Justice T.N.C. Rangarajan to examine the various aspects of motor underwriting including de-tariffing and pooling arrangements.

Rangarajan S. Committee on Motor Insurance

The Committee assisted by members representing the insurance companies, automobile manufactures, car owners, truck operators consumers, policyholders, surveyors, an advocate and a representative of the Government of India has studied at length on the issues and difficulties faced by various interests of the industry. Third party liability insurance being the only way of funding social security, worldwide, the system of compulsory vehicle insurance is followed. The report has mentioned the advantages, of, and fears, that were expressed on the projected de-tariffing.

The advantages projected were:

- Competition will improve efficiency
- Efficiency will lead to reduction of premia and benefit policyholders
- It is part of the reforms towards liberalized economy.

The fears apprehended were:

- De-tariffing may make insurance unavailable at reasonable premia
- Companies may form cartels and jack up the premia
- Free market may lead to insolvency of companies and loss of protection for policyholders.

The problems relating to the own damage portion of the motor tariff were examined by a committee. Suggesting for de-tariffing, the committee stated that liberalization means allow the market to function in the competitive environment. It expressed hope that competition would improve efficiency and consumers will benefit by not only price reduction but also value addition while industry may benefit by introduction of newer technology and innovation. It also added that by de-tariffing, companies would be interested in marketing their products innovatively and with cost cutting may reduce the premia to gather a wider market share.

However, de-tariffing requires safeguards for uninsurable vehicle owners. There should be a mechanism for an appeal to an insurance pool which would consider proposals rejected by the companies and grant insurance on premium loaded according to risk perception.

At the end of their study, the Committee recommended that the IRDA may:

- a) Quarantine the Third Party liability insurance business and its accounting in insurance company's books;
- b) Request the Government of India to review the statutory liability for third party liability for motor vehicle accidents;
- c) Set up an independent data bank under TAC and compel the companies to supply the data to the bank, and draw on the bank data to justify proposed tariffs;
- d) De-tariff the own damage business of motor portfolio under a competitive premium setting model by a file and use procedure with a time frame for the change over.

Steps taken by IRDA (For Motor)

As the committee after examining various alternatives finally concluded that the initial step in regard to de-tariffing of the premium structure could be undertaken in the case of the own damage portion of the motor insurance, a meeting of all CEOs of the general insurance companies was held in Hyderabad on 6th of May, 2003. The meeting agreed unanimously to usher effective 1st of April, 2005 a system of free pricing on the own damage portion of the motor liability.

As a follow up of the recommendations made in the report of Justice Rangarajan Committee, Authority constituted a committee under the chairmanship of Shri S.V. Mony for preparing a roadmap to detariffing of the premium structure of Own Damage portion of the Motor Insurance.

However, in order to derive the rates in a scientific manner based on market dynamics, it is essential to have accurate data on the different lines of business, which was abysmal in the general insurance industry. The insurers were unable to generate adequate database to enable scientific calculations for risk assessment and rating of different groups of vehicles. For free-pricing of products, data base relating to different



classes of risks had to be collected, compiled, disseminated and analysed which was a time consuming activity. Hence, the de-tariffing of Motor OD Business could not take off on 1st April, 2005, as proposed earlier and the general insurers expressed that the de-tariffing should take place across the board for all business portfolios instead of Motor (OD).

A small beginning

Pending the issue of de-tariffing of motor (OD) insurance, Tea Crop Insurance (2) Cardamom Insurance (3) Coffee Insurance (4) Rubber Insurance (5) Package policy for exporters under Duty Exemption Scheme were de-tariffed w.e.f. 01/04/04 and all the non-life insurance companies were advised to file the products with IRDA under file and use procedures of Authority.

De-tariffing of Marine Hull Insurance

Continuing the spirit of competition, all general insurers who wish to write marine hull class of business were allowed to go out of the tariff from 1.4.2005. However, it was mandated that they shall follow the existing policy wordings, terms and conditions including clauses such as the Institute clauses till further orders.

Data Collection

To fill up the gap of non-availability of accurate data for proper pricing, as a first step, IRDA in consultation with the insurers devised new formats for collection of past data as well as future data in the field of motor and health insurance. New formats were devised taking into account various risk factors hitherto not considered by the rigid tariff structure.

For instance, the salient features of the new format for collection of motor data were the introduction of various code masters. The code masters relate to

- i) Insurer
- ii) Policy
- iii) Class of vehicle
- iv) Make of vehicle
- v) Zone
- vi) Cubic Capacity (CC)/ Passenger Carrying Capacity (PCC)/ Gross Vehicle Weight (GVW)
- vii) Nature of loss
- viii) Nature of goods
- ix) Permit

- x) Road Type
- xi) Driver Type
- xii) Driver Age
- xiii) Driver experience
- xiv) Driver education
- xv) Incurred claims experience
- xvi) Claims History of the vehicle
- xvii) Nature of injury
- xviii) Occupation
- xix) Reasons for Court Hearing and
- xx) Type of Summons

These formats covered the details on driver, geographical zone of driving and the vehicle which are indispensable for rate fixing in equitable manner in a detariff regime.

Road map for a tariff free regime

With the intention to ensure that there is an orderly movement from tariff regime to the future set up, on 23rd September, 2005, IRDA circulated a detailed note to all general insurers outlining the various steps to be taken by insurers for movement to a tariff-free market. Considering the existence of tariffs contrary to free-market forces, the road map has emphasized the need for strengthening internal capabilities of insurers.

IRDA enunciated the various steps to be taken by insurers in the following areas:

- i) Underwriting
- ii) Rating of risks
- iii) Policy terms and conditions
- iv) Corporate governance

Exposure Draft Guidelines on File & Use procedures

After notifying the road map, the Exposure draft on File & Use guidelines prepared by IRDA was placed on the website of IRDA seeking comments of insurers and industry for filing of products, to be filed once de-tariffing takes place. The guidelines were discussed at length and the responses were consolidated for finalizing of the guidelines.



Guidelines on File & Use procedures for general insurance products

Based on the feedback received on the exposure draft guidelines on File & Use procedures, IRDA requirements for consideration and review of products under File & Use guidelines along with underlying logic are as under:

- (i) Design and rating of products must always be on sound and prudent underwriting basis. The contingencies insured under the product should be clear and provide transparent cover which is of value to the insured.
- (ii) All literature relating to the product should be in simple language and easily understandable to the public at large. As far as possible, a similar sequence of presentation may be followed. All technical terms should be clarified in simple language for the benefit of the insured.
- (iii) The product should be a genuine insurance product of an insurable risk with a real risk transfer. Alternate risk transfer or financial guarantee business in any form will not be accepted.
- (iv) The insurance product should comply with all the requirements of the Protection of Policyholders Interests Regulations 2002.
- (v) Insurers should use as far as possible, similar wordings for describing the same cover or the same requirement across all their products. For example clauses on renewal of insurance, basis of insurance, due diligence, cancellation, arbitration etc., should have similar wordings across all products.
- (vi) The pricing of products should be based on appropriate data and with technical justification.
- (vii) The terms and conditions of cover shall be fair between the insurer and the insured.
- (viii) Margins built into rates shall be consistent with the experience of the insurer in respect of commission, management expenses, contingencies and profit.
- (ix) Insurer should take necessary steps in ensuring that competition will not lead to unprincipled rate cutting and other improper underwriting practices.

Final take off

Finally, the IRDA confirmed withdrawal of tariffs effective from 1st January, 2007. It was reiterated that the tariff general regulations, other than those relating to rating viz. terms, conditions, clauses, warranties, policy wordings etc. shall continue to be followed until further orders. In case of the mandatory motor TP, where the insurers have been expressing difficulty to underwrite unless they are permitted to charge the premium that they consider appropriate (which means heavy premium in commensuration with

high claim ratios of motor portfolios) rates are prescribed by regulator. The Authority also issued Order directing insurers that they shall not refuse cover for third party risks. The underlying reason for existence of price regulation is consumer pressure to avoid enhancement of premium and to ensure that insurers shall provide motor third party liability insurance cover to all vehicles.

Formation of Motor Third Party Insurance Pool

As per Section 34 of the Insurance Act, the IRDA directed that all general insurers registered to carry on general insurance business including motor insurance business or general reinsurance business shall collectively participate in a pooling arrangement with the following provisions to share in all motor third party business written by any of the registered general insurers:

- 1. Participation in pooling arrangement:** Every insurer registered to carry on general insurance business (including motor insurance business) or general reinsurance business shall automatically participate in the pooling arrangement to the extent set out herein.
- 2. Underwriting insurers:** Every underwriting office of every insurer that is authorized to underwrite motor insurance business for the insurer shall also be authorized to underwrite motor third party insurance business that will be shared among all insurers through the pooling arrangement.
- 3. Pooling mechanism:** The pooling of business among all insurers will be achieved through a multi-lateral reinsurance arrangement between the underwriting insurer and all the other registered insurers carrying on general insurance business (including motor insurance business) and general insurance reinsurers.
- 4. Participation in motor third party insurance pooled business:** The participation of General Insurance Corporation of India (GIC) in the Pooled business shall be such percentage of the motor business that is ceded to it by all insurers as statutory reinsurance cessions under Section 101A of the Insurance Act. The business remaining after such cession to GIC shall be shared among all the registered general insurers writing motor insurance business in proportion to the gross direct general insurance premium in all classes of general insurance underwritten by them in that financial year.
- 5. Underwriting of business:** Underwriting offices of insurers shall follow the underwriting instructions of the General Insurance Council in the matter of procedures for underwriting and documentation and accounting and settlement of balances. The business shall be underwritten at rates and terms and conditions of cover as notified by the Authority from time to time. No vehicle owner shall be denied third party insurance cover in respect of his vehicle which is holding a valid permit for use on public roads except on grounds of attempted fraud.



6. **Claims processing and settlement:** All claims in respect of third party death or injury or physical damage shall be processed for settlement in a speedy and efficient manner in accordance with the instructions of the General Insurance Council. For this purpose, the Council shall adopt a pro-active claims settlement policy adopting the most efficient claims processing practices possible.
7. **Administration of the Pooling arrangement:** The GIC shall act as the administrator of the pooling arrangement. It will act under the guidance of the General Insurance Council. For this purpose, the Council may establish such Committees of insurers as are necessary to operate the Pooling arrangement and process and settle claims in the most efficient manner.
8. **Remuneration:** There will be no agency commission or brokerage payable in respect of motor third party insurance business. The underwriting insurer will be paid a reinsurance commission of 10% on the premium ceded by it to all the other insurers and reinsurers. The GIC as administrator shall be paid a fee of 2.5% of the total premium on motor third party insurance business in respect of the business underwritten for the pooled account. Each insurer shall bear the cost of hardware required to operate the pooling arrangement within its offices. The GIC will bear the cost of hardware necessary to administer the pooling arrangement in its offices. The cost of the operating software for the pooling arrangement shall be shared by all the insurers and reinsurers in the manner decided by the General Insurance Council. Each insurer shall bear the cost of travel of its executives to attend to the work relating to the pooling arrangement. However, any travel specifically to service a claim shall be recoverable as claims related expenses.
9. **Agreement:** The insurers and GIC shall enter into a multi-lateral reinsurance arrangement to give effect to this pooling scheme.
10. **Review:** The Authority will review the operation of the pooling arrangement and the need for regulation of the premium rates and terms of cover and will issue such directions from time to time as may be considered necessary.

Managing the Transition

It may be noted carefully that de-tariffing does not imply or mean that the companies can set the premium whimsically. It facilitates setting competitive premium model where there is neither excessive pricing nor non-viable premium undercutting which may create instability. The companies are encouraged to promote better underwriting decisions and the products filed have to be justified with supporting data regarding the rates. If the companies were to undercut the premium to uneconomical levels, then again they would be brought back by the losses that they may face.

Therefore, IRDA, since its inception firmly believed that sustainable growth in the insurance industry is possible only in an environment which values and promotes

financial stability, increased management capability and total public accountability. This necessitates in turn, good corporate governance practices to be followed in the companies as well as with the regulator. With this objective the Authority conducts off-site and on-site supervision at periodic intervals in order to assess the soundness of the insurance company.

TARIFF ADVISORY COMMITTEE

The Tariff Advisory Committee (TAC) is a statutory autonomous body in India under the Insurance Act, 1938. It formulates and administers tariff for major classes of General Insurance business such as Fire and Allied perils, Petrochemicals, Marine Hull, Engineering and Motor etc. TAC also regulates terms and conditions that are offered by the insurers.

The TAC is a body of experts headed by the Chairman of the (IRDA) GIC as an ex-officio Chairman, and representatives from insurance companies, Ministry of Finance and Bureau of Industrial Costs and Prices (BICP), Government of India. Further, technical groups consisting of representatives of insurers as well as of the TAC have been constituted for various classes of insurance. These groups assist the TAC in making changes in ratings from time to time, in relation to loss experience. The TAC, while evaluating and rating a risk takes into consideration, the past loss record and physical features of the risk such as safe distances between blocks, provision for Fire fighting appliances, and good house-keeping. Further, the TAC also specifies special ratings and discounts to extend the benefits of lower premiums to the insured. The TAC at regular intervals interacts with the insured's interest groups, Surveyors, Associations, Trade bodies, and other forums. It also advises on upgrading safety standards, and makes publications of Fire Protection Systems and Building regulations etc.

History of TAC in the pre and post De-tariffed era

Before understanding the role of TAC in the detariffed regime, a brief peep into the past history of TAC will throw light on the objectives behind the setting up of this committee, the reasons leading to the government to detariff and the role assumed by this committee at present in the detariffed regime.

Basically, Insurance in India started without any regulations in the nineteenth century of British colonial era. However, after the independence, the Life Insurance business was nationalized in 1956, and the general insurance business was nationalized in 1972, with 4 insurance companies operating under the supervision of General Insurance Corporation of India (as discussed in the earlier part of this chapter). It was expected that the subsidiary companies would provide effective competition to each other. As seen, these companies acquired considerable experience, expertise and financial strength over the decades and also established reasonable standards of conduct of business.



Role of TAC in the present de-tariffed era

With the abolition of tariffs, the role of Tariff Advisory Committee has undergone a change. TAC is now entrusted with the following functions in the changed scenario:

- Collection of data on premiums and claims, analysis of such data and dissemination of the results to the insurers
- Report to IRDA on the underwriting health of the market and any aberrations in market behaviour
- Constitution of Expert Groups at the request of the General Insurance Council, to look into underwriting issues and recommend necessary action
- Organize training to underwriters at the market level and
- Attend to public grievances on non-availability of insurance and try to resolve the issues by discussion with insurers.

Therefore, finally Detariffing refers to the withdrawals of rates in specified class of insurance by the Regulator. In other words, it means all the insurers have the freedom to price based on their experience and judgment. It improves the variety and make competitive the price of insurance products. The Committee also recommended that the area under tariffs should be progressively reduced with the object of limiting it to only few classes to promote competition and improve underwriting skills.

LOSS PREVENTION ASSOCIATION OF INDIA (LPA)

It was due to the increasing incidence of fire accidents, road mishaps, industrial accidents, damage to cargo resulting in loss to cargo and life that the GIC has initiated steps in setting up of the LPA to prevent such losses and minimize their consequences. The Loss Prevention Association of India Ltd is engaged in promoting safety and loss control through education, training and consultancy in India and abroad.

The LPA is a company limited by guarantee established in January 1978. It is sponsored by the GIC of India and its four subsidiaries. GIC and its subsidiaries provide the entire finances for all its activities. Membership subscription and fees for services are also source of finance for LPA.

LPA's work involves both educational and engineering aspects of safety. To meet these requirements, the Association employs a team of professionals with expertise in various technological aspects of loss prevention.

While, the insurance companies constitute ordinary members, some of the organizations such as Central Building Research Institute, Central Road Research Institute, Indian Institute of Packaging, and Indian Standards Institute, are honorary members of LPA.

The main objectives of the LPA are as follows:

- To create awareness and appreciation of the need for loss prevention and loss reduction.
- To provide advice and expertise on techniques of loss prevention
- To educate public and workers in techniques of loss prevention.
- To support research efforts in various fields of loss prevention.
- To organize and supervise facilities at marine terminals for cargo loss minimization.
- To organize fire salvage operations.

The activities of the LPA are very wide and comprehensive ranging from conducting mass communication campaigns to draw the attention of the public for the need and methods of loss prevention.

Some of the important activities broadly include:

- * Development of training programmes on fire safety, material handling, road safety and a host of other related subjects. These programmes are aimed at supervisory and managerial personnel.
- * Providing safety and risk analysis services, including identifying and evaluating exposures to property damage, and other accident hazards affecting an organisation.
- * Offering risk management service aimed at identifying risks to which manufacturing and business houses are exposed, suggesting appropriate risk control and transfer strategies. This also includes analysis of total insurance portfolio from coverage and adequacy point of view. In providing these services, the LPA works hand-in-hand with other professional organizations like the Bombay Fire Brigade and Salvage Corps, in their efforts to reduce and prevent fire accidents in industrial sector as well as at homes.
- Undertaking fire protection system inspection and certification as per Tariff Advisory Committee (TAC) norms.
- Publication of manuals, handbooks, guidelines, periodical newsletter for disseminating information on safety through its quarterly journals-Loss Prevention News and Road Safety Digest. LPA also provides advice on safety through posters, bulletins, leaflets, data sheets etc.



Questions



1. Discuss the historical evolution of the general insurance business in India.
2. Discuss the importance and need for training and qualified professionals in insurance selling, in the wake of competition.
3. How does the TAC fix and regulate the rates for various general insurance policies?
4. Discuss the various services rendered by the LPA in India.

CHAPTER – 2

GENERAL INSURANCE CONTRACT DESIGN

OUTLINE OF THE CHAPTER

- Introduction to Insurance
- Definition of a contract
- Requirements of an Insurance contract
- Fundamental Principles of General Insurance contracts
- Questions

LEARNING OBJECTIVES

- To understand the mechanism of insurance as a risk transfer system, a business and a contract
- To understand the application of the provisions of the Indian Contract Act to insurance contracts
- To study the fundamental principles governing general insurance contracts
- To examine the various provisions required for enforcement of an insurance contract

INTRODUCTION TO INSURANCE

Every individual family and business organization needs insurance, for inherent risk exposures to which they are exposed. Insurance seeks to redress the assured from the financial consequences of the loss exposures in the event of the uncertain event happening, resulting in a loss of his assets, or properties or even income earnings.

Insurance is actually a combination of three elements

- A transfer system
- A business
- A contract

Insurance as a Transfer System

As a transfer system, insurance enables a person, family or business to transfer the costs of losses to an insurance company. In turn the company pays for the insured



losses and distributes the costs of losses among all insureds. Thus, the key elements of insurance as a transfer system refers to the transferring of risks from the insured to the insurance company which is financially sound and has the capacity and willingness to take risks. The person transfers the consequences of a loss to the company, thereby exchanging the possibility of a large loss for the certainty of a much smaller periodic payment (premium). For transferring a cost of loss it is not necessary for a loss to occur or exist. A mere possibility of a loss constitutes a loss exposure that can be insured or transferred.

A Loss exposure can give rise to three types of losses, namely:

- Property loss (including net income loss),
- Liability loss, and
- Human and personnel loss.

On the other hand, sharing of risks implies the pooling of premiums paid by the insureds into a fund out of which the losses are paid as and when they occur.

Thus, the role of insurance is to protect insured's assets from the financial consequences of loss. But, not all risks are insurable. Insurance covers only pure risks. (Discussed in Chapter I of Module I).

Insurance as a Business

As a **business**, insurance primarily attempts to meet its costs and expenses from the premium that it earns and also make a reasonable margin of profit for its own sustainability. As a business organization, it provides jobs to millions of people in life and non-life insurance companies, agencies, brokerage firms. The various operations of these companies include marketing, underwriting, claims handling, ratemaking and information processing. As a business concern, it also needs to satisfy the regulators, insureds and others of its financial stability. Therefore, to protect the consumers, the regulator monitor the rates, policy forms, solvency margins, and also investigate complaints and consumers' grievances. In addition to payment of losses, the business of insurance offers several benefits to individuals and families and to the society as a whole such as:

- Payments for the costs of covered losses
- Reduction of the insured's financial uncertain
- Efficient use of resources
- Support for credit
- Satisfaction of legal requirements
- Satisfaction of business requirements
- Source of investment funds for infrastructure development
- Reduction of social burden

However, the benefit of insurance is not cost free. There are some direct costs as well as indirect costs which are incurred, such as the premiums paid, operating costs of the insurers, opportunity costs, increased losses, and increased law suits.

Insurance as a Contract

As a **contract**, an insurance policy is a legally enforceable contract. The contract is between the insurance company and the insured. Through insurance policies, the insured transfers the costs of losses to insurance company. In return for the premiums paid by the insured, the insurers promise to pay for the losses covered under the policy.

The policy contains all the terms and conditions for its enforceability, and the benefits payable by the insurer. The breach of these conditions by either party will result in the invalidation of the contract. Thus, through the coverage provided by insurance policies, the individuals, families and businesses are enabled to protect their assets, and minimize the adverse financial affects of losses. Hence, an insurance contract needs to be interpreted and carefully designed so that, all fortuitous losses are covered and insured against.

The most common four basic types of insurance (property, liability, life and health) are generally divided into two broad categories:

1. Property/Liability insurance
 2. Life/Health insurance
1. Property insurance provides coverage for property and net income loss exposures. It protects an insured's assets by paying to repair, or replace property that is damaged, lost, or destroyed or by replacing the net income lost and extra expenses incurred as a result of property loss.

Liability insurance covers the liability loss exposures. It provides for payments on behalf of the insured for injury to others or damage to others' property for which the insured is legally liable.

2. Life and health insurance cover the financial consequence of human (personal) loss exposures. Life insurance replaces the income-earning potential lost through death and also helps to pay expenses related to insured's death. Health insurance provides additional income security by paying for medical expenses. Disability income as popular in most of the Western countries, replaces as insured's income if the insured is unable to work because of injury or illness.

DEFINITION OF 'CONTRACT'

An agreement enforceable by law is called a contract. It creates certain rights and obligations for parties agreeing to it. A valid contract is one, which the court enforces.



Requirements of an insurance contract

Insurance contracts are also governed by the provisions of the Indian Contract Act, 1872. In general, there are four requirements that are common to all valid contracts. To be legally enforceable, an insurance contract must meet these four requirements:

1. Offer and acceptance
2. Consideration
3. Capacity
4. Legal purpose

1. **There must be valid offer and acceptance:** The first requirement of a binding insurance contract is that there must be an offer and an acceptance of its terms. In most cases, the applicant for insurance makes this offer, and the company accepts or rejects the offer. An agent merely solicits or invites the prospective insured to make an offer.

A legal offer by an applicant for insurance must be supported by a tender of the premium and it should always be prior to commencement of the 'coverage'. The agent usually gives the insured a conditional receipt that provides that acceptance takes place when the insurability of the applicant has been determined by the Insurer.

In property and liability insurance, the offer and acceptance can be oral or written.

2. **Promises must be supported by the exchange of Consideration:** A consideration is the value given to each contracting party. The insured's consideration is made up of the monetary amount paid in premiums, plus an agreement to abide by the conditions of the insurance contract. The insurer's consideration is its promise to indemnify upon the occurrence of loss due to certain perils, to defend the insured in legal actions, or to perform other activities such as inspection or collection services, or loss prevention and safety services, or as the contract may specify.

3. **Parties must have legal capacity to contract:** This requirement of a valid insurance contract is that each party to a contract must be *legally competent*. This means the parties must have legal capacity to enter into binding contract.

Parties who have no legal capacity to contract include:

- Insane persons who cannot understand the nature (obligations and liabilities) of the agreement
- Intoxicated persons
- Corporations acting outside the scope of their charters, bylaws, or articles of incorporation, or authority
- Minors

Note:Minors normally are not legally competent to enter into binding insurance contracts; but most states have enacted laws that permit minors, such as a teenager age 15, to enter into valid life or health insurance contract.

4. **Agreement must be for legal purpose:** For insurance policies, this requirement means that the contract must neither violate the requirements of insurable interest nor protect or encourage illegal ventures. In other words, an insurance policy that encourages or promotes something illegal and immoral is contrary to public interest and cannot be enforced.

Example:

A street pusher of heroin and other illegal drugs cannot purchase property insurance policy that would cover seizure of the drugs by the police.

FUNDAMENTAL PRINCIPLES GOVERNING GENERAL INSURANCE CONTRACTS

The business of insurance aims to protect the economic value of assets or life of a person. Through a contract of insurance the insurer agrees to make good any loss on the insured property or loss of life (as the case may be) that may occur in course of time in consideration for a small premium to be paid by the insured.

Apart from the above essentials of a valid contract, insurance contracts are subject to additional principles. These are:

- Principle of Utmost good faith
- Principle of Insurable interest
- Principle of Indemnity
- Principle of Subrogation
- Principle of Contribution
- Principle of Proximate cause

These distinctive features are based on the basic principles of law and are applicable to all types of insurance contracts. These principles provide guidelines based upon which insurance agreements are undertaken.

A proper understanding of these principles is therefore necessary for a clear interpretation of insurance contracts and helps in proper termination of contracts, settlement of claims, enforcement of rules and smooth award of verdicts in case of disputes.



The Principle of Utmost Good Faith

Definition

A positive duty voluntarily to disclose, accurately and fully, all facts material to the risk being proposed, whether requested or not.

This principle of insurance stems from the doctrine of “*Uberrimae Fides*” which is essential for a valid insurance contract. It implies that in a contract of insurance, the concerned contracting parties must rely on each other’s honesty.

Normally the doctrine of “*Caveat Emptor*” governs the formation of commercial contracts which means ‘*let the buyer beware*’. The buyer is responsible for examining the good or service and their features and functions. It is not binding upon the parties to disclose the information, which is not asked for.

But in case of insurance, the products sold are intangible. Here the required facts relate to the proposer, those that are very personal and known only to him. The law imposes a greater duty on the parties to an insurance contract than those involved in commercial contracts. They need to have utmost good faith in each other, which implies full and correct disclosure of all material facts by both the parties to the contract of insurance.

The term “*material fact*” refers to every fact or information, which has a bearing on the decisions with respect to the determination of the severity of risk involved and the amount of premium. The disclosure of material facts determines the terms of coverage of the policy. Any concealment of material facts may lead to negative repercussions on the functioning of the insurance company’s normal business.

Non-disclosure of any fact may be unintentional on the part of the insured. Even so such a contract is rendered voidable at the insurer’s option and it can refuse any compensation.

Any concealment of material facts is considered intentional. In this case also the policy is considered void. The intentional non-disclosure amounts to fraud and un-intentional disclosure amounts to voidable contract.

For example, disclosures in life insurance pertain to age, income, health, residence, family details, occupation and plan of insurance. Similarly, in case of property or general insurance, the material facts pertain to the details of the property (car) such as year of make, usage, model, seating capacity etc. particularly in case of marine insurance, the insurance company may not always be in a position to inspect the ship at the port physically and it relies solely on the facts provided by the insured. Hence it is imperative on the part of the insured to disclose all the facts voluntarily.

Utmost good faith principle imposes duty of disclosure on both the insurance agent and the company authorities also. Any laxity at this point may tilt judgments-in favor of the insured in case of a dispute.

However, some the following facts need not be disclosed:

- Circumstances which diminish the risk (such as fire or burglary alarms set)
- Facts which are known or reasonably should be known to the insurer in his ordinary course of business
- Facts which are waived by the insurer
- Facts of public knowledge
- Facts of law
- Facts covered by policy conditions.

Breach of duty of Utmost Good Faith

Breach of duty of Utmost good faith arise under one or both of the following:

- a) Misrepresentation which may be either innocent or fraudulent with reference to false facts, material to the acceptance or assessment of the risk.
- b) Non-disclosure which may be either innocent or fraudulent gives grounds for avoidance by the second party where a fact is within the knowledge of the first party and not known to the second party.

Principle of Insurable Interest

Definition

The legal right to insure arising out of a financial relationship recognized under the law, between the insured and the subject matter of insurance.

The existence of insurable interest is an essential ingredient of any insurance contract. It is an important and fundamental principle of insurance. Insurable interest simply means “right to insure”. The policyholder must have a pecuniary or monetary interest in the property, which he has insured. The subject matter of insurance can be any type of property or any event that may result in a loss of a legal right or creation of a legal liability.

Therefore the essentials of insurable interest include:

- There must be some property, right, interest, liability or potential liability capable of being insured.
- It is this property, right etc, which must be the subject matter of insurance.
- The insured must stand in a relationship with the subject matter of insurance whereby he benefits from its safety, well being or freedom from liability and would be prejudiced by its loss, damage or existence of liability.



- The relationship between the insured and the subject matter of insurance must be recognized at law.

For example, the subject matter of insurance under a fire policy can be a building, stocks, machinery, under a liability policy it can be a person's legal liability for injury or damage, a ship in a marine policy etc. Any damage to the property must result in financial loss to the policyholder. Only then insurable interest is said to exist.

There are a number of ways in which insurable interest will arise or be limited:

- a) **By Common Law:** under common law insurable interest is automatically created by 'ownership' rights. Similarly, the common law of 'duty of care' that one owes to the other may give rise to a liability which is also insurable.

For E.g. the owner of a tractor who depends on it for his agricultural operation stands to lose financially if the tractor meets with an accident, as his business will come to a standstill. Thus the owner has an insurable interest in the asset, i.e., his tractor. Hence the tractor forms the subject matter when insurance is purchased on it.

- b) **By Contract:** sometimes insurable interest is also created by contractual obligations. For example, a lease agreement between a landlord and a tenant may make a tenant responsible for the maintenance or repair of the building. This contract places the tenant in a legally recognized relationship to the building which gives him insurable interest.

- c) **By statute:** sometimes an act of parliament may create insurable interest either by granting a benefit or by imposing a duty.

Application of insurable interest

There are three main categories of application of Insurable interest as mentioned below:

- Life

Every individual has unlimited insurable interest in his or her own life. In life insurance context, insurable interest is deemed to exist in the case of certain relationships based on sentiment. (E.g. Husband & wife, parent & child) Insurable interest is also deemed to exist when the members of a family are in business together. Under such circumstances, it is not the family ties which create insurable interest but it is the extent of financial involvement that creates insurable interest. The business partners can insure each other's lives because they stand to lose in the event of the death of any of them.

- **Property**

Insurable interest normally arises out of ownership where the insured is the owner of the subject matter of insurance, such as a car or a house. Sometimes, there are some other financial relationships that give rise to insurable interest although they do not involve full ownership. They include:

- Part of joint ventures – wherein the joint owner is treated as trustee for the other owner[s].
- Mortgagees and Mortgagors – the insurable interest under a mortgage sale arises for the purchaser (mortgagor) from the ownership of an asset and for the financial institution (mortgagee) as a creditor, it is limited to the extent of the loan.
- Executors and Trustees – insurable interest arises out of the legal responsibility vested in them for the property kept in their charge.
- Bailees – who are responsible to take reasonable care of the goods which are in their custody, have insurable interest.
- Agents – where a principal has insurable interest, his agent can effect insurance on his behalf.

- **Liability**

The concept of liability insurance is very different from property and life assurance. In this insurance, it is not possible to predetermine the extent of the insurable interest because there is no way of knowing how often one may incur liability and in such a case, what would be the monetary value of such liability. Thus, in other words it is implied that insurable interest in liability insurance is without monetary limit, but in practice it is possible to make a realistic judgment as to the maximum liability that may be incurred. Hence it can be said that a person has insurable interest to the extent of any potential liability which may be incurred by way of damages and other costs (limited by sum insured which is the max. expected liability quantum).

Another important aspect in the application of the principle of insurable interest is the time of its application. While in life insurance, insurable interest needs to be present at the inception of the contract or policy, there is no requirement at the time of a claim under the policy. On the contrary, insurable interest in the subject matter of insurance must be present at the time of loss in a marine insurance contract, and it means in other words, that there need be no insurable interest when the insurance is effected.

In all other insurance policies, insurable interest must be present both at the time of inception of the contract and as well as at the time of loss.



Insurer's insurable interest

Like the insured, the insurance companies also derive an insurable interest having assumed liability under the policies which they issue. In other words, they may insure with another insurer a part or all of the risk they have assumed. This is usually done under a contract of Reinsurance.

Principle of Indemnity

The dictionary meaning of 'indemnity' is 'the protection or security against damage or loss or security against legal responsibility'.

Indemnity may be referred to as a mechanism by which insurers provide financial compensation in an attempt to place the insured in the same pecuniary position after the loss as enjoyed just before it. The literal meaning of the term "Indemnity" is making good the loss. *On the happening of the insured event for which the insurance policy is taken up the insured should be replenished the amount of loss.*

This principle sets the rule according to which insurance companies undertake to compensate the insured upon fulfillment of all the stipulations that are agreed upon in the insurance contract. The insurer charges a small amount as premium for undertaking the liability to cover the risk and in return promises to pay the value of the insurance policy or the amount of loss whichever is lower.

The principle of Indemnity ensures that the insurer is liable to pay up to the amount of loss and not more than that. In other words it implies that the insured should not derive any unwarranted benefit from a loss.

Normally the principle of indemnity applies to property and liability insurance contracts and it promises that the insured be restored to the same financial position that existed prior to the occurrence of loss.

Whenever the insurance company indemnifies the insurer for the full value of the insurance policy (when the asset is completely damaged) the insurer takes possession of the damaged asset to realize the salvage value.

Importance of the principle of indemnity

1. The principle of indemnity is important in the sense that it ensures that the insured does not derive any undue benefit from the loss.

Example –

Mr. Kumar had insured his car for Rs. 5 lakhs. The car met with an accident and was damaged. The loss suffered was valued at Rs.1 lakh. As per the principle of indemnity the compensation to be paid will be based on the amount of loss, i.e. Rs. 1 lakh. In case the compensation exceeds Rs. 1 lakh, Mr. Kumar stands to gain from the loss.

2. The principle of indemnity also aims to control moral hazard. It is possible that the insured may try to secure the maximum amount through dubious and unfair means. For example he may:

- Deliberately inflict loss upon the property to seek compensation
- Resort to exaggerating the loss
- Make false claims, etc.

Such claims when accepted confer undue profits on the insured. The insured may try to inflate the value of the property and over insure it to seek profit. If the compensation to be paid by the insurer is limited to the market value of the loss or less, it would put a check on this avenue for undue gains for the insured. Thus the principle of Indemnity helps to eliminate this possibility. This is demonstrated in the following example:

Example –

Mr. Ajay owns a restaurant, which he had bought three years ago for Rs. 2 lakhs. He had bought fire insurance worth Rs. 1.6 lakhs (which is the written down value of his insured property). His restaurant caught fire and the amount of loss suffered was worth Rs. 90000.

The amount of compensation to be paid by the insurance company
 = Rs. (sum insured/value of insured asset) * actual loss
 = Rs. (1.6 lakhs/2 lakhs) * 90000
 = Rs. 72000

Indemnity in practice

Even though the property is fully covered, all covered losses are not actually paid in full amount of loss since it would contravene the provisions and implications of the principle of indemnity.

As per certain provisions in force the amount of compensation paid can be less than the loss suffered. They are:

i. Actual Cash Value (ACV)

The actual amount of payment to be made by the insurer for the loss is based on ACV of the property, which is insured. Usually ACV is determined using the following three methods:

1. Replacement cost less depreciation

In this method ACV is the written down value of the property after taking into account the depreciation and inflation in the value of the property over a period of time.



Thus actual cash value = (replacement cost - depreciation)

Example –

Suppose a Machinery is purchased by A five years ago at a cost of Rs. 10 lakhs.

The cumulative depreciation on the machine for the five years (@ 10% Straight Line Method)

= Rs. 5 lakhs

Replacement cost = Rs. 10 lakhs

Hence ACV = Rs. (10 - 5) lakhs

= Rs. 5 lakhs

2. Fair Market Value (FMV)

FMV, which is the price that would normally be determined in a free market during a transaction entered into by a willing buyer and a willing seller, can be taken as ACV where replacement cost cannot be determined.

The concept of fair market value can be better understood by the following case. X owns an independent house property purchased ten years ago for Rs. 15 lakhs. The Municipal authorities are developing a cremation ground on the uninhabited land near the property of Mr. X. Hence the market value of property has come down for the property due to lack of market interest in the property and the only prospective buyer is willing to pay Rs. 8 lakhs for the property.

In case of any loss to the property the fair market value will be considered to be Rs. 8 lakhs by the insurance authorities.

3. Broad Evidence Rule

In this method ACV is determined scientifically applying techniques such as replacement cost less depreciation, FMV, discounting income streams derived from the property, taking the value of similar property, etc.

Here the method of judgment and application of commonsense is resorted to by the experts to reach an agreeable value.

ii. Other Insurance

In case the insured has taken up two policies for the same property, the compensation will be paid proportionately according to ACV by both the insurers. Thus the insured cannot benefit by resorting to multiple policies for the same property.

Example –

A stevedoring company owns an ocean steamer valued at Rs. 32 crores. The steamer has been insured with three different insurance companies A, B and C. The amount underwritten by A is Rs. 6 crores, by B is Rs 10 crores and by C is Rs. 16 crores. Thus the total sum insured amounts to Rs. 32 crores. The steamer meets with an accident and the loss is valued at Rs. 4 crores.

Hence the liability of each individual insurer

= (Amount underwritten by the insurer * amount of loss)/total sum insured

So the liability of insurer A

= Rs. $(4 * 6)/32$

= Rs. 75 lakhs

The liability of insurer B = Rs. $(4 * 10) / 32$ = Rs. 1.25 crore.

The liability of insurer C = Rs. $(4 * 16) / 32$ = Rs. 2 crores.

How indemnity is provided

Most of the general insurance policies contain the following wordings:

The company may at its option indemnify the insured by payment of the amount of the loss or damage or by repair, reinstatement or replacement.

In other words, indemnity is made in the following ways:

- Cash payment – for the amount payable under the policy
- Repair – most extensively used method of providing indemnity (motor claims)
- Replacement – commonly used in glass insurance
- Reinstatement – used in restoring or rebuilding machinery or building under engineering insurance policies

Factors limiting the payment of indemnity

The maximum amount recoverable under any policy is limited by the sum insured [or the limit of indemnity]. The actual amount payable to the insured is governed by a number of considerations:

- Average – this is applicable where an insured deliberately or otherwise underinsures his property. Application of this principle would make the insured his, own insurer to the extent of underinsurance [i.e. the difference between the value of the property and the sum insured].
- Excess – it is the amount of each and every claim which is not covered by the policy. Excesses may be voluntary or compulsory. Most common in private car policies, where accidental damages could be insured for 80% or 90%.



- Limits – refers to the limit in the amount to be paid for certain events, as mentioned by the wording in the policy. E.g. value of pictures, works of art restricted to 5% of the total sum insured in household policies.
- Deductible – refers to very large excess. Claims exceeding the deductible amounts become payable by the insurer.

Principle of indemnity– Exception to the rule with respect to life insurance (In non-life insurance this covers Personal Accident Insurance and certain types of Health Insurance such as ‘Critical Illness’, ‘Hospital Cash’, etc., where the agreed amount is paid as claims without having to establish the actual spending by the policyholder).

The life of a person is different from a material or property. The principle of valuing material property like replacement cost less depreciation and discounted cash flows cannot be applied to determine the monetary value of the life of a person.

The value of life is broadly determined by certain qualitative factors and is subject to one’s opinion. The most important factor here is the earning capacity of the person and the insurable value is the value of the policy taken up by the person.

A life insurance policy is not subject to the principle of indemnity but is a valued policy wherein the agreed upon amount in full is paid to the beneficiary in case of loss of life.

Principle of subrogation

Subrogation means the restitution of the rights of an assured in favour of the insurer against the third party for any damages caused by him in place of the assured after the insurer has indemnified him for the loss.

The principle of subrogation is invoked when a third party is responsible for the loss.

It is to be noted that on the happening of the event for which the asset has been insured and after the damage has been caused the insured can sue the party who has caused the damage to claim compensation for the loss. Alternatively the insured can seek compensation from the insurance company.

In case the insured opts for the latter course he loses the right to sue the party, who has caused the damage and seek further compensation from him. In accordance with the principle of subrogation the insurance company acquires the right of the insured to sue the third party to compensate for his negligence and loss inflicted upon when it indemnifies the insured for the losses suffered by him.

Example –

Mr. X was on his way to office in his car when it was hit from behind by a Lorry, and the lorry driver was drunk. Here X can claim compensation from the insurance company. The insurer in turn can sue the lorry owner Y for the damages.

Here X has no right of action against Y since he has already been paid compensation for the loss.

The principle of subrogation is a corollary of the principle of indemnity and is applicable when the damage has been caused due to the negligence or highhandedness of another party. Principle of indemnity seeks to make good the financial loss suffered by the insured by the insurer.

Thus after having been compensated for the loss the insured is restored to the same financial position as he was before the incident.

In case he is allowed to sue the damaging party again he stands to make a profit from the loss, which is inconsistent with the principle of indemnity.

In the case of *Castellain Vs Preston*, Preston the owner of a house property entered into a transaction under which he contracted to sell his house. The property was insured against fire. Before the transfer of title of the property to the buyer, the house was partly damaged by fire. The insurer for the loss indemnified Preston.

After that the sale was completed and the buyer paid the full price that was agreed upon to Preston. Ultimately the insurer came to know about this and filed a suit against Preston on the ground that since he received the full price he doesn't stand to incur any financial loss from the mishap. So there is no valid reason for him to receive payment from the insurer. The court accepted the insurer's stand and ordered Preston to return the amount indemnified by the insurer.

Importance of the principle of subrogation

The principle of subrogation serves to achieve the following objectives:

1. It prevents the insured from profiting from the damage, i.e., obtaining compensation twice for the same loss.
2. It enforces the rule of law that the guilty is brought to book and made to pay for the loss.
3. It helps the insurer to partially or fully recover the amount paid for the loss.
4. It helps to lower the insurance rates. With reimbursements from the concerned third party, the insurance company's losses are substantially scaled down, the benefit of which in turn is passed on to the final policyholder by way of reduction in premium.

Whenever the insurance company indemnifies the insured for the full value of the insurance policy (when the asset is completely damaged) the insurer takes possession of the damaged asset to realise the salvage value.

It has to be noted that if the value of compensation recovered by the insurance company from the responsible third party is more than the amount indemnified to the insured, the



insurer has to return the excess amount to the insured (after deducting the expenses incurred in recovering the money such as legal charges, etc.).

In the case where the insured himself takes action against the negligent party the insurer is not liable to pay any compensation.

If the insured comes ahead to relieve the negligent party from his liability for the loss that may happen when the concerned person is a close relation of the insured, the insurer is not liable for compensation as his right to sue the negligent party is lost.

Applicability of the doctrine of subrogation

Necessarily the principle of subrogation applies to general insurance (other than insurance on human) only. It has no relevance with respect to life insurance or health insurance since the principle of indemnity on which it rests upon applies exclusively to general insurance.

There can be no subrogation on anyone's life. In case of loss of life the insurance company has to pay the assured amount to the beneficiary of the insured. Here the insurer has no right of action against the third party for financial claims even if the loss of life was caused by him.

Limitations of the doctrine of subrogation

1. This doctrine is not applicable to life insurance policies, so the insurer has no right of action against third parties responsible for the death.
2. The doctrine becomes operative only after the insured has been indemnified. There is no relation between the indemnity provided for and the exercise of subrogation. The insurer may not be able to recover the same amount by exercising the right of subrogation against the third party.
3. Subrogation cannot be exercised where the assured is not in a position to take action against the damaging party.

Example –

Mr. Bhagat had insured his personal computer. It was damaged by his teenage son Jagat who smashed it with a cricket ball in a fit of rage. In this case Mr. Bhagat does not want to subject his son to any action. Hence the insurer is not obliged to make payment for the loss.

Principle of Contribution

Definition

Contribution is the right of an insurer to call upon others similarly, but not necessarily equally liable to the same insured to share the cost of an indemnity payment. This principle of contribution enables the total claim to be shared in a fair way.

The doctrine of contribution operates as a corollary of the doctrine of Indemnity and hence is applicable in case of general insurance.

As per the doctrine of contribution the indemnity provided for the loss occurring on the asset, which is insured with several insurers has to be proportionately shared among them according to the rateable proportion of the loss.

The amount of total compensation or indemnity provided to the insured by all the insurers should not exceed the amount of loss.

Sometimes when the value of the asset is very high the amount of risk involved is higher and that particular asset if insured by the company forms a significant portion of the total risk. This in turn increases the business (operation) risk of the insurance company. Usually insurance companies try to concentrate on a higher number of policies of lower value for diversification benefits. Diversification serves to reduce the overall risk level of an insurance company.

Rather than avoiding business arising from high value assets insurers follow the practice of underwriting high value assets partially. Thus a single insurer takes up a part of the total value of the asset and the asset is insured by a group of two or more insurance companies.

This practice has further implications particularly in case of settlement of claims relating to such contracts. The question of how much of the compensation is to be borne by each Insurer has to be addressed. It is here that the *doctrine of Contribution* is applied to resolve such complications.

The insured has the choice to recover from any insurer on a priority basis. After recovering the share of loss from the first insurer the insured can approach other insurers as per the doctrine of contribution.

In case one insurer indemnifies the insured in full the concerned insurance company can claim the share of compensation from other insurance companies.

Requisites to invoke the doctrine of contribution

1. The insured asset/Person (in case of hospitalization insurance) must be common to all the policies
2. The risk insured against must be common to all the policies



3. The insured owner of the asset must be the same person
4. All the policies must be in force during the occurrence of loss

Example–

1. Where there are two insurers covering the asset equally, in case of loss each has to contribute half of the compensation.

Principle of Proximate Cause

Definition

It is not the latest, but the direct, dominant, operative and efficient cause that must be regarded as proximate.

When an insurance policy is bought it is issued with respect to some peril, which may result in loss to the policyholder. No policy covers all types of risks. The insurance company is liable to indemnify only against the insured perils.

The term “Proximate cause” literally means the nearest cause or direct cause. In insurance parlance it relates to the immediate cause of the mishap, which resulted in the loss.

In general insurance there are numerous policies on vehicle insurance, property insurance, fire insurance, burglary insurance, etc. Each policy offers protection from the risks that are mentioned in the policy.

If a person has bought fire insurance for his house the protection will be from the loss caused by fire, which may have resulted from the sources mentioned in the policy. In case the fire occurs from any source other than that mentioned in the policy the insurer is not liable to compensate the insured.

For example if the person is insured to be protected against fire occurring due to electric short circuit and the fire occurs due to leakage of LPG cylinder then the insurance company is not liable to pay for the losses. In this case only if the fire were caused by short circuit would the loss be covered.

All the details related to proximate cause have to be clearly mentioned at the time of entering into the contract. Sometimes the causes not covered by the policy have to be expressly mentioned and though it is impossible to mention the whole range of causes that are to be avoided they are usually assumed by implication. The replenishment of compensation proceeds strictly depend upon the causes agreed upon.

Determination of proximate cause

Where the mishap occurs as a single event the determination of Proximate Cause is simple and that particular event can be attributed for the loss. In case where the loss occurs as a chain of events in succession with one event setting off the other it

may be difficult to determine the exact cause of the damage. In such an eventuality the parties have to carefully examine and find out the correct reason for the loss, the extent to which the loss has been caused by the proximate cause and the amount of compensation to be paid based upon it. It may happen that the actual peril, which has caused the loss in turn, is caused by another peril.

It has to be noted that while determining 'proximate cause' the sequence of events according to their *time of occurrence is irrelevant*. The deciding factor is the correct cause of loss.

Many court judgments act as precedents in arriving at decisions while making settlements. They have been set out below:

I. The insurer is liable:

- When the peril is a single event and it is insured.
- Where the *insured peril* (the event for which the policy has been taken for protection) occurs first and it is followed by an *excluded peril* (the event which has not been covered by the policy, i.e., which is not insured). Here the insurer has to pay for the loss, which had occurred up to the happening of the excluded peril only if the two perils can be distinguished from each other.
- Where the excluded peril causes the insured peril and the events occur in a broken sequence the insurer has to pay for the loss caused by the insured peril.
- Where both the perils are occurring concurrently and both the events are independent of each other.

II. The insurer is not liable:

- Where the excluded peril is the cause of the insured peril and they act consecutively
- Where the insured peril is followed by the excepted peril and both cannot be distinguished from each other.
- Where both the perils are occurring concurrently

Examples –

1. In the case of Tootal Broadhurst Lee & Co vs. London & Lancashire Fire Insurance Co. the fire was caused by an earthquake. Here earthquake was not part of covered risk hence the insurer was not liable as the loss was proximate to an excepted peril.
2. In case where fire causes an explosion (an excepted peril), the insurer will be liable for fire damage up to the time of explosion.



3. In the case of Marsden vs City and Country Assurance Co., Marsden had insured his plate glass from any risk except fire. Eventually a fire occurred in the neighbouring premises and in the commotion that followed some miscreants broke into the premises by smashing the insured plate glass to commit theft. As per the verdict the proximate cause of the loss was mob ambush and not the fire. Hence the insurer was liable for the loss.

Questions



1. Discuss the applicability of the Indian Contract Act, 1872 to an insurance contract.
2. Discuss the consequences that follow for non-disclosure of material facts in a contract?
2. Explain how the principle of insurable interest adds legal validity to an insurance contract. Cite the instances of life insurance contracts where insurable interest has to be proved.
4. Why is the principle of indemnity not applicable to life insurance contracts? Explain how the principle of indemnity controls moral hazard and undue benefit to the insured in a general insurance contract.
5. Discuss the subrogation rights of an insurer.
6. What are the principles behind the doctrine of contribution? Explain the mechanism behind contribution through rateable proportion of the loss.

CHAPTER – 3

INSURANCE LEGISLATIONS

OUTLINE OF THE CHAPTER

- Introduction
- General Insurance Business Nationalization Act, 1972
- The Insurance Act, 1938
- Insurance Regulatory Authority
- Insurance Regulatory and Development Authority
- Other legislations governing insurance business in India
- Questions

LEARNING OBJECTIVE

- To study the provisions of the various legislations governing the general insurance business in India
- To study the evolution of the regulatory body to monitor the insurance operations in India

INTRODUCTION

Insurance business is one of the most highly regulated businesses globally for reasons of equity and efficiency. It has a well-defined regulatory and legislative framework to operate. Insurance law by itself is both unique and comprehensive because it operates within the limitations of all the other governing legislations and ensures the legal provisions by incorporating the same in its various policies.

The transactions of general insurance business in India are governed by two main statutes, namely:

- The Insurance Act, 1938
- General Insurance Business (Nationalisation) Act, 1972

THE INSURANCE ACT, 1938

This Act was passed in 1938 and was brought into force from 1st July, 1939. This act applies to the GIC and the four subsidiaries. The act was amended several times in the years 1950, 1968, 1988, 1999. This Act specifies the restrictions and limitations



applicable as specified by the Central Government under powers conferred by section 35 of the General Insurance Business (Nationalization) Act.

The important provisions of the Act relate to:

Registration: Every insurer is required to obtain a Certificate of Registration from the Controller of Insurance, by making the payment of requisite fees. Registration should be renewed annually.

Accounts and audit: An insurer is required to maintain separate accounts of the receipts and payments in each class of insurance viz. Fire. Marine and Miscellaneous Insurance. Apart from the regular financial statements, the companies are required to maintain the following documents in respect of each class of insurance:

- Record of Cover notes specifying the details of the risk covered
- Record of policies
- Record of premiums
- Record of endorsements
- Record of Bank guarantees
- Record of claims
- Register of agency force and business procured by each with details of commission
- Register of employees
- Cash Books
- Reinsurance details
- Claims register

Investments: Investments of insurance company are usually made in approved investments under the provisions of the Act. The guidelines and limitations are issued by the Central Government from time to time.

Limitation on management expenses: The Act prescribes the maximum limits of expenses of management including commission that may be incurred by an insurer. The percentages are prescribed in relation to the total gross direct business written by the insurer in India.

Prohibition of Rebates: The Act prohibits any person from offering any rebate of commission or a rebate of premium to any person to take insurance. Any person found guilty would be punished with a fine up to five hundred rupees.

Powers of Investigation: The Central Government may at any time direct the Controller or any other person by order, to investigate the affairs of any insurer and report to the central government.

Other Provisions: Other provisions of the Act deal with the licensing of agents, surveyors, advance payment of premium and Tariff Advisory Committee (TAC).

- Prohibition of rebates
- Powers of investigation
- Licensing of agents
- Advance payments of premiums
- Tariff Advisory Committee

GENERAL INSURANCE BUSINESS NATIONALIZATION ACT, 1972

This Act came into force on 1st January, 1973. This Act gave effect to clause (c) of Article 39 of the constitution of India.

Article 39 (c) read as follows:

“The State shall direct its policy towards securing that the operation of the economic system does not result in concentration of wealth and means of production so as to prove harmful to the common interest of the community”.

Under this Act, there were no longer private insurers in the country. As a result general insurance business became the domain of the State. The General Insurance Corporation of India (GIC) became the holding company with four subsidiaries, namely United India Insurance Company with Head Office in Madras, Oriental Insurance Company with Head Office in New Delhi, National Insurance Company with Head Office in Calcutta and New India Assurance Company with Head Office in Bombay.

The ownership of all shares of both the Indian insurance companies and the foreign insurers from then on vested in the Central Government with effect from 1.1.1973. The services of all the personnel in the private sector were also transferred to the holding company and subsidiaries based on factors such as qualification, seniority, position and location.



Objectives of the Act

The object of the Act was primarily,

- To provide for the acquisition of the shares of the existing general insurance companies
- To serve the needs of the economy by development of general insurance business
- To establish the GIC by the central government under the provisions of the Companies Act of 1956, with an initial authorized share capital of seventy – five crores
- To aid, assist, and advise the companies in the matter of setting up of standards in the conduct of general insurance business
- To encourage healthy competition amongst the companies as far as possible
- To ensure that the operation of the economic system does not result in the concentration of wealth to the common detriment.
- To ensure that no person shall take insurance in respect of any property in India with an insurer whose principal registered office is outside India
- To carry on of any part of the general insurance business if it thinks it desirable to do so
- To advice the companies in the matter of controlling their experience and investment of funds.

The Mission of GIC

- To provide need-based and low cost general insurance covers to rural population
- To administer a crop insurance scheme for the benefit of the farmers
- To develop and introduce covers with social security benefits
- To develop a marketing network throughout the country including areas with low premium potential
- Promote balanced regional development irrespective of cost considerations
- To make benefits of insurance available to the masses.

INSURANCE REGULATORY AUTHORITY (IRA)

The Insurance Act, 1938, recommended the appointment of the Controller of Insurance, to ensure the compliance of the various provisions under the Act by insurance companies. The Controller approves the terms and conditions of various

plans and adequacy of premiums. The Authority also periodically scrutinizes the return on investments, annual accounts, and periodical actuarial valuation submitted by insurance companies.

The IRA consists of not more than seven (see below) members out of which a Chairman and two members representing the Life and general insurance business are appointed on full time basis. The whole time members shall hold office for 5 years or until the age of 62 (65 years for the Chairman) whichever is earlier. The part time members hold the office for not more than 5 years.

Composition of Authority

The Authority shall consist of the following members, namely:-

- (a) a Chairperson;
- (b) not more than five whole-time members;
- (c) not more than four part-time members,

to be appointed by the Central Government from amongst persons of ability, integrity and standing who have knowledge or experience in life insurance, general insurance, actuarial science, finance, economics, law, accountancy, administration or any other discipline which would, in the opinion of the Central Government, be useful to the Authority

The important duties of the IRA include the following:

- To regulate, promote and ensure orderly growth of the insurance business
- To exercise all powers and functions of the Authority
- To protect the interests of the policyholder with regard to settlement of claims and other terms and conditions
- To promote and regulate professional bodies connected with insurance organization
- To undertake inspection, investigation, and audit of companies, intermediaries, and other organizations connected with the insurance business.
- To regulate and control the rates of non-tariffed general insurance policies under section 64(u) of the Insurance Act.
- To prescribe the format for the maintenance and submission of accounts by insurers
- To regulate the investment of funds
- To regulate the margins of solvency
- To adjudicate disputes between the insurer and intermediaries.



INSURANCE REGULATORY AND DEVELOPEMNT AUTHORITY (IRDA)

The Committee on reforms of the insurance sector under the chairmanship of Shri R N Malhotra, ex-governor of Reserve Bank of India, recommended for the creation of a more efficient and competitive financial system in tune with global trends. It recommended amendments to regulate the insurance sector to adjust with the economic policies of privatization. The government in pursuance of the recommendation of the committee, decided to establish a Provisional Insurance Regulatory and Development Authority in 1996, to replace the erstwhile authority called the Controller of Insurance constituted under the Insurance Act, 1938, which initially worked under the Ministry of Commerce and later transferred to the Ministry of Finance.

Finally, the decision to establish the Insurance Regulatory and Development Authority was implemented by the passing of the Insurance Regulatory and Development Authority Act, 1999. In India, presently after the opening up of the insurance sector, the regulator for the monitoring of the operations of the insurance companies is the IRDA, having its head office in Hyderabad. The regulatory framework mainly aims to focus on three areas, viz.,

- The protection of the interest of the consumers
- To ensure the financial soundness of the insurance industry
- To pave the way to help a healthy growth of the insurance market where both the government and the private players play simultaneously.

Some of the important duties, powers and functions of Authority include to

- Issue certificate of registration, to applicants interested in insurance business, and also to renew, modify, withdraw, suspend or cancel such registration
- Specify requisite qualifications and practical training for insurance intermediaries and agents
- Specify the code of conduct for surveyors and loss assessors
- Levy fees and other charges for carrying out the purposes of this Act
- Control and regulate the rates, terms and conditions that may be offered by insurers in respect of general insurance business
- Regulate investment of funds by insurance companies
- Regulate maintenance of margin of solvency
- Adjudication of disputes between insurers and insurance intermediaries
- Supervise the functioning of the Tariff Advisory Committee

- Specify percentage of life and general insurance business to be undertaken by the insurer in the rural or social sector.

The Authority shall consist of the following members namely a chairperson, five whole-time members and four part-time members, to be appointed by the Central Government from amongst persons of ability, integrity and standing who have knowledge or experience in life insurance, general insurance, actuarial science, finance, economics, law, accountancy, administration or any other discipline.

The Chairperson and every other whole-time member shall hold office for a term of five years provided that no person shall hold office as a whole-time member after he has attained the age of sixty-two (65 years for Chairman) years. A part-time member also shall hold office for a term not exceeding five years from the date on which he enters upon his office.

The IRDA shall constitute a fund to be called “the Insurance Regulatory and Development Authority Fund” and there shall be credited thereto –

- (a) All Government grants, fees and charges received by the Authority;
- (b) All sums received by the Authority from such other source as may be decided upon by the Central Government;
- (c) The percentage of prescribed income received from the insurer.

The fund shall be applied for meeting –

- Salaries, allowances and other remuneration of the members, officers and other employees of the Authority;
- Other expenses of the Authority in connection with the discharge of its functions and for the purposes of this Act.

Establishment of Insurance Advisory Committee

The Insurance Advisory Committee shall consist of not more than twenty-five members from various fields like commerce, industry, transport, agriculture, consumer forum, surveyors, agents, intermediaries, organizations engaged in safety and loss prevention, research bodies and employees association in the insurance sector. The Chairperson and the members of the Authority shall be the ex-officio Chairperson and the ex-officio members of the Insurance Advisory Committee.

According to Section 64A of the Insurance Act, 1938, the Insurance Association of India was established, consisting of all the insurers carrying on business in India as members and as per provisions of Section 64C, the Act recommended the establishment of independent Life Insurance Council and General Insurance Councils.

Now, the Insurance Regulatory and Development Authority now brings into existence the following:

- (a) The Life Insurance Council
- (b) The General Insurance Council



Life insurance Council

Structure

- The Life Insurance Council will have an Executive Committee of 21 members of which 2 will be from the IRDA and the rest from licensed life insurers
- The Committee will set up standards of conduct and practices for efficient customer service, advise IRDA on controlling insurers' expenses and serve as a forum that helps maintain healthy market conduct
- It will create and manage a process for agent examination and certification
- The Life Insurance Council is funded by the Life Insurers in India.

Purpose

- The Life Insurance Council seeks to play a significant and complementary role in transforming India's life insurance industry into a vibrant, trustworthy and profitable service, helping the people of India on their journey to prosperity.

Its mission:

- To function as an active forum to aid, advise and assist insurers in maintaining high standards of conduct and service to policyholders
- Advise the supervisory authority in the matter of controlling expenses
- Interact with the Government and other bodies on policy matters
- Actively participate in spreading insurance awareness in India
- Take steps to develop education and research in insurance
- To bring the benefit of the best practices in the world to India.

The Council will

- Strive for a positive image of the industry through media, forums and opinion-makers and enhance consumer confidence in the industry
- Assist the industry in maintaining high standards of ethics and governance
- Promote awareness regarding the role and benefits of life insurance
- Organize structured, regular and proactive discussions with Government, lawmakers and Regulators on matters relevant to the contribution by the life insurance industry and act as an effective liaison between them
- Conduct research on operational, economic, legislative, regulatory and customer-oriented issues in life insurance, publish monographs on current developments in life insurance and contribute to the development of the sector

- Set up the Mortality and Morbidity Information Bureau (MMIB) and take an active role in its functioning
- Set up similar organizations for the benefit of the life insurance industry
- Act as a forum of interaction with organizations in other segments of the financial services sector
- Play a leading role in insurance education, research, training, discussion forums and conferences
- Provide help and guidance to members when necessary
- Be an active link between the Indian life insurance industry and the global markets.

Legislations & Control

- Address common issues in legislation and practice. Interface with the various other regulatory bodies on behalf of the insurance industry.
- Identify regularly the important issues to be taken up with Government and/or IRDA & PFRDA and make presentations on behalf of the industry
- Prepare benchmarks for the industry in all areas of operation and help maintain high standards of conduct, ethics and governance
- Take measures to prevent practices that are detrimental to the interests of the policyholders.

Training & Certification

- Take up the work relating to the training, examination and certification of Agents as provided in the Insurance Act
- Play a positive role in establishing standards, training of officials and intermediaries not only in products and sales but also other aspects relevant to the life insurance industry and lift the level of professionalism
- Conduct professional development programs in collaboration with international councils and life insurance institutes.

Education & Awareness

- Launch regular insurance awareness programs
- Facilitate the conducting of Continuous Development Programs for intermediaries
- Provide structured regular information to the public about the industry
- Launch an interactive website/Life Insurance Journals/newsletters



- Organise/participate in major conferences, seminars, workshops and lectures by Indian/visiting experts on insurance and related areas
- Facilitate knowledge-exchange programs (both in India and with Councils abroad) to develop and upgrade the skills of local insurance professionals
- Co-ordinate with educational institutions in India and overseas to encourage research, professional development courses etc.
- Elevate the profession of insurance selling and that of the Advisor, to that of financial analysts and planners through certification programs developed in conjunction with Indian and International institutions
- Establish a consumer relations cell.

General Insurance (GI) Council

The Vision for the industry and the GI Council

- A sustainable, profitable and growing non-life insurance industry in India
- An industry trusted and recognised as contributing to society and the economy
- An economic and public policy climate conducive to a flourishing industry
- A body (GI Council) recognised as providing active leadership and an authoritative collective voice for the non-life insurance industry in India.

The GI Council's mission

To provide leadership on issues having a bearing on the industry's collective strength and image and to shape and influence decisions made by the Government, regulator and other public authorities, within the country, in order to benefit the industry collectively.

This will be achieved on an active, collective and non-competitive basis by:

- pro-active analysis and lobbying to secure improvement in the legal and regulatory framework
- analysis and representations in response to initiatives from others which affect the industry
- being recognised as a leading contributor to public policy thinking on issues relevant to non-life insurance industry
- presenting a positive image of the industry to the public, the media and other opinion-formers
- providing leadership and guidance to the industry on issues which may affect its public image and reputation

- maintaining a core secretariat with staff of high calibre and relevant skills drawn from the industry on project to project basis, working under the guidance of the Board and its committees, focussed on delivering the mission.

GI Council will provide other services to member companies (such as an active role in management of commercial vehicle third party liability motor pool) which benefit the industry collectively; which support the mission; which can be provided without diversion of resources from the core functions; and which cannot be done more effectively by any other body.

OTHER IMPORTANT LEGISLATIONS GOVERNING GENERAL INSURANCE BUSINESS IN INDIA

THE MOTOR VEHICLES ACT, 1939

The Motor Vehicles Act was first passed in 1939 and Chapter VIII was brought into force from 1st July, 1946. The Act was subsequently amended in 1956 and 1988. Chapter VIII provides for compulsory insurance of motor vehicles. According to the provisions of the Act, no vehicle can be used in a public place unless there is in force in relation to that vehicle a policy of insurance issued by an authorised insurer. This policy covers the insured's liability in respect of death or bodily injury of third parties, fare-paying passengers, paid drivers, etc., and damage to property of third parties. The Act also prescribes the limits of liability.

The MV Act, 1939 was amended in 1956 to provide for the constitution of Motor Accidents Claims Tribunals (MACT) by the state governments to ensure speedy settlement of claims of persons involved in accidents. These tribunals follow simple and fast procedure and charge nominal fees.

Important Legal Provisions

● No Fault Liability

Section 140(1) of the MV Act, 1988 contains provisions regarding no-fault liability of the insured as follows:

“Where the death or permanent disablement of any person has resulted from an accident arising out of the use of a motor vehicle, the owner of the vehicle shall, or, as the case may be, the owners of the vehicle shall, jointly and severally, be liable to pay compensation in respect of such death or disablement in accordance with the provisions of this section”.

The essence of this provision is that, the negligence of the owner, or user of the motor vehicle is no longer relevant to decide the question of liability. On the other hand the claimants shall also not be required to plead and establish that the death or permanent disablement in respect of which the claim has been made was due to any wrongful



act, neglect or default of the owner, or owners, of the vehicle or vehicles concerned or any other person. This concept is known as **No-Fault Liability**.

The compensation payable following is as follows:

	Motor Vehicle Act, 1939	MV Act, 1988 (amended in 1994)
Death	Rs. 25,000	Rs. 50,000
Permanent Disablement	Rs. 12,000	Rs. 25,000

Note: Permanent disablement refers to injury or injuries involving permanent privation of sight of either eye, hearing of either ear, or privation of any member of joint, or disfiguration of the head or face.

● Hit and Run Accidents

Hit and run accident is “an accident arising out of the use of a motor vehicle or motor vehicles, the identity whereof cannot be ascertained in spite of reasonable efforts for the purpose.” Section 163 of the MV Act provides that the Central Government may establish a fund known as Solatium Fund to be utilised for paying compensation in respect of death or grievous hurt to persons resulting from Hit and run motor accidents.

The compensation payable following is as follows:

	Motor Vehicle Act, 1939	Amended Act, 1988 (1994 amendment)
Death	Rs. 8,500	Rs. 25,000
Grievous Hurt	Rs. 2,000	Rs. 12,500

Note: According to section 320 of IPC ‘Grievous Hurt’ includes emasculation, permanent privation of sight of either eye, hearing of either ear, or privation of any member of joint, or disfiguration of the head or face, fracture or dislocation of a bone or tooth, any hurt which endangers life or which causes severe bodily pain for twenty days, or unable to follow his ordinary pursuits.

● Solatium Scheme

The Solatium Scheme was initiated by the Central Government in 1989 for the payment of compensation to the victims of ‘Hit and Run’ accidents. This scheme came into force from 1st July, 1989.

The salient features of the scheme are as follows:

- The GIC nominates officers in each district for settlement of claims
- Application for compensation to be filed with the Claims Enquiry Officer (CEO) designated in each district within six months from the date of accident
- The CEO will hold enquiry and submit a report to the Claims Settlement Commissioner nominated for the district for sanction
- The sanction order with all supporting documents to be communicated to the concerned insurance company for making payment
- Payment to be made by Cheque/ Demand Draft to the claimant within 15 days from the date of receipt of the sanction order
- Monthly returns of claims paid and pending to be submitted to the Claims Settlement Commissioner
- Annual report of the scheme to be submitted by GIC to the Standing Committee and to the Central Government

The Standing Committee members are nominees of the GIC and four subsidiaries. It reviews the working of the scheme. The District Level Committee is concerned with the implementation of the scheme at the district level.

- Structured Formula for compensation

Section 163A, of the Motor Vehicle Act (amended on 14.11.1994) provides for fixed compensation to be paid to victims of fatal injuries to be made on the basis of “structured formula basis” based on their age and income.

The Inland Steam – Vessels (Amendment) Act, 1977

The Inland Steam – Vessels (Amendment) Act, 1917 as amended in 1977 provides for the application of the provisions of Chapter VIII of the Motor Vehicles Act, 1939 in relation to the insurance of mechanically propelled vessels against third party risks.

The act makes it mandatory for owners or operators of inland vessels to insure against legal liability for death or bodily injury of third parties or of passengers carried for hire or reward and for damage to property of third parties. The limits of liability are also prescribed.

Marine Insurance Act, 1963

This Marine Insurance Act, 1963 contains the law relating to marine insurance. This Act governs the practice of the marine insurance contracts. The provisions for subrogation proceedings for underwriters to pursue rights of recovery from carriers and bailees are also contained in this act.



The Carriage of Goods by Sea Act, 1925

This act defines the rights, liabilities and immunities of a ship-owner in respect loss or damage to cargo carried. It also deals with three aspects of the ship owner's liabilities towards cargo owners, viz.:

- a) where the ship-owner is deemed to be liable for loss or damage to cargo unless he proves otherwise
- b) where the ship owner is exempted from liability: loss resulting from perils of the seas
- c) limits of liability of a ship owner for loss of or damage to cargo calculated in monetary terms per package or unit of cargo.

The Merchant Shipping Act, 1958

This Act provides protection to shipowners. For example, the liability of the shipowner can be limited to certain maximum limits for some losses, which have occurred without the privity or fault of the ship owner. Generally these claims may relate to loss of life, personal injury or damage to property on land or water. At the same time, the Act imposes an obligation on the shipowner to send the ship to sea in a seaworthy and safe condition.

The Bill of Lading Act, 1856

The Bill of Lading is one of the important documents needed to substantiate a Marine claim. This Act defines the character of a Bill of Lading as a documentary evidence of the contract of carriage of goods between the shipper and shipowner. This Bill also is an acknowledgement of the receipt of goods on board the vessel and serves as a document of title.

The Indian Ports (Major Ports) Act, 1963

This Act defines the liability of the Port Trust Authorities for the loss of or damage to goods whilst in their custody and also prescribes the time limits for filing monetary claims, or suit against, the Port Trust Authorities.

Indian Railways Act, 1989

This Act deals with the various administrative aspects, and important provisions relating to marine insurance. These provisions define the rights and the liabilities of the railways as carriers of goods.

The Railways Claims Tribunal Act, 1987, defines the procedures for the settlement of claims relating to claims for cargo loss, personal injuries, refund of excess freight and other issues.

The Carriers Act, 1865

This Act contains provisions defining the rights and liabilities of the truck owners or operators who carry goods for the public on hire basis, for any loss of or damage to the goods carried by them. The provisions also prescribe the time frame for the notification of the loss of or damage of the goods to be filed with the road carriers.

The Indian Post Office Act, 1898

This Act defines the liability of the government for the loss, misdelivery, delay, of or damage to any postal article in the course of postal transit.

The Carriage by Air Act, 1972

This Act, gives effect to the provisions of the Warsaw Convention, 1929 and the Hague Protocol, 1955 relating to international carriage of goods and passengers by air. The Act also defines the liability of the air carrier for death of or injury to passengers and for the loss of or damage to registered cargo and luggage. The time limitation for filing of claims, and maximum limits of liability for injury, death, damage etc are also clearly defined in the various sections of the Act. Almost all the provisions, with little modifications, are equally applicable to domestic carriage.

Multi-modal Transportation Act, 1993 (Mmts)

This Act provides for the registration of the multi-modal transport operators who are engaged in transportation of goods under more than one mode of transport i.e. rail/ road and sea. The provisions define the limits of liability of the operator, for any loss, contents of the various documents, notification etc.

Public Liability Insurance Act, 1991

This Act was enacted for the purpose of providing relief to the persons affected by accident occurring while handling any hazardous substance and for matters connected therewith or incidental thereto. The underlying basis for relief under the act is the No-Fault basis.

The compensation payable by the owner of the establishment in the case of death or injury to any person other than a workman or damage to any property resulting from an accident is as follows:



Medical expenses (Reimbursement)	Maximum of Rs.12,500 per person
Death	Rs. 25,000
Fatal Accidents	Rs.25,000 per person + Medical expenses upto maximum of Rs.12,500
Permanent Partial Disability/ injury/ sickness	Reimbursement of medical expenses up to maximum of Rs.12,500 + cash benefit on the basis of medical certification
Temporary Partial Disability (Loss of wages) <ul style="list-style-type: none"> • unless hospitalized for 3 days • victim is above 16 years of age 	Fixed monthly relief not exceeding Rs. 1,000/- per month up to a maximum of 3 months
Permanent Total Disablement	Rs. 25,000
Actual damage to private property	Rs.6,000

The Indian Stamp Act, 1899

The Indian Stamp Act, 1899 requires that the policy of insurance be stamped in accordance with the schedule of rates prescribed therein.

Exchange Control Regulations

The Exchange Control Regulations governing the general insurance business in India are set out in a Memorandum which is issued by the RBI under section 73(3) of the FERA, 1973.

Important definitions

- **Resident:** A 'non-resident' is a person other than a person resident in India. Firms and companies resident outside India are treated as persons resident outside India.

Following are resident for the purpose of transactions in Indian rupees.

- Indians, Nepalese, Bhutanese resident in Nepal and Bhutan

- Offices of and branches of Indian, Nepalese and Bhutanese, firms, in Nepal and Bhutan
- **Foreign Currency:** any currency other than the currencies in India, Nepal and Bhutan

The FERA Act, 1973 (replaced by FEMA 1999) under section 73(3) exclusively has provisions for all the main classes of general insurance business as follows:

Schedule	Business covered	Provisions
PART – A	Marine	
PART – B	Non-Marine	
PART – C	Reinsurance	
PART – D	Foreign Currency Accounts and Investments Abroad	
PART – E	Submission of Statements to RBI	

- Under the Foreign Exchange Regulation Act (FERA) the Reserve Bank of India has issued in a Memorandum, exchange control regulations pertaining to the general insurance business in India.
- The regulations specify the rules as to the payments of claims in Indian currencies or foreign currencies and prescribe procedure where foreign currency is involved.
- The remittances of premiums and settlement of liabilities under the reinsurance arrangements of the GIC are also subject to these regulations.
- The regulations also apply to the business undertaken by the subsidiaries of the GIC abroad.

The Consumer Protection Act, 1986

This Act was enacted to provide for the protection of the interest of the consumers and to make provision for the establishment of the consumer councils and other authorities for the settlement of consumer disputes.

A **consumer dispute** means a dispute where the person against whom a complaint has been made denies and disputes the allegations contained in the complaint.

For the purpose of the Act, Consumer Disputes Redressal Agencies are established in each district and state and at the national level.



Authority	Jurisdiction	Reward
District Forum	Order Civil Court for execution of decree	Value of goods, services and compensation payable is less than Rs.5 lakhs
State Commission	Original, appellate and as well as supervisory jurisdiction	Value of goods, services and compensation payable is not less than Rs.5 lakhs < 20 lakhs
National Commission	Original, appellate and as well as supervisory jurisdiction – Final Authority	Value of goods, services and compensation payable exceeds Rs. 20 lakhs

Note: All the three agencies have powers of Civil Court.

Consumer Forum Orders

The Redressal Forums after detailed evaluation of the cases filed, can issue direction to the opposite party to do one of the following things namely:

- To remove the defect from the goods in question
- To replace the goods which shall be free from any defect
- To return to the complainant the price or charges paid by him/her
- To pay compensation for any loss or injury suffered by the consumer due to the negligence of the opposite party
- To remove the defects/ deficiencies in the services in question
- To disallow the continuation of any unfair trade practice or the restrictive trade practice
- Not to offer any hazardous goods for sale
- To withdraw hazardous goods from being offered for sale
- To provide for adequate costs to parties.

Insurance as a 'service'

The business of insurance is defined as 'service' under the provisions of this act. Most of the consumer disputes relating to insurance fall in the following categories:

- Delay in settlement of claims
- Non- settlement of claims
- Repudiation of claims

- Quantum of loss
- Policy terms and conditions.

Note: The Consumer Protection Act also takes into consideration cases pertaining to Products Liability insurances and Professional Indemnities. The cases may pertain to injuries, etc. caused by defective products or negligence of professionals like doctors, lawyers and accountants.

In a study conducted on 114 consumer cases adjudicated by the National Commission during the period 1991 to 1994, 65 cases were decided against insurers and 49 cases in their favour.

Can also mention about Insurance Ombudsman, though it is not through a legislation but only through a govt. notification. It is like an arbitrator facilitating redressal of customer grievances.

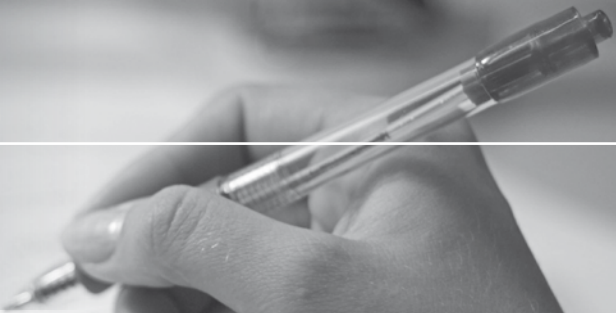
Questions



1. Discuss the dual role of IRDA in the present insurance market in India.
2. Discuss the important provisions of the Motor Vehicles Act with regards to the third party liability.
3. Explain the benefits available under the provisions of the ESI schemes.
4. What is the rationale behind the provisions of the Public liability Act of 1991.
5. How is an insurance consumer protected under the provisions of the Consumer protection Act, 1986.

CHAPTER – 4

UNDERWRITING



OUTLINE OF THE CHAPTER

- Introduction
- Objectives of underwriting
- Principles of underwriting
- Underwriting process
- Need for underwriting
- Underwriting authority
- Underwriting activities
- Underwriting policy
- Underwriting guides
- Rate making
- Underwriting results
- Underwriting in Special policies
- Questions

LEARNING OBJECTIVES

After reading this chapter you will be able to:

- To understand the principles and practice of underwriting
- To recognize the risks involved in underwriting
- To evaluate the underwriting factors involved in special policies

INTRODUCTION

Underwriting can be defined as “assumption of liability”. Underwriting involves the selection of policyholders after thoroughly evaluating all hazards, establishing prices and then determining the terms and conditions of the insurance policy.

The term ‘Underwriting’, refers to the formal acceptance of a risk by the insurance company for a price, which is termed as ‘Premium’. Of the many facets of insurance, underwriting has always been considered one of the most critical features. During

the 1950s, there were specialists who worked as underwriters and covered almost every type of insurance. The years since then have seen underwriting emerge as an art in itself.

The importance of underwriting can be well understood by the fact that even though several activities of an insurance company such as marketing, accounting, claims processing etc. are sometimes outsourced, underwriting is an area over which the company always retains complete control.

Once the risk involved is deemed acceptable, underwriting then fixes the rate of premium, and subsequently, all other terms involved. There are certain guiding objectives and principles that the underwriter must follow.

‘Underwriting’ in its real sense is being practised after the detariffing last year and the subsequent removal of control on pricing from 01.01.2008. Each risk shall be assessed on its own merit. Gone are the days when rates were quoted blindly based on the tariff or the internal guidelines of the insurer, without actually assessing and evaluating the risk proposed, for fixing of premium.

OBJECTIVES OF UNDERWRITING

The objectives of underwriting are three-fold:

- Producing a large volume of premium income that is sufficient to maintain and enlarge the insurance company’s operations and to achieve a better spread of the risk portfolio;
- Earning a reasonable amount of profit on insurance operations;
- Maintaining a profitable book of business (by ensuring underwriting profits) – that contains all the policies that the insurer has in force;
- More spread – across the profile and geography.

PRINCIPLES OF UNDERWRITING

Insurance is a concept of creation of a fund of premiums collected from various persons by pooling all of their risks, from which the financial losses of those few who suffer from the insured perils are compensated. The theory of probability, which can predict with a certain degree of precision, the possibility of a certain event occurring that can give rise to a claim provided there is sufficient data on past experience, is invariably the basis on which the concept of underwriting rests.

The principles that guide an underwriter before accepting a risk are:

- **Selecting insureds who fit the company’s underwriting standards:** only those insureds whose actual loss experience does not exceed the loss experience assumed in the company’s rating structure will be selected.



- **There should be proper balance within each rate classification:** the underwriter must be able to group insureds in such a way that the average rate in the group is enough to pay for all claims and expenses. Units with similar loss-producing features are placed in the same class and charged the same rate.
- **Charging equitable rates:** the rates that apply to one group should not be charged to another group as well. For example, in the case of Health insurance, charging the same premium rate for people in the age group of 20-25 years and those in the age group of 50-55 years will result in the younger lot subsidizing the older people.
- Each portfolio (fire, marine, health, etc.) to be self sustaining without assuming any cross-subsidy.

THE UNDERWRITING PROCESS

The underwriting process follows a series of stages, at the end of which the status of a risk is decided. It is only after the risk has been weighed and all possible alternatives evaluated that the final underwriting is done. When a proposal for insurance is received, the underwriter has four possible courses of action:

- Accept the risk at standard rates
- Charge extra premium depending on the risk factor
- Impose special conditions
- Reject the risk.

The underwriter follows specific steps when evaluating a potential risk. These are as follows:

Assimilating information about the applicant

The underwriter obtains this information from a wide variety of sources. The most important sources are:

- **The application or the proposal form:** It contains specific information about the applicant. For example, in Motor insurance, information regarding the age of the vehicle, weight, purpose/usage, past claims history etc will be given.
- **The agent's report:** the agent does an evaluation of the prospective insured. The agent must have first hand knowledge about the applicant's operations and reputation. It is the agent's responsibility to screen the applicant initially according to the company's specified requirements.
- **Government records:** these records include information from civil and criminal courts, property tax records, bankruptcy filings etc. These may be referred to if required.

- **Pre-insurance inspection report:** for property insurance, this consists of a physical assessment of the building or plant to be insured.
- **Claim files:** these are helpful when renewing an existing policy. The underwriter can gain an insight into the policyholder's character by reviewing the claim files or through investigation.
- **Reinsurers** – in the case of large risks

Evaluating and making a decision

The underwriter can accept a proposal, reject it or accept it with certain modifications. Some of the modifications that can be made are:

- **Hazard can be reduced:** For loss prevention and minimisation, underwriters can recommend certain changes that will safeguard against physical hazards. For example, installing sprinkler systems and better fire-fighting equipment in offices will reduce damages in case of fire. This advice can either be followed by the applicant or rejected.
- **Changing rating plans and policy terms:** Sometimes a proposal that seems unacceptable at one rate may become a desirable business under another rating plan or with Special Conditions such as 'compulsory excess'. A rate that will fetch the insurance company a decent profit as well as be acceptable to the applicant is fixed on the basis of how the underwriter judges that particular case.
- **Facultative reinsurance can be used:** When the business is not covered by the insurer's reinsurance treaty or the amount of insurance needed exceeds the net treaty capacity, the underwriter can transfer that excess to a facultative reinsurer. As an alternative to this, the insurance can also be divided among several insurers.

Executing the decision

After perusing all the alternatives and making a decision, it now remains for the decision to be put into action. There are three courses of action to be taken.

- The applicant should be briefed about the decision along with all the modifications made. If any application has been rejected, the underwriter must convey this decision to the agent in such a way that it does not further damage any business relations they may have.
- The underwriter is also in charge of preparing the documents, which include a binder or a policy work sheet to be sent to the policy writing department and also issue of certificates of insurance.
- The final step is concerned with recording information about the applicant and the policy for accounting, statistical and monitoring purposes. Information like the



location, coverages, limits, risk features etc must be coded, as these are essential for the purpose of rate making, financial accounting and business evaluations.

Monitoring the activities

The underwriter must always be alert to any change in the loss exposures of the insureds. This type of monitoring usually takes place when policy changes and losses are brought to the underwriter's attention. Premium audit and loss control reports also help to review individual policies.

When a claim is made or after a premium audit has been carried out, the underwriter can contact the reinsurance personnel and secure first-hand knowledge of the insured. This will help in uncovering any additional hazards, that will in turn help the underwriter to re-evaluate the account and decide on its continued acceptability.

The underwriter must also monitor the entire book of business and use premium and loss statistics to determine what causes the problems that make a business deteriorate. This will also help in finding out whether the underwriting policy is being complied with.

Maintaining the records of business

This involves evaluating the profitability of all the business written during a particular period of time, covering a specific territory and for a certain type of insurance. This evaluation should be able to weed out any problems in that line of business. The insurer's primary concerns are the development of adequate premium volumes, the coverage of fixed costs, the loss ratio that develops and overhead expenses. For the purpose of evaluation, the business can be subdivided on the basis of its class, size of the account, the territory and producer.

The producer or agent's records concerning premium volume, policy retention loss ratio etc must be evaluated. The goals that had been initially decided by the insurer and the agent and the progression made towards these goals must be considered while evaluating.

NEED FOR UNDERWRITING

The need for underwriting arises because of some basic reasons: To avoid the concept of adverse selection and certain other hazards, to maintain fair prices and subsidisation and stay ahead of competition.

To check Adverse selection

This term is used for a situation where the insurance applicant presents a possibility of loss that is higher than the average expected from a random sample of all applicants. It arises when the information presented to the insurer and the actual material facts relating to the risk are different.

For example, flood insurance is more likely to be purchased by those businesses that expect flooding rather than by all other businesses. Or people already suffering from a disease or belonging to the high mortality rate group will be eager to claim coverage while those enjoying good health may not go in for insurance.

Along with adverse selection there are certain types of hazards that an underwriter must watch out for. These are –

- Physical hazards
- Moral hazards, and
- Morale hazards.

Physical hazards

These are hazards that affect the physical characteristics of whatever is being insured. For example a building made of wood represents a higher level of physical hazard than one made of brick. An untrained driver, faulty fire- safety equipment are both examples of a physical hazard.

Moral hazards

These hazards refer to the defects that exist in a person's character that may increase the frequency or the severity of loss. Such a character may tend to increase the loss for the company.

Morale hazards

The fundamental postulate of insurance is that the insured should always conduct himself as if he is uninsured. However, if there is a situation of a wilful carelessness on the part of the policyholder because of the existence of insurance, then it is a case of Morale hazard.

To ensure fair pricing and subsidising

Underwriting helps in determining the expected loss potential of the proposed insured and selecting a price in line with this expected loss. Insureds with an approximately equal loss potential are put into one group and charged the same rate.

Competition

An underwriter can also help an insurance company stay one step ahead of its competitors. Some of the ways this is done is through lower premium rates, innovative marketing strategies etc. The underwriter provides all necessary information and thus helps the insurer make the best possible decisions.



Other risks

There is also another category- the 'Declined Risks'. These are extra hazardous risks that should be rejected. Sometimes, a premium is fixed after imposing restrictive conditions, clauses and warranties. The acceptance of such risks is called 'Accommodation'. Some examples of such risks are Ammunition works, Camphor boiling works.

UNDERWRITING AUTHORITY

Underwriting authority refers to the degree of autonomy granted to individual underwriters or groups of underwriters. This authority will differ by position and experience. Different insurance organisations have varying degrees of decentralisation. In India, the underwriting authority vests with the insurance company. Post opening up of the insurance sector, some private insurers are decentralizing certain classes of business like travel insurance, where an insurance intermediary is allowed to issue (better to put it as 'generate') the policy.

Specially lines like aviation and livestock mortality have retained centralised underwriting authority, while some other insurers are delegating a considerable part of their authority to selected brokers. Insurers who follow the decentralization system state that it eliminates duplication and makes the most of the producers' familiarity with local conditions. In return, brokers receive a higher commission rate and a larger share in the profits.

The degree of decentralization permissible depends upon several factors like the line of business involved, the experience and the track record of the producers. There may be insurers who allow their brokers to issue personal lines policies and bill the policyholders. This is certainly a significant amount of underwriting authority. Some other insurers may permit a high degree of authority but restrict policy issuance only to the company, so that control over the brokers' activities is maintained.

There are also lines of business where the producer may have no underwriting authority at all. These usually include very hazardous or specialised classes of business.

UNDERWRITING ACTIVITIES

Underwriting activities can be divided into two types –

- **Line underwriting** – Where daily underwriting tasks are carried out; the underwriters are usually located in regional offices of the insurer.
- **Staff underwriting** – Where the underwriter helps the management in formulating and implementing underwriting policy. They are usually located at the Head Office.

Line underwriting activities:

The line underwriters take care of the following activities: -

- Choosing insureds with care. This is an ongoing process – once an account is accepted, it must be monitored to check on its continued acceptability. Corrective action may be required in certain cases. Here, the underwriter must watch out for adverse selection.
- Categorizing the risks involved. Insureds having similar expected loss frequency and loss severity are pooled together. Only then will the insurer be able to develop a sufficient rate to pay the losses incurred and to generate profit.
- A rate should be so set that it not only allows the insurer to make a profit but also is competitive when compared to the rates of other insurers. The underwriter must make this after thorough appraisal of the application.
- The underwriter allows the agent to issue certain types of policies and endorsements by making use of an independent agency marketing system. The underwriter also prepares quotations, files for the policy typist and assists the agent with drawing up proposals.

Staff underwriting activities

The staff underwriters take care of the following activities: -

- On the basis of research done and knowledge about the market, they put together the company's underwriting policy. They must determine the company's capacity for business. Capacity refers to the volume of premium that an insurer can safely write, based on the policyholder's retained earnings or surplus.
- They update the rates and rating plans of the company. This is done to address the effects caused by changing competition, inflation and loss experience. Examining the operational costs and the profit requirements and combining them with the loss costs decides the final rate.
- Preparing and updating the underwriting guides and bulletins that contain the company's underwriting policy. The guides also differentiate between acceptable and unacceptable business.
- Underwriting audits are conducted to monitor the line underwriting activities. The audit is a control tool used by the management to make sure that the underwriting policy is being properly implemented. This is done through statistical analysis of underwriting results and also through field audits.
- Staff underwriters also offer advice to other underwriters – by virtue of their own experience in handling complex accounts.



- Staff underwriters also conduct training programs and other educational activities for the benefit of line underwriters. They also act as instructors when there is a need for information on a technical insurance area.

THE UNDERWRITING POLICY

Underwriting Policy is like the Constitution of a country. It provides the frame work within which the company would develop products for the market. The basic purpose of an underwriting policy is to transform the objectives of the management into rules and guidelines that will direct the company's underwriting decisions. The underwriting policy decides the composition of the book of business.

An underwriting policy must take into consideration the following dimensions – the lines of business, the territories involved and the rating plans, reinsurance and retention patterns, levels of centralization/decentralisation. Any change in the underwriting policy must be evaluated on the basis of other dimensions. Changes must also recognise the effects of certain limiting factors that influence the underwriting policy. These include:

- The capacity – the relation between the premiums written and the size of the policyholders' surplus is called the capacity.
- Capital & Reserves – It helps to gauge an insurer's solvency.
- Skilled human resources – insurers require skilled personnel to efficiently market the product, employ loss control efforts and adjust any loss that occurs. The insurer must ensure that there are enough personnel and that they are conversant with the company's policies.
- Insurers must also follow the rules and regulations laid down by the insurance regulator in whose territory they operate. The impact of regulation varies from country to country. They must obtain licenses for writing insurance by individual line within each state, and all rates, rules and other documents must be filed with Government regulators.
- Portfolios in which the company operates, e.g., exclusive health insurer/ECGC/ other than health, etc.
- Reinsurance sets limitations on what the underwriter can write. Reinsurance refers to the contractual relationship by virtue of which, risks are shared with another insurer.

Application of the underwriting policy

Once the underwriting policy is set, it must be communicated to all concerned, as well as applied. Presently, IRDA requires that it should be placed before the Board of Directors of the Insurer and submitted to the Regulator with the board resolution. There should also be a 'Compliance Officer' for the underwriting policy. Underwriting bulletins

and guides are utilised for this purpose. Once the policy is established, underwriting audits are conducted to review the effectiveness of the policy.

Applying the provisions given in the underwriting policy involves communicating whatever decision has been taken, to the agent. Data about the policyholder including the class, location, risks involved and coverages must be coded, so that the information can be used later.

UNDERWRITING GUIDES

Underwriting guides outline the ways to realise the objectives stated in the policy. (basically 'do's and 'dont's) They contain the standards for acceptability and summarise the underwriting authority requirements. The chief purposes of an underwriting guide are as follows:

- Supplying a basic framework for formulating underwriting decisions: underwriting guides identify the principal factors that should be weighed when a particular type of insurance is written.
- The underwriting guide is a means of making sure that the selection process is uniform and consistent. Submissions that are identical in all respects must be treated in the same way. The guides are also a means of informing individual underwriters of a suitable approach to evaluate policyholders.
- Underwriting guides help to unite the insights of experienced underwriters, which will help those less familiar with a particular line of business. The guides contain significant observations that have been gathered on the basis of the insurer's past experiences.
- The guides enable routine decisions to be handled at lower levels of authority and allow the experienced underwriters to concentrate on the more difficult cases.

RATE MAKING

Rate making, also known as insurance pricing, has an important part to play in the overall profitability of the company. Rate making involves the selection of classes of exposure units on which statistics can be collected regarding the possibility of loss. The underwriter must think about all aspects before deciding on the pricing of a policy. The rates charged must have the following basic characteristics –

- The rate must be high enough to pay for any expenses or losses incurred
- The rate must not be too high
- The rates must not be inequitable i.e. if two exposures are similar as far as losses are concerned, they should not be charged significantly different rates
- The system of rating must be simple and understandable so that premiums can be quoted promptly



- The rates must not keep fluctuating i.e. they must be stable. Otherwise irate consumers may look to the government to regulate the rates
- The rating system must provide the insured with a strong incentive to adopt loss control
- The rates must change with the changing economic conditions- rates must increase when loss exposure increases.

Rate making methods

There are three fundamental rate making methods in property and liability insurance. They are as follows:

- Judgment rating method

This method is used when the loss exposures are so diverse that it is not possible to calculate a class rate. Therefore, each exposure is individually evaluated and the rate determined by the underwriter's judgment. This method is frequently used in ocean marine insurance because the vessels, ports, waters and cargoes carried are very diverse.

- Class rating method

Under this method, exposures with similar characteristics are grouped together and charged the same rate. This is based on the assumption that any future loss to the insured will be decided by the same set of factors. Some of the major factors in life insurance are age, health, gender etc. This method is also called manual rating because the rates are published in a rating manual. There are two ways of determining the class rates:

- **The pure premium method:** (burning cost) pure premium is that part of the gross rate, which is utilised to pay losses and adjustment expenses. It is calculated by dividing the amount of incurred losses and loss-adjustment expenses by the number of exposure units. Incurred losses include all the losses -whether paid or not -that occur at the end of the accounting period.

$$\text{Pure premium} = \frac{\text{Incurred losses and loss-adjustment expenses}}{\text{Number of exposure units}}$$

The final step in this method is to add a loading for expenses, underwriting profit and a margin for contingencies. The expense loading, also known as the expense ratio is that proportion of the gross rate available for expenses and profit. The final gross rate is arrived at by dividing the pure premium by 1 minus the expense ratio.

$$\text{Gross rate} = \frac{\text{Pure premium}}{1 - \text{Expense ratio}}$$

- **The loss ratio method:** under this method, the actual loss ratio –which is the ratio of incurred losses and loss-adjustment expenses to the earned premiums - is compared to the loss ratio that was expected and the rate is adjusted accordingly. The loss ratio that is expected is the percentage of the premiums that are expected to be used to pay losses.

$$\text{Rate change} = \text{Actual loss ratio} - \text{Expected loss ratio}$$

Merit Rating method:

Merit rating is a rating plan by which class rates (manual rates) are adjusted upward or downward based on individual loss experience. It is based on the assumption that loss experience will differ significantly from individual to individual. The types of merit rating plans are:

- **Schedule rating:** under this plan, each exposure is individually rated. A basis rate is fixed for each exposure and this is then modified by debits or credits for undesirable or desirable physical features. The physical characteristics of the exposure to be insured are very important in this plan. Schedule rating is used in commercial property insurance such as for industrial plants. These buildings are evaluated on the following criteria:
 - Physical features of the building – its height, the materials used to build it, the area surrounding it, etc.
 - It's use i.e. what is the building being utilised for. For example, presence of inflammable materials will increase the risk of a fire.
 - The protective devices set up in the building. Rate credits are given for the presence of a fire alarm, sprinkler system etc.
 - The building's exposure – this refers to the likelihood of the building being damaged from a fire in the adjacent buildings. The greater the exposure, the higher will be the charges applied.
 - The maintenance of the building – debits are applied for poor maintenance and housekeeping.
- **Experience rating:** under this rating plan, the class or manual rate is adjusted upward or downward based on past loss experience. The insured's past loss experience is the basis for fixing the premium for the next policy period. If this loss experience is better than the average for the class as a whole, the class rate is reduced and vice versa. This system is usually used only for larger firms with a high volume of premiums.



- **Retrospective rating:** in retrospective rating, the insured's loss experience during the current policy period determines the actual premium paid for that period. There is a minimum and a maximum premium. When losses are small, a minimum premium is paid and when losses are large a maximum premium is paid. Large firms use this system in general liability insurance, burglary and glass insurance, workers' compensation insurance and auto liability and physical damage insurance.

UNDERWRITING RESULTS

Underwriting results are an indication of the effectiveness of the company's underwriting policy. Statistically, it is represented by the insurer's combined loss and expense ratio. Evaluation of results by the line, territory etc will help identify all the problem areas. Besides these, over the years, the entire insurance industry is cyclical in nature, thus providing industry average performances against which any insurer can be measured.

The causal mechanism for this cyclic nature of the industry is yet to be determined. Certain factors like inflation, regulation and competition have had a considerable impact. For example slow regulatory response to requests for rate increase in times of inflation could have been responsible for unsatisfactory underwriting results.

The evaluation of underwriting results based upon the combined loss and expense ratio is complicated because of several factors, two of which are outlined below:

The Volume of Premium

The volume of premium and the underwriting policy have a direct relationship i.e. when the existing underwriting rules are unduly tightened, it will usually result in a drop in premium volume. In the same way, the relaxing of underwriting standards usually results in an increase in underwriting premium. The interpretation of the insurer's combined loss and expense ratio, both on an aggregate as well as a line basis, must be tempered by considering the extent to which the insurer's premium volume goals have or have not been met.

For example, an insurer takes on a much stricter underwriting view than in the past, resulting in a drop from 100 percent to 94 percent in the combined loss and expense ratio, based on incurred losses and expenses to earned premium. If the written premium drops by 24 percent during the same year, then an evaluation of the results using an expense ratio that compares expenses to written premiums will reflect a deterioration of results, with an increase in the combined ratio.

Loss Development Delay

In some business lines, a significant time gap exists between a loss that has taken place and the final settlement of a claim. Though there are reserves that are established as soon as the loss is reported, a considerable amount of imprecision exists in the estimate of the final loss costs. This is known as loss development delay. This has two major characteristics:

- Changes in the reserves in the case of reported losses
- Changes in the reserves for incurred-but-not-reported (IBNR) losses.

In those lines of business, which are written on an occurrence basis and where there is an extensive period of discovery between the time of loss and the consequent suit by the claimant, the exactness of the current reported losses is greatly affected by the IBNR. Many professional liability insurers have addressed this problem by changing to “claims-made” forms and by introducing the claims-made commercial general liability policy.

If a policy has been written on an occurrence basis, the underwriter provides coverage for only those injuries that occur during the period of the policy, even when such claims have not been brought against the insured for many years after the coverage has expired. If the policy has been written on a claims-made basis, the underwriter gives coverage only for those claims made against the insured during the policy period. Therefore, on paper, a claims-made policy does not cover losses that are unreported at the end of the policy period. But, in practice, claims-made policies very often cover losses reported after the policy period by virtue of “extended reporting periods.”

Yet another way to appraise the functioning of the underwriting department is by setting standards of performance with respect to several important areas of underwriting. Standards of performance comprise the following factors:

Standards of selection

There should be well-outlined selection rules in the underwriting guide. These rules should help to decide what is the desirable, average and below average – type of insured. Each branch of the insurance company must have an idea about the correct balance of all these types of account.

A desirable product mix

The underwriting guide should contain the desired product mix for new and renewal businesses. Based on past performances, the product mix is decided. For example, if liability losses are high, the product mix standard may require a reduction in manufacturing classes, but an increase in writing in the service, mercantile and contractor classes.



Standards of accommodating risks

All accommodated risks should be entered together along with the complete particulars concerning the reason for accommodation. During underwriting audits, the evaluation of these entries can determine whether they are being over used and also make sure that the increased volume promised by the producer is duly followed up.

Standards of pricing

The pricing standard consists of a procedure where all accounts that have deviated from the manual premium by more than a selected percent are identified and recorded. Goals are set for each branch so that the entire book will not deviate from the natural premium by more than a set acceptable range.

Retention and success ratio standards

The retention ratio is the percentage of business renewal. The success ratio is the ratio of business written to business quoted. An unfavourable percentage of renewals indicate serious deficits like unfavourable claims services, uncompetitive pricing etc. The renewal rate should be monitored carefully and evaluation of any trends recognised.

The success ratio standard is usually employed in commercial lines. Ratios that are too high or too low require thorough investigation. Under the success ratio, a high ratio is indicative of an inadequacy in rates; rates that are lower than other insurers; a broader coverage when compared to other insurers or deterioration in selection criteria. A low success ratio is indicative of very restrictive coverages; poor service; high rates and very high selection criteria.

Services to producers standards

Insurers must constantly evaluate their services. There should be a set of minimum acceptable standards for certain services to producers. The performance of each branch and region towards services to the producer is compared to the mandated level of performance.

UNDERWRITING CONSIDERATIONS IN SPECIAL POLICIES

Engineering Insurance

Engineering insurance requires highly specialised and technical expertise in underwriting, risk inspection, rating etc. A pre-acceptance risk inspection is conducted for most of the proposals and an inspection report is prepared that deals with the inspection of motors, generators, transformers, steam turbines, oil and gas engines, compressors, pumps, refrigerating plant, external and internal examination of boiler and pressure vessels and the loss of profits survey report.

Most classes of engineering insurance are controlled by tariffs and insurance companies can fix the prescribed rates. In some cases though, the proposals are referred to the Tariff.

When it comes to the question of engineering claims, the underwriter has to bear in mind the following points:

- Early notification of a claim should be followed by an early visit by a surveyor.
- If liability exists under the policy, the company can give advice concerning the extent and type of damage and the necessary repair work.
- During repair, there are significant maintenance costs that occur and here the company can fix a suitable proportion of costs.
- For whatever liability is incurred, the company has the right to approve the type of repair from a safety aspect as well as with an eye on the future risk aspect.

There are also instances where acceptance of risk is subject to special considerations, which are accepted by insurance companies. Some of these are listed below:

- **Fire** – consequential loss (fire) policy may be granted only to those clients whose books of accounts have been regularly audited by a reputed firm of auditors, or whose previous loss experience has been inspected and accepted.
- **Motor** – older vehicles are accepted, subject to inspection. Comprehensive insurance on imported cars is allowed subject to the inclusion of an excess clause. Vehicles like those belonging to the military will be covered only for third party risks.
- **Marine and Cargo** – ocean marine insurance is divided into three categories:
 - **Yachts** – all sailboats and inboard powered boats including luxury vessels fall under this category. The underwriting conditions can be grouped under three categories:
 - **Seaworthiness:** this refers to the age, construction and maintenance of the vessel. The older a vessel, the lower its value. The best way to obtain information about a vessel is through a marine survey.
 - **Navigable waters and season:** underwriters restrict coverage to only the area for which the yacht, equipment and the operator's experience are appropriate. This is done with the help of a navigation warranty, which limits coverage when the vessel is under conditions that have not been agreed to by the underwriter.
 - **Operator experience:** insurers also consider the policyholder's experience and training. For example, there are insurers who give credit for completion of Power Squadron or Coast Guard Auxiliary courses. Membership in a



relevant organisation, such as a yacht club, is taken as an indicator of the policyholder's interest in his or her chosen field.

Commercial hulls – as far as commercial hulls are concerned, the emphasis is again on the physical characteristics such as construction of the ship, equipment and its maintenance, the area of operation etc. The safety regulations under which the ship should be operated will be determined by the nation in which the ship is registered. The quality of maintenance is verified by regular inspections.

In marine insurance, the acceptance of certain risks requires careful consideration. These include:

- Asbestos/cement pipes and sheets (breakage is excluded)
- Transformers (breakage is excluded and excess imposed on all leakages)
- Refrigerators and air conditioners (risks of denting and scratching are excluded)
- Cargo in paper bags (tearing and bursting of bags is excluded)
- Glass (breakage, scratching and chipping are excluded)
- Sanitary ware (breakage, chipping and denting are excluded)
- Machinery (second hand) breakage is excluded
- Oil in second hand drums (leakage and contamination are excluded)
- Motor spare parts and ball bearing (theft, pilferage and non-delivery are excluded)
- Motor vehicles (denting and scratching excluded)
- Watches (TPND, breakage is excluded)

Cargo Insurance

In cargo insurance, the quality of the policyholder and the business reputation are of the utmost importance. The ports between which the goods will be shipped and the land transportation to be used from warehouse-to-warehouse are also important underwriting concerns.

In cargo insurance, there are again certain specifications that are followed.

- Normal rates for cargo carried on standard vessels (i.e. conforming to standards prescribed by Tariff).
- Extra rates if vessel is over-aged.
- Close scrutiny of tramp vessels – that includes the financial position of the owners, the age of the vessel and its tonnage. If the vessel does not fulfill the criteria, 1 percent extra premium is charged on the sum under marine cargo policies.

- The above were the special instances where the underwriter makes exceptions for accepting risks in special cases. This is because the basic principle of underwriting has always been that the underwriting must neither be too firm nor too relaxed. Wherever a risk can be accommodated after suitable adjustment, it must be done.

Conclusion

Underwriting is of paramount importance to the insurance business. In fact, a sound underwriting policy sets the agenda for profitable business by providing against loss and ensuring returns.

Questions



1. What are the objectives of underwriting?
2. What are the activities of a line underwriter?
3. What is adverse selection?
4. Give a few examples of occupational hazards.
5. What is numerical rating?
6. What purposes do Endorsements and Deductibles serve?
7. What can be considered a 'desirable product mix' from the point of view of the insurer?
8. "The volume of premium and the underwriting policy have a direct relationship" Explain.

CHAPTER – 5

INSURANCE FORMS

OUTLINE OF THE CHAPTER

- Introduction
- Proposal forms
- Cover notes
- Certificate of insurance
- Policy forms
- Endorsements
- Interpretation of policies
- Co-insurance
- Renewal notice
- General Insurance policy provisions and conditions
- Questions

LEARNING OBJECTIVES

- To know the procedural rules for application of insurance
- To understand the implications of disclosures in proposal forms
- To study the importance of other documents attached with the policy
- To explain various provisions and conditions contained in the policy

INTRODUCTION

Insurance is a legally enforceable contract to indemnify the insured for the covered losses as given in the policy. The insurance policy document is the evidence of the contract of insurance. However, before an insurance company issues a policy document, the insurers require compliance of formal procedures to be followed by applicants who need insurance for their property and liability loss exposures.

PROPOSAL FORMS

One of the prerequisites of an insurance contract is the mutual agreement between the insurer and the insured. There must be a valid offer and an unqualified acceptance between the two parties. The proposal for insurance is also called as application for insurance.

An offer or a proposal for insurance is a request for cover, and may be made either verbally

(IRDA (Protection of Policyholders' Interests) Regulations, 2002

4. Proposal for insurance

- (1) Except in cases of a marine insurance cover, where current market practices do not insist on a written proposal form, in all cases, a proposal for grant of a cover, either for life business or for general business, must be evidenced by a written document. It is the duty of an insurer to furnish to the insured free of charge, within 30 days of the acceptance of a proposal, a copy of the proposal form.
 - (4) Where a proposal form is not used, the insurer shall record the information obtained orally or in writing, and confirm it within a period of 15 days thereof with the proposer and incorporate the information in its cover note or policy. The onus of proof shall rest with the insurer in respect of any information not so recorded, where the insurer claims that the proposer suppressed any material information or provided misleading or false information on any matter material to the grant of a cover.
-

or in writing or by the completion of a printed proposal form supplied by the insurer. So proposal has to be in writing or confirmed in writing and can not be oral alone.

These proposals are called as applications for insurance in USA, and the Britishers call it Proposal Forms. One who seeks cover is the proposer. The proposer must have a property, which may be at risk or he or she may have dependents who will suffer financial loss at his or her death.

General Insurance deals with property and liability risks (also humans – Personal Accident & Health Insurance). From some event the organizer of the event or the owner of a property or a contractor at a situation may incur a legal liability to others from injury to them. These others are called third parties because the two parties to the contract of insurance are the *insured* and *insurer*.

The seeker of cover or protection must furnish accurate and truthful answers to the many questions contained in the Proposal Form. The proposal form will be similar for most property risks, but may differ depending on certain special adverse features of the risk.



Material facts disclosed in a proposal form

Some common questions, which occur in all proposal forms, and also particular questions, which relate to specific risks. A typical property insurance proposal form will, inter alia, include the following common information, which is sought:

- (1) Name, address, telephone number, and other personal identification details
- (2) The situation of the property
- (3) Proposer's profession
- (4) Previous and present insurance
- (5) Loss experience
- (6) Sum insured
- (7) The contents on the premises in the location.
- (8) The type of property mentioning whether hazardous, non-hazardous and extra-hazardous.
- (9) The type of fire protection available.
- (10) The proportion of ownership of others in the property at risk, in other words, specifying the interest of mortgagee like banks or lessees.
- (11) The nature of adjoining risks, say, what are the people who are the applicant's immediate neighbours doing.
- (12) The value at risk or the sum proposed for insurance or as is generally known as sum insured.

The proposal form generally ends with a declaration to be signed by the proposer. In this the proposer must declare that whatever information he has provided is true to the best of his/her knowledge. Such a declaration becomes the basis of the insurance contract. Every proposal form must also be dated.

Proposal for Non-Marine Insurance

Generally in non-marine insurance, the applicant is required to fill a proposal form containing important questions for the purpose of risk assessment. The applicant declares at the end of the form and warrants that all information stated in the proposal form are true to the best of his knowledge. The proposer agrees that the answers to the questions in the form would be the basis of the insurance contract. The material facts disclosed in the form are assumed to remain constant, till the day the contract comes into existence. Any change before this date must be brought to the notice of the insurer to get the offer re-approved.

When the insurance contract comes into being on the basis of the statements recorded in the proposal form the insurer can avoid liability, if any of the above statements are found

untrue. (underwriter should ensure that none of the questions are left blank or just put '---'. Otherwise, in case of dispute, it will be construed in favour of the insured in case of a disputed claim)

Proposal for Marine Insurance

There is no requirement for proposal form in case of marine insurance. In U.K, the broker, under the instruction of the proposer, fills up a slip mentioning all the bare essentials needed for assessing the risk proposed. The clauses identifying the liabilities of the underwriter are also included in the slip.

In India the proposer himself has to approach the insurers. The General Insurance industry is capable of underwriting the entire risk, however big it may be, and reinsure any part of it. It had to be approached through agents licensed by the Controller of Insurance, the Govt. of India. Now of course the authority to issue licence lies with the IRDA. The IRDA also allowed private insurers to obtain licences for their agents. Brokers are introduced in Indian market.

COVER NOTES

A cover note is an evidence of insurance. It is as good as an insurance policy. A cover note is a temporary and limited agreement, sent prior to the completion of the proposal (preparation of the final policy document, pending some information to be filled in), or when the proposal is under consideration or the policy is being prepared for delivery. It usually serves as an interim cover, with the same terms and conditions that are generally issued for such proposals. It automatically expires at the end of the declared period. It also expires if the regular policy is issued or declined by the insurer.

Any claim arising during the period for which the cover note remains valid will be determined by the terms of the note and not by the terms of the policy subsequent to it. Where the insurer sends a temporary cover, inviting the renewal of the insurance on its expiry, it becomes enforceable if accepted by the insurer. Or else it remains as an offer waiting for an acceptance.

Some insurers charge a nominal fee for the issue of cover notes. In fact there will be a statement in the cover note that this is issued subject to the terms and conditions of insurance policy to be issued. This cover rate is different from the premium, which is the consideration for the Contract of Insurance.

Some of the circumstances when cover notes are issued are when negotiations for insurance are in progress and it is necessary to provide cover on a provisional basis or when the premises are being inspected for determining the actual rate applicable. The cover note is not stamped but represents the same insurance as that provided by the policy. The cover note is subject to the usual terms and conditions of the insurers policy for the class of insurance insured. It is also subject to any special clauses if applicable, e.g. Agreed Bank Clause, Declaration Clause etc.



THE SLIP

The “Slip” is a document mentioning all the essential information needed for assessing the risk proposed. The clauses identifying the liabilities of the underwriter are also included in the slip. The insurance broker acting as the agent of the insured prepares the slip. The broker takes it to a leading underwriter and tries to get the best deal for this client. The underwriter agrees to the amount he is willing to cover and signifies his ascent on the slip by initialling it.

Unlike the cover note the slip serves as the acceptance to the proposal by the underwriter, and is binding on the underwriter for the issuance of a policy according to its terms. The slip should be correctly stamped under the Stamp Act. Under Sec. 23 of the Marine Insurance Act, 1963, the ‘slip’, ‘covering note’ or any other ‘customary memorandum of the contract’ can only be used for the purpose of reference, and showing when the offer was accepted. However, no action can be brought about on the basis of these documents. ‘The policy may be executed and issued either at the time when the contract is concluded or afterwards’, (Section 24). Section 88 of The Marine Insurance Act 1963 states that, ‘where there is a duly stamped policy, reference may be made, as heretofore to the slip or covering note, in any legal proceeding’. The corresponding British Act was passed in 1906. This practice is not followed in India. This is a British market practice.

CERTIFICATE OF INSURANCE

Many statutory authorities have need to verify the existence of an insurance policy in order to fulfill their duties such as issue of motor driving license, issuing a letter of credit to an international trader, or sanctioning a loan on hypothecation of goods. It is understood that there may be some delay in the issue of insurance policies. This it is hoped may not be the case in future with the advent of information technology and increasing computerization in trading and manufacturing enterprises.

The certificate of insurance will generally be printed and will both be dated and numbered. A certificate will not be valid unless it is signed by an authorized signatory of the insurance company. The certificate of insurance will mention brief details of the insured, the location and situation of property, the sum insured and the period of insurance. Some certificates do mention the premium even though in the majority of cases it is not mentioned. Common examples are Certificates of Insurance in Automobile Insurance, Marine Cargo Insurance and Fire Insurance.

In Group Personal Accident Insurance, which covers a large number of employees of a company, insurers have the practice not to issue policies to all the employees but to issue only individual certificates of insurance. Usually, the single policy that is issued is kept with the Employer.

POLICY FORMS

This is the pucca legal document, which is an evidence of the contract of insurance between the insured and the insurer. In many countries the policy is not valid unless stamped. The policy contains some basic clauses, which are essential to every policy. The format of the policy (may) remain the same for all classes of insurance, but the terms and conditions of insurance will be different for different risks. Where the insurance is governed by Tariff, the policy wording is prescribed by the tariff. This document has to be stamped in accordance with the provisions of the Indian Stamp Act, 1989.

The following are the common features in all policies of General Insurance:

- (1) **The Heading:** giving the insurers name and address of the registered office.
- (2) **Preamble and recital clause:** This mentions the names of parties to the contract of insurance namely the insured and the insurer. There is then a mention of the contingency on the occurrence of which the insurer will indemnify the insured as agreed between them.
- (3) **Operative or insuring clause:** This is the essence of the contract. It specifies the perils insured under the policy, perils specifically excluded, terms and conditions, endorsements, and limits of liability.
- (4) **The Schedule:** Wherein are mentioned the description of the property insured and its location and situation.
- (5) **The value at risk/the sum insured:** If there are some warranties attached to the property, these would be mentioned on the face of the policy.
- (6) **Attestations and signature clause:** Provides for the signatures of the authorized official of the insurer.
- (7) **Conditions:** Any express conditions, which regulate the contract.
- (8) **The period of insurance:** Normally, every General Insurance contract is issued for one full year.

In India, the Fire Insurance policy is written to commence from the midnight of a certain date till 4.00 p.m. on the date following the completion of one year. e.g. A fire policy will be issued to commence from the midnight of 1st January, 1999 to 4.00 p.m. on 1st January, 2000. When a policy is issued to commence from 1st January, 1998 to 31st December, 1998 it means the cover is from midnight to midnight. Most marine and motor policies are issued in this way from midnight to midnight.

Every policy contains terms and conditions which must be fulfilled. The most important conditions are those relating to the prompt and immediate notice of loss to the insurer, those making it obligatory on the part of the insured to take adequate steps to minimize the losses, those in respect of cancellation of the policy from either the insurer or the



insured and the extent of the premium refundable for the unexpired portion of the risk and other contingencies like reference to arbitrators in the event of a dispute on the amount of settlement and finally on the period of limitation in making a claim.

The schedule of the policy, which contains important features of risks is sometimes separately attached to the policy but nevertheless forms part of the policy.

ENDORSEMENTS

Subsequent to the issue of an insurance policy, if there is a need to modify the terms and conditions of the policy, it is done by setting out the alteration in a memorandum. This memorandum is called as endorsement.

An endorsement is issued subsequent to the issue of policy, whenever there is a need for it. When an endorsement is issued the policy must be read together with the endorsement since many endorsements may give effect to an alteration of the important features of the risk, warranting in many cases, charging of a different premium. (basically 3 types of endorsements – Extra, Nil & Refund. Extra endorsement – Involves additional premium, Nil endorsement – Involves change in some data such as address, corrections etc. Refund endorsement – Means cancellation of policy or refund of a part of/full premium)

Generally endorsements are issued for such alterations as

- (1) Change in insurable interest
- (2) Cancellation of insurance
- (3) Change in the value at risk
- (4) Change in the location or situation of risk
- (5) Reduction or addition to the risk
- (6) Change of the insured as when a transfer of interest or assignment of interest is made. Sometimes an endorsement is also issued to correct a typographical error in the policy already issued.

INTERPRETATION OF POLICIES

In the past, most insurance policies had complicated wording and thus were variously interpreted and whenever a dispute arose between the insured and the insurer on the interpretation of the policy, the courts laid down some specific norms for interpretation of policies. For example a vague term in the policy must be interpreted against the insurer who drafted the policy, that is to say, for the benefit of the insured whose rights may have been prejudiced by an unfavorable interpretation of the policy. In the policy itself the typed word has precedence over the printed word and the written word has precedence over the typed word. Since the policy is based on the proposal form, when the proposal form contains a misrepresentation which is material to the risk, the policy

may be held to be null and void and no claim is payable. However, if the suppression of the material fact is innocent, the contract is voidable at the option of the insurer who is the aggrieved party.

Some of the rules are as follows:

- Printed and written portion of the policy is to be construed together as far as possible. In case of contradiction, the written portion over-rides the printed portion.
- The policy is to be interpreted as a whole.
- The words in the policy are to be given their plain, ordinary and popular meaning.
- Technical words are to be given their strict technical meaning.
- The ordinary rules of grammar shall apply.

CO-INSURANCE

Where the amount of insurance on large industrial complexes is substantial, it is possible for the insured to interest different insurers in the risk for varying proportions of acceptance, so that the total is covered. The practice is for each insurer to issue a policy with a specification or schedule giving a description of the property insured, with the “co-insurance clause” included therein.

Survey of the risk, rating, collection of premium and preparation of the specification is carried out by the “leading office”, that is the office carrying the largest share in the business.

Co-insurance in British circles means insuring part of the value at risks as agreed with the original insurer. All co-insurances are agreed upon prior to the issue of the original policy. The co-insurances in practice are dictated by business connections or for reducing the insurers’ commitments. Where different insurers have a history of association with subsidiaries, Co-insurance is generally made between them.

The co-insurers will be given a percentage of the original premium depending on their share of the sum insured and also bear a ratable share of loss where there is co-insurance. The names of co-insurers with the share of the sum insured will be mentioned in the original policy. This is called a collective co-insurance policy. Sometimes, co-insurers for their relative share of sum insured issue individual co-insurance policies.

Methods by which co-insurance agreements are transacted can be summarised as follows:

- **Method I:** Each insurer issues a separate policy for the proportion of interest insured. In the event of loss, each company’s liability is limited to such proportion of loss.



- **Method II:** The specification of the property is attached to the policy issued by the leading office. The policy is signed by the leading office for its proportion of insurance and then signed by the other insurers for their respective shares of interest. This is called as a collective policy.
- **Method III:** The leading office issues the policy and signs on behalf of the participating insurers. A clause called “collective clause” is incorporated in the policy.

A letter of authority is issued by the “participating insurers” to the “leading office” for the following:

- Signing the policies, endorsements, and renewal receipts
- Collection and adjustment of premium
- Inspection of risk
- Settlement of standard claims.

After receipt of the premium or the payment of a claim is made, the leading office makes arrangements for payment to or recovery from the co-insurers of their proportion of the premiums and the claims as the case may be.

RENEWAL NOTICE

This is the notice sent by the insurer to the insured calling for renewal of the policy. This is a traditional formality. Although it is not obligatory on the part of insurers to intimate to the insured regarding the policy renewal date, yet as a matter of courtesy and healthy business practice, insurers generally send renewal notices.

This is normally sent at least a month before the expiry of the policy. This is not necessary but useful especially where there is competition. Many times the insureds do not renew the policy merely because they did not receive the renewal notice; then it becomes a matter of prestige.

Sometimes the insurers do not seek renewal where the loss experience is adverse. For renewal notices to be sent, there must be proper registration of all the risks. A renewal register is maintained based on copies of policies issued in an office, that is why, whenever a policy is cancelled a copy of the cancellation notice must be sent to the person or the section maintaining the renewal register. The renewal notice mentions the premium payable for renewal along with the breakup indicating loading and discounts as permissible.

The renewal notice incorporates all the relevant particulars of the policy such as the sum insured, the annual premium, etc.

The insured is also advised in the note that he should intimate any material alteration in the risk, if any. In a motor renewal notice for example, the insured’s attention is

drawn to revise the sum insured (i.e. the insured declared value) in the light of current market values.

Lastly, the insured's attention is also drawn to the statutory provision that no risk can be assumed unless the premium is paid in advance.

GENERAL INSURANCE POLICY PROVISIONS & CONDITIONS

Exclusions Provision

1. Perils excluded

In general all insurance policies exclude some perils, which can cause higher losses. Exclusions are the insurers way of drafting and limiting the agreement to make it unambiguous and definite. In general, exclusions are made for three different reasons:

- To exclude perils that are uninsurable;
- To see that these perils are covered separately in another policy;
- To cover these perils through separate endorsements on payment of additional premium.

2. Uninsurable perils

Losses arising out of war or a warlike action or rebellion and nuclear risks are generally excluded by all insurance because these losses are unpredictable and are often catastrophic in nature. Similarly insurance companies also exclude normal wear and tear, gradual deterioration, and damages due to insects etc, because these are non-accidental and are normal losses.

3. Perils to be covered through separate policies

Some of the policies are specially designed for the perils, which are to be excluded from coverage under normal insurance policies. This system helps to separate insurance for personal risk and business risk. Like for example, perils arising out of use of personal vehicles for business purposes are excluded from personal automobile coverage. Separate policies have to be obtained for the two different risks.

4. Coverage through endorsement at extra premium

Certain perils, which are normally excluded from the policies, can be added to the normal policy through endorsements, at the request of the insured. These endorsements are normally undertaken at a higher premium than the normal policy premium. Like, for example, damages due to earthquake are excluded from the normal property insurance policies that are offered. And the insured can obtain coverage as an endorsement on payment of an additional premium.



5. Excluded Losses

Most insurance policies differentiate between direct losses and indirect losses; they do not cover indirect losses arising out of the peril, even though the peril itself is covered under the policy. Commercial property insurance generally covers only direct losses arising due to proximate causes. If the loss arises due to an unbroken chain of events caused by the peril, which is insured, it qualifies under “direct loss”. Like, for example in case of loss due to fire, losses arising as a result of fire fighting, viz. breaking windows, making holes on the roof, are also considered as direct loss. But loss of income due to interruption in business as a result of the fire is considered as indirect loss.

If the assured wants to be covered against the indirect losses, he must obtain separate policy for the same.

6. Property Exclusions

Property insurance is taken to cover the loss arising out of property damages. Property insurance policies commonly exclude loss of money, bills, manuscripts, deeds, bullions etc. Unless provided for, property insurance only covers the integral parts of the property and excludes all its contents. For example, automobile policies cover any damage to the vehicle but exclude damage of any property (goods, etc.) transported in the vehicle.

7. Exclusion of Locations

The property insurance policy agreements, in general, specify that the coverage is available only if the property is within the limits of the location specified in the declaration. Only a few insurers provide worldwide protection for the policy. Some insurers provide partial coverage for some specific properties, if it is outside the boundaries of the specified location.

The exception to the limitation of location is when the property is moved to a safe place for the sake of safeguarding it from destruction. The removal is generally allowed for a limited time and the coverage for the removal is generally broad with very few limitations. Accidental damage during transit is also covered. Courts also allow coverage for thefts during the removal process even though theft may be excluded from the insurance policy.

Warranties

Warranty is a statement by which the assured undertakes that some particular thing shall not be done or that some condition shall be fulfilled, or whereby he affirms or negates the existence of a particular state of facts. Warranties can either relate to facts existing at the time of the contract or relate to the future. It is an undertaking given by the insured either voluntarily or at the instance of the insurer about something that will determine the insurability of the risk. For example, in a Marine Cargo policy, a

warranty may read “Warranted that the condiments transported are packed in airtight containers”.

Common Policy Conditions

Conditions are stipulations in the policy, which help in regulating the contract. These may be implied or express conditions.

The implied conditions

In the absence of express conditions, the insurance contract is subject to implied conditions, which relate to

- i. Good faith
- ii. Insurable interest
- iii. Subject matter of insurance
- iv. Identification of the subject matter

Implied conditions can be expressed in a policy explicitly, or can be modified or excluded by the express conditions.

Express conditions

These are clearly stated on the policy. There are two types of express conditions,

- a) General conditions, which are applicable to all policies of that class and are therefore, printed on the policy document.
- b) Special conditions, which are applicable only to that specific policy. The special conditions are thus handwritten or typed or rubber-stamped on the policy. (e.g., type of packing, compulsory excess, unloading survey, etc.)

All conditions whether expressed or implied are the operative clauses of a policy. They are recited as conditions to be fulfilled by the insured for assuming the right to recover under the policy. The conditions are further classified into the following types:

- **Conditions precedent:** which precede the formation of the insurance contract. The statements made in the proposal must be true and complete. The contracts also pre-requires that the subject matter must be adequate in all respects, and should exist when the contract comes into force. The fulfillment of the conditions is essential for the validity of the contract.
- **Conditions subsequent:** to validity of the policy are matters that are considered by the parties as required for the continued validity of the policy. One of these is that the insured would not transfer his interest in the property or the subject matter without the consent of the insurer. The risk of the contract should remain constant and should not be altered.



- **Conditions precedent to liability:** The assured in the event of occurrence of a loss must fulfil conditions, which are precedent to the liability of the insurer. Otherwise the insurer is freed from honouring the claim even if the loss is covered by the policy. These types of conditions include:
 - Sending the notice of the loss to the insurer immediately on its occurrence
 - Every claim, notice, and writ received by the insured on the subject matter should be forwarded to the insurer
 - The assured must cooperate fully in the investigation of the cause of loss by the insurer
 - The assured must not assume any liability or promise or offer to make any payment to the third party.
 - Loss minimization efforts – as if uninsured
 - For life insurance, proof of age and death certificate are some such conditions precedent to the liability of the insurer

The insurer cannot be held liable for non-payment if these conditions are not fulfilled.

Breach of Conditions

The policy ceases to be operative from the date of the breach. However, if the insured complies with the requisite conditions, he can hold the insurer liable for indemnification of the loss. Most of the conditions are framed to deal with the claims settlements, action required at the time of the loss, etc.

Provisions relating to Fraud

Generally insurance contracts mention that misrepresentation and concealment of any material fact or fraud will render the contract void. This condition can be included as a warning or as a condition enforceable by the court of law.

Notice of loss

Most of the contracts of insurance require the assured to give an immediate notice of any type of damage or loss, if possible. However, if it is not practicable then the insured should report the loss within a reasonable time frame. The purpose of this clause is to enable the insurer to inspect the loss and collect the evidences needed to support the claim. Again it also ensures that the insured gets the benefit of the policy quickly.

Proof of loss

After property loss has occurred the insured has to submit a formal proof of loss and its amount within the stipulated time. Generally the insurance agent or an adjuster helps the insured in doing so but the onus is primarily on the insured to notify the insurer and substantiate the amount of loss.

However the insurer can take adequate time to investigate further if he wishes to. Lastly, any legal suit must commence within 12 months of the occurrence of the loss. The insurer has to settle the claim expeditiously after receiving all relevant documents.

Appraisal

Most property insurance contracts provide that if the parties to the contract cannot agree on the amount of loss, an independent arbitrator can be selected by both of them. This arbitrator can act as an impartial umpire and can value the loss. Although the parties to the contract do not resort to this process generally, it is mandatory in nature since it is a policy condition.

Protection of property

Most insurance contracts contain provisions that require the insured to take up reasonable steps for protecting the property from damage. The failure of the insured to carry out the requirements of such provisions relieves the insurer from any liability.

Cancellation

All insurance contracts mention the conditions under which the policy might be terminated and cancelled. In case of general insurance contracts, either of the parties can cancel the policy. The notice for the same is given for 7, 10 or 30 days. This gives the insured time to obtain coverage elsewhere. Any advance premium paid has to be returned to the insured. Where the insured opts for canceling the policy he receives a lesser amount than what is otherwise available calculated on the basis of short-period rates.

Time limitations

As has been mentioned earlier the insured has to notify the insurer on the loss suffered within the specified limits of time set forth. The event of loss has to be notified, the proof of loss has to be submitted, and the claim amount is to be paid.

Certain other types of time limits are also found in the insurance contracts. In case of business interruption insurance, the payment is made on account of net profit lost and necessary continuing expenses. The payment primarily depends on the length of time for which the business was shut down.

Waiver of Breach

Where the insurer waives the breach of any of the conditions by the insured the effect is same as the condition being fulfilled by the insured.

In Barrett Bros. Ltd. Vs. Lickiss, the assured was involved in a motor accident. He had received a notice, which was an intended prosecution for the above accident. The insured had neither informed the insurer about the accident nor had he forwarded the notice to them. The insurer on coming to know about the prosecution from the police,



instead of asking for the notices, merely asked for the reason why he had not complied with the requisite condition. The letter of the insurer was considered as a waiver of the breach by the insured. The fulfillment of the conditions mostly depends on the conduct of the insurer, and sometimes is made redundant by his conduct.

Assignment

The policy of insurance is a personal contract, and thus if the insured wants to transfer the rights of the policy, he can only do so with the consent of the insurer. The transfer of rights can be made through assignment of the policy. Assignment means transfer of the rights to another person usually made through a written document.

When the property on which insurance has been obtained, is sold the existing policy might be transferred to the buyer of the policy, with the permission of the insurer.

Assignment of Proceeds of the Policy

Mere transfer of the rights of receiving the benefits of the policy, which the insured is entitled to, does not require the approval of the insurer. This is because it does not amount to the assignment of the policy or its subject matter. The assignee thus only stands in the place of the insured for receiving the benefits of the policy. Where due to a breach of a condition the insurer declines to pay, the assignee cannot recover anything from the insurer.

Premium

The consideration for assuming the risk, by the insurer is the insurance premium. The payment can be in the form of a lump sum or in the form of a series of periodical installments (in certain portfolios such as marine cum erection, marine hull, etc.). The form of payment would be determined by the terms of the contract.

Under section 64VB of the Insurance Act 1938, the insurer is prohibited from assuming any risk in India without receiving the premium in advance. Where the payment is made in the form of a cheque against the cover note, the risk on the part of the insurer only arises on receipt of the premium. In case the cheque bounces the insurer is not liable to pay anything. (but the procedures to be followed by the insurer such as intimation of cancellation by RPAD, passing cancellation endt., intimate RTO in case of motor insurance, etc.)

The insurer should actually receive the premium before he can assume the risk. The insurer can assume risk if the amount is paid to the agent or a money order is booked or is posted. It must also be noted that acceptance of the premium by the insurer does not amount to conclusion of the contract (acceptance of the money as 'advance deposit' only saves the insurer. Otherwise, insurer is most likely to be held liable in a legal proceeding).

Return of Premium

The right to make a claim for the refund of premium arises:

1. For failures in consideration
2. By agreement
 - a) The insured can claim for a refund of the premium if the insurer doesn't run any risk,
 - Where the parties were never ad idem, i.e. were of one mind. This is applicable for all branches;
 - Where the contract is ultra vires;
 - Where the contract is void ab initio due to fraud or misrepresentation by the insured;
 - Where the risk was never attached, as for example insurance for property, which was destroyed before the contract was made;
 - Where the policy is illegal.
 - b) In case the insurer has assumed risk and the contract becomes void thereafter, the insurer cannot claim refund of the premium or any part thereof.
 - c) Where the insured commits a breach of warranty, owing to fraud or misrepresentation, the insurer avoids the contract and has to return the premium received; he can of course forfeit the premiums if the contract provides so.
 - d) Premium amount can be refunded partially when the insurance contract is terminated before the normal expiry date, either through mutual agreement or by virtue of the right to terminate the contract (as may be contractual) at any time.

Deductibles Provisions

A deductible is that portion of the amount of an insured loss, which the insured agrees to pay. It is common in almost all types of insurance policies to stipulate a definite amount of money, which is to be borne by the insured. The insurer becomes liable for any amount beyond the deductible amount stated in the contract.

Deductibles

A deductible is a provision by which a specific amount is subtracted from the total loss payment that otherwise would be payable. Deductibles are usually found in auto, property and health insurance. Deductibles are not used in life insurance because the death of an insured is always a total loss. It is also not used in personal liability insurance because even for a small claim, the insurer must provide a legal defence.



Deductibles may be either compulsory or voluntary. Voluntary deductibles will fetch a discount in the premium. (also known as 'excess').

The most common forms of deductibles are as under: -

- **Straight deductibles** the simplest yet most effective type, apply to all types of policies and involve subtracting the deductible amount from the aggregate loss to determine the loss payment.
- **Aggregate and calendar year deductibles**, applies for an entire year, where the insured absorbs all the losses occurring during the year, till the deductible limit. The insurer pays for all the losses beyond that level.
- **Franchisee deductible** is expressed as a percentage of the total value of the property. The liability of the insurer arises if the loss amount exceeds this amount.

Coinsurance Provisions

Coinsurance has different meanings for different types of insurance policies. For property related policies the insured bears a portion of the risk only when it is underinsured. The main reason behind this is to ensure that the insured willingly protects the property insured.

Different meanings of coinsurance

1. Coinsurance is a method by which more than one insurer share a risk in agreed proportion.

Example: An industry that is insured for Rs. 1000 crores with a premium of Rs. 50 crores is shared by three insurers.

Insurer	Share	Sum insured	Premium
A	40%	400 crore	20 crore
B	30%	300 crore	15 crore
C	30%	300 crore	15 crore

If and when a claim arises it is paid in the same proportion. Insurer A who is having a larger share is the leader and he will issue policy and services the account.

2. Coinsurance also means sharing the loss by the insured. When a claim arises under the policy the insured bears an agreed portion of loss. This may be expressed as a percent or certain specified amount.

Example: Under a Mediclaim policy it may be agreed that in every claim the insured bears 10% and the balance is paid by the insurer. This is also known as deductible or excess. In some policies there will be compulsory deductible.

Along with compulsory deductible there can be provision for voluntary deductible, which will result in reduction in premium depending upon the size of deductible. Higher the deductible more the discount in the premium.

Operational aspects

The losses are calculated and divided between the insurer and the insured on a prorata basis.

This depends on the ratio between the actual insurance carried and the amount of insurance required. The amount to be collected from the insurer is thus calculated using the following formula: -

$$\text{Recovery} = \frac{\text{insurance carried}}{\text{insurance required}} * \text{loss}$$

Questions



1. "Proposal is the basis of insurance". Discuss
2. Discuss the relative importance of the information called for in a proposal form.
3. Differentiate between a cover note and an insurance policy.
4. When and why are "certificate of insurance" issued in place of a regular policy?
5. Enumerate and discuss the circumstances when insurers insist on filing of Endorsements.
6. What are the rules for interpretation of policies?
7. How do insurers limit their liability through a contract of co-insurance?
8. Is it obligatory for insurers to issue renewal notices?

CHAPTER – 6

PROPERTY AND CASUALTY INSURANCE

OUTLINE OF THE CHAPTER

- Introduction
- Nature and Scope of Standard Fire and special perils policy
- Nature and Scope of Marine Insurance policy
- Nature and Scope of Motor Insurance policy
- Questions

LEARNING OBJECTIVES

- To understand the coverage of a fire insurance policy to mitigate fire loss consequences
- To know the different types of perils that can hamper a marine adventure, that need to be covered by insurance.
- To understand the implications of third party liability as covered under a motor insurance policy
- To study the claims settlement procedure followed in the settlement of claims under the fire, marine and motor policies
- To understand the grievance redressal procedure under the MACT (Motor Accident Claims Tribunal)
- Understand the importance of the Lok Adalat/Lok Nyayalaya

INTRODUCTION

Property Loss exposures refers to the inherent risks to which the different types of property are exposed. The various risks exposures are natural calamities, fire, floods, theft, etc. All general insurance policies intend to protect the insured from the financial consequences of these risks. This chapter deals with property loss exposures and the ways in which such property loss exposures may be covered in practice. The various types of property include Buildings, Personal property, Money and securities, Motor vehicles and trailer, Property in transit, Ships and cargo, Boilers and machinery etc.

Causes of loss, or perils, that can damage or destroy property are sometimes listed in insurance policies called “Named Perils” policies. Other policies called “Special Forms coverage” or “Open Perils”, provide coverage for any direct loss to property unless

the loss is covered by a peril that is specifically excluded by the policy. The financial consequences of a property loss can include:

- A loss of/reduction in the value of the property
- Loss to income because the property cannot be used
- Increased expenses

It is to be noted that, in any loss situation, there are other parties, in addition to the property owner, who might be affected by a property loss. These parties include secured lenders, users of property and other holders of property.

We shall now discuss the various general insurance covers namely:

- Fire Insurance
- Marine Insurance
- Motor insurance

FIRE INSURANCE

A contract of fire insurance can be defined as a property insurance agreement whereby the insurer undertakes to compensate the financial loss suffered by the insured due to damage or destruction of the insured property by fire or other specified perils, during a stated period.

Like other insurance contracts the general provisions of Law of Contract as laid down in the Indian Contract Act, 1872 govern fire insurance contracts. It implies that fire insurance also has to satisfy the essentials of a valid contract.

Definition of fire insurance

The Insurance Companies Act 1958, of England defined fire insurance business as “the issue of, or the undertaking of liability under policies of insurance against loss by or incidental to fire”.

Section 2 of the Indian Insurance Act, 1938 defines fire insurance business as “*the business of effecting, otherwise than incidentally to some other class of insurance business, contract of insurance against loss by or incidental to fire or other occurrence customarily included among the risks insured against in fire insurance policies*”.

From the above definitions the test of fire insurance contract can be summarised as whether or not

- It is a contract of insurance
- The primary object is insurance against loss or damage caused by fire
- The liability of insurer is limited to the extent of the sum assured or to the extent of damage caused by fire, whichever is less



- The insurer has no interest in the safety or damage of the insured property other than the liability undertaken

Characteristics of fire insurance contract

The above discussion implies that a fire insurance contract like other general insurance contract has the following specific characteristics:

- It is a contract of indemnity
- It is a contract of utmost good faith
- It is a personal contract
- Generally the cause of fire is immaterial
- Existence of insurable interest
- It is an indivisible contract
- Subrogation and contribution

STANDARD FIRE INSURANCE POLICY

A standard fire insurance policy contains the terms and conditions of the policy. The General Insurance Act (Tariff) recommends the form of the contract in which a fire insurance is to be written. The policy form contains a preamble and operative clauses, general exclusions and general conditions.

(From April 2008, insurers can be flexible in drafting and designing their own wordings of all insurance contracts – subject to IRDA's prior approval.)

Preamble and operative clause: This clause contains the preamble, the perils covered and limitation of the sum assured. The preamble lists out the parties to the contract.

General exclusions: This section of the policy lists out the nine general exclusions expressed in the policy.

General conditions: There are fifteen expressed general conditions in a fire insurance policy.

In India, the fire tariff was recently revised w.e.f. 1st April 2000 and underwent one more change w.e.f. 31st March 2001.

The fire policy has been renamed as THE STANDARD FIRE AND SPECIAL PERILS POLICY.

Scope and Coverage Under A Standard Fire and Special Perils Policy

The Fire Policy can be issued to cover standard fire risks as well as certain special perils. There are 12 different types of risks covered under the above policy:

1. Fire
2. Lightning
3. Explosion / implosion
4. Aircraft damage
5. Riot, Strike, Malicious and Terrorism damage (RSMTD)
6. Storm, Cyclone, Typhoon, Tempest, Hurricane, Tornado, Flood and Inundation (STFI)
7. Impact damage by rail/ road/ vehicle or animal
8. Subsidence and landslide (including rockslide)
9. Bursting and/or overflowing of water tanks, apparatus and pipes
10. Missile testing operations
11. Leakage from automatic sprinkler installations
12. Bush fire – damage caused by forest fire is excluded

***Note:** The liability of the insurance company *shall in no case exceed:*

- In case of individual items – the sum insured (SI) for each item stated in the schedule
- As a whole – the total sum insured (TSI)

Add-on-covers

With certain additional premiums, and subject to certain conditions and warranties, there are 14 add-on-covers that can be availed such as:

1. Architects, Surveyors, and Consulting Engineers fees (in excess of 3% of adjusted loss)
2. Cost of removal of debris (in excess of 1% of claim amount)
3. Deterioration of stocks in cold storage premises due to
 - Power failure
 - Change in temperature
4. Forest fire
5. Impact damage due to insured's own vehicle, forklifts etc.
6. Spontaneous combustion including own fermentation and natural heating
7. Omission to insure addition/ alteration/ extensions
8. Earthquake (fire and shock) – India has four zones for rating purposes



9. Spoilage material damage cover – due to retardation or interruption of any process
10. Leakage and contamination cover – applicable to oils and chemicals only
11. Temporary removal of stocks – not exceeding 10% of S.I under the policy
12. Loss of rent – caused by operation of insured perils
13. Additional rent for alternative accommodation – caused due to operation of insured perils Start-up expenses.

General Exclusions

The Standard fire and special perils policy does not cover the following:

1. 5% of each and every claim –
 - Subject to a minimum of Rs. 10,000/- in respect of losses arising from *Acts of God Perils*
 - Rs. 10,000/- for each and every loss out of other perils

The excess shall apply per event per insured.

2. Loss, destruction or damage caused by
 - war
 - ionizing/ radiation/ nuclear fuel or material
 - pollution
3. Loss, destruction or damage caused to
 - bullion, precious stones, works of art for an amount exceeding Rs. 10,000, books of accounts, paper money explosives etc. (to be specifically described and valued)
 - stocks in cold storage
 - any electrical/electronic machinery (fans, wiring due to short circuit)
4. Loss of earnings, loss by delay, consequential loss etc.
5. Loss/ damage by spoilage, interruption/ cessation of any process
6. Loss by theft during or after the occurrence of an insured peril
7. Loss by natural calamity
8. Loss due to temporary shifting of machinery for repairs, cleaning, renovation for a period not exceeding 60 days
9. Expenses in excess of
 - 3% of adjusted loss in respect of Architects, surveyors, engineers fees
 - 1% of claim amount in respect of debris removal

TYPES OF FIRE POLICIES

Reinstatement value policies

Reinstatement in simple terms means replacement of lost property or repairing damaged property. The clause is related to the fire insurance policy of fixed assets like buildings, machinery, furniture and fittings etc.

A reinstatement value policy is the standard policy with a value reinstatement clause. The reinstatement clause of the policy states that in the event of loss, the payment to be made to the insured is the cost of reinstating the same kind of property by a new one. Unlike a standard policy where the insured can recover only the depreciated value of the insured property here the insured is entitled to recover the cost of replacing the lost or damaged property.

The conditions governing the reinstatement by insurer are stated in the Condition 7 of the policy. The following points are considered in a reinstatement value policy:

- The insured shall intimate the insurer about his interest in reinstating the property within the time allowed. Otherwise the loss is settled on indemnity basis.
- If the insured is not interested in reinstatement, the insurer is liable only for the market value (or the depreciated value) of the property lost by fire.
- Until reinstatement is carried out and expenditure incurred, the insurer's liability is on an indemnity basis.
- The insured must carry on the process of reinstatement within a reasonable time and complete it within 12 months after destruction of the property or within the time stipulated by the insurer. If the insured fails to do so the insurer's liability is on the basis of market value.
- The insured has to submit the plans, specifications and other details needed for the reinstatement, to the insurer at his expense. In addition, when the insurer demands for such plans it does not imply that he is elected to reinstate the property.
- The insured may opt for reinstatement at a different site provided the insurer's liability doesn't increase.
- The insurer after electing to reinstate should put the property considerably close to what it was before the fire. He is liable for the damages if he fails to do so (Braithwaite Vs. Employer's Liability Assce. Corp.).

The insurer exercises his right of reinstatement when:

- The conditions of the policy confer the right to reinstatement on the insurer.
- The insurer suspects that the loss is the result of a willful act of the insured.
- The insurer is bound to reinstate upon a request of any person but not the insured who has an interest in the subject-matter of insurance.



Floating policy

Floating policy is applicable to the inventory of the policyholder. Some traders have stocks that are stored in more than one warehouse or may be lying in process blocks. They may not be able to keep an account of these stocks on daily basis. Such traders can furnish the total value of all the stocks to the insurer and obtain a floating policy of fire insurance. A floating policy covers stocks located in various godowns in a single sum insured. Such policies involve higher risk and therefore higher premium. The premium charged is the highest rate chargeable to any one location with a nominal rate of loading. If the stocks are located in the same compound no loading is charged on the premium. The premium may be loaded by say 25% for three locations and 50% for more than 3 locations. (during 2007, after detariffing, insurers were allowed to give a max. of 51.25% discount on the applicable rates. Now, pricing and wordings and terms can be decided by individual insurers – after clearance from IRDA)

Illustration 1:

A trader has stocks stored in 3 godowns namely X, Y & Z. The premium chargeable at different locations is given below:

Godown	Rate of premium per '000	
X	Rs.	1.25
Y	Rs.	1.75
Z	Rs.	2.00
Sum assured	Rs.	12,00,000

Since the highest premium is Rs. 2.00 per Rs. 1000 the premium chargeable is Rs. 2400.

The loading is taken as 25% here because there are only three locations. So, the loading is 25% of Rs. 2400 that is equal to Rs. 600. Thus, the premium payable is Rs. 3000.

General features of floating policy:

- The policy is issued only for the stocks and does not apply to immovable properties like machinery, furniture etc.
- The insured has to give the addresses of each godown. Any change in address should be intimated to the insurer.
- The insured is required to have an efficient internal audit and accounting system that can provide the total amount at risk and locations whenever required.

Declaration policy

Declaration policy is a special policy related to stocks of the insured. It is issued in the

interest of those traders who deal in seasonal goods. The stocks may have fluctuating values. During peak time the stock values are highest and during the slack season their value is reduced. It is difficult to fix a sum assured for such goods. There may be over insurance if the value is ascertained during peak season and under insurance if the value is ascertained in the slack season. To overcome this problem, a declaration policy is devised.

In the declaration policy the sum assured is selected by the insured on the basis of highest stock value. On this value premium is computed provisionally and is paid as provisional premium. Subsequently, the insured declares the actual stock value at risk every month. Monthly declarations are based on (a) The average of the values at risk on each day of the month or (b) The highest value at risk during the month.

As per the provisions of Tariff Rules, (no more tariff now) declaration policies can be issued only when the minimum sum assured is Rs. 1 crore and in respect of stocks, which are the sole property of the insured. In policies “covering stock in different locations – the sum insured in at least one of these locations should not be less than Rs. 25 lacs. Hence the following Illustration 2 is to be reworked as under:

Illustration 2:

Sum assured	Rs.5,00,00,000/-
Rate per 1000	Rs.1.20
Premium due	Rs.60,000/-
Provisional premium	Rs.60,000/-
Monthly declarations of stock values:	
Jan	3,00,00,000
Feb	2,75,00,000
Mar	4,20,00,000
Apr	2,00,00,000
May	1,00,00,000
Jun	2,25,00,000
Jul	1,50,00,000
Aug	75,00,000
Sep	4,75,00,000
Oct	5,00,00,000
Nov	4,25,00,000
Dec	3,15,00,000
Total	Rs. 34,60,00,000



Average sum insured is Rs.34,60,00,000/12 = 2,88,33,333.33

Premium on average sum insured at Rs. 1.20 per 1000 will be Rs.34600.

Therefore, the premium to be refunded is Rs.60,000 – 34,600 = Rs.25,400

The balance refunded to the insured shall not exceed 50% of the provisional premium. The insurer is liable at the most to the sum insured and cannot receive any excess premium.

Illustration 3:

Let us assume that declaration for April is Rs.6,40,00,000, for May Rs.6,25,00,000 and on June 6th the stock is destroyed by fire causing a loss of 13,00,000. Later it is found that the actual declaration for May is 6,50,00,000. Then, the loss payable is calculated as follows:

$$\begin{array}{r} 1300000 \\ \hline 65000000 \end{array} \times 62500000 = \text{Rs. } 12,50,000$$

If the insured has taken any other policy in addition to declaration policy, then the claim is settled first by the other policy. The declaration policy operates for the excess of the stock value over the sum insured under the other policy.

Illustration 4:

Value of stock at the time of fire	Rs.1,50,00,000
Loss assessed	Rs. 15,00,000
Standard policy A incurred	Rs. 50,00,000
Standard policy B	Rs. 30,00,000
Declaration policy C	Rs. 1,00,00,000

Now, when the loss occurs, policy A and B will be applied first. For the remaining loss if any, the declaration policy C shall be applied. This is explained below.

Apply average

Share of loss = Insured value/value of property*loss

$$\begin{array}{r} \text{A's share} = 50,00,000 \\ \hline 1,50,00,000 \end{array} * 15,00,000 = 5,00,000$$

$$\begin{array}{r} \text{B's share} = 30,00,000 \\ \hline 1,50,00,000 \end{array} * 15,00,000 = 3,00,000$$

It is clear that the loss remains even after receiving payments from A and B. The excess of loss over the sum insured is the difference between the declared value and the policy valued in A and B.

Declared value	Rs. 1,50,00,000
Policy valued in A and B	Rs. 8,00,000 (5,00,000 + 3,00,000)
Excess of loss	Rs. 7,00,000 (15,00,000 - 8,00,000)

Declaration policy's share = Sum assured or excess whichever is less loss

Declared value

$$\text{Therefore, C's share} = \frac{1,00,00,000}{1,50,00,000} * 15,00,000 = \text{Rs. } 10,00,000$$

However, since the claim amount is only Rs.15,00,000/-, the liability under the Declaration Policy will be limited to Rs.7,00,000/-.

However, if the stock values at the time of loss are collectively of greater value than the sum insured then the insured shall be liable for the rateable proportion of the loss accordingly. This is known as the prorata condition average.

The sum insured will be maintained at the same level at all times during the currency of the policy. Even when loss occurs, prorata premium shall be charged on the amount of loss paid.

Floater Declaration

Floater Declaration Policies can be issued subject to a minimum sum insured of Rs.2,00,00,00/- and compliance with the rules of Floater and Declaration Policies respectively except that the minimum retention should be 80% of the annual premium.

Discount in premium

The insurance company allows discount to those insured, where the insured take utmost care and precautionary measures in preventing fire. For instance, the insured may be entitled for a special discount if the insured installs a sprinkler (or other favourable features) in the insured building.

FIRE CLAIMS

In the event of fire, the insured must immediately give the insurer a notice about the loss caused by fire. A written claim should be delivered within 15 days from the date of loss. In addition, the insured is required to furnish all plans, invoices, documents, proofs and other relevant information required by the insurer. If the insured fails to submit these documents within 6 months from the date of loss the insurer has the right to consider it as no claim.



Procedure on receipt of claim

On receipt of the claim the insurer verifies whether the following essentials of a valid claim are satisfied or not:

(Practically, first appoint a surveyor after obtaining the claim form or send even an oral intimation. Time is of essence in not losing crucial evidences of a fire accident. If major claim, it can be a preliminary survey. Only the surveyor gives his opinion in his report whether the claim is admissible or not)

- The cause of fire should be an insured peril. When fire is caused by more than one reason the dominant reason should be an insured peril
- The operation of the peril should not be an exception
- The fire caused by insured peril should result in a loss or damage of the property insured
- Such a loss should occur during the time the policy is under operation
- The insured has to carryout all the terms and conditions of the policy and should also fulfil the post-claim requirements.

Claim form: If the claim arises in a new insurance or closely after the renewal of the policy the insurer observes close proximity. This necessitates an extra investigation of the circumstances. When these conditions are complied with, a claim is registered and a claim number is allotted for future reference. The claim register records all the details of the claim like date of fire, policy number, name of the insured etc; a claim form is issued to the insured after registration. It requires details like

1. Name and address of the insured and the policy number
2. Date, time, cause and circumstances of the fire
3. Details of damaged property
4. Sound value of the property at the time of fire
5. Amount claimed after deduction of salvage value
6. Situation and occupancy of the premises in which the fire occurred
7. Capacity in which the insured claims, as owner, mortgagee etc.
8. If any other person is interested in the property damaged
9. If any other insurance is in force upon such property, if so details thereof.
10. Whether reported to Fire Brigade and if so, their report. For all fire claims, where actual fire has taken place, fire brigade report is a must. It is like an FIR for an accident claim.

The insured completes the form, signs the declaration given in the form as to the truthfulness and accuracy of the information and returns the same. The issue of the claim form is in no way deemed to be an acceptance of liability by the insurer.

In-house survey: In-house survey is applied to the uncomplicated claims involving small losses. An official employed by the insurer investigates such small and simple claims. On the basis of the claim form and the investigation report the company then settles the claim.

Independent surveyor: For large claims the insurance company employs independent loss surveyor and assessors to investigate and report on the cause and extent of claim. As per the Insurance Act 1938, a licensed surveyor must survey all claims of Rs. 20,000/- and above. (IRDA increased the limits to 50,000 after Gujarat floods for a limited period of 2 months).

The surveyor interviews the insured and other persons, inspects the damaged premises and examines the documents submitted by the insured. After the initial investigation he submits his first report to briefly point out –

- The date of loss
- Situation of loss and the details of the occupancy at the time of loss
- The cause of the loss if ascertainable
- A preliminary estimate of the loss or damage
- Any other relevant information.

The preliminary report submitted by the surveyor assists the insurer in discussing the issue with the insured if required. The surveyor may also submit such a report to take the guidance and instructions from the insurer to overcome the problems of assessment. The surveyor also submits the interim reports to notify the insurer about the progress in loss assessment in respect of the specific feature of the loss such as laboratory reports, analysis reports etc. Finally, the surveyor submits his final report to the insurer. He can however only recommend. He is not authorised to admit any liability.

Scrutiny: The insurer scrutinises the final report and all the supporting documents like final bills of repairs, photographs etc, and attachments like fire brigade reports, police reports, etc.

Adjustment of loss: The next step is to sanction the claim for payment. The insurer sends a discharge voucher to the insured. All the persons named in the policy as insured sign and return it to the insurer.

Burden of proof

As per the provisions of the Evidence Act, 1872, “the burden of proof as to any particular fact lies on that person who wishes the court to believe in its existence.” therefore, the burden of proof lies on the insured to prove that he incurred a loss that was caused



by an insured peril. However, if under any circumstances the insured caused the loss, the burden is on the insurer to prove that the insured himself caused the loss.

TERMINATION OF FIRE INSURANCE POLICY

Insurance under a fire insurance policy may cease where:

- The insured is guilty of misrepresentation, misdescription or non-disclosure of any material facts.
- The insured building structure or part thereof is destroyed by reasons other than an insured peril, (on the expiry of seven days there from).
- The company terminates the contract on 15 days notice to the insured on the request of the insured.
- Where the insurable interest of the owner ceases after the commencement of the policy.

MARINE INSURANCE POLICY

Marine insurance as we know it today, originated in England owing to the frequent movement of ships over high seas for trade. Marine insurance is an important element of general insurance. It essentially provides cover from loss suffered due to marine perils. Marine insurance extends beyond marine perils to provide cover for loss incurred during shipment of cargo over water bodies like rivers, lakes and inland waterways. It also covers ships under construction, docked for repairs, stranded at ports and ships transporting consignment.

Maritime insurance business today is governed by the provisions of the English Maritime Insurance Act 1906, and in India the business is regulated by the Indian Marine Insurance Act 1963, which is based on the original English act. Marine insurance covers three main interests in a marine venture. They are:

- Hull – it represents the ship;
- Cargo – it is the goods being transported by the vessel; and
- Freight – is the profit or earnings of the ship at the end of a marine venture.

(“Marine” insurance policy covers not only sea voyage but also purely inland transits through any mode like rail / road / multimodal / even by post.)

General Characteristics

Marine contract is also like any other contract. It has certain general characteristics, which will help in a better understanding of different aspects of a marine insurance contract.

Marine Insurance Act, 1963

As we already know that London was the centre of all operations regarding marine insurance transactions, hence all the customs and branches of the trade developed here. Further a bench of jurors was also appointed by Lord Mansfield to settle disputes arising as a result of breach of contract or misinterpretations or due to false claims. For years, all countries across the world followed the British Act. But necessary changes had to be made by the respective countries to suit their requirements. After Independence, the Indian Navy and shipping began growing rapidly yet there was no Indian law governing marine insurance, which was still subject to the English Marine Insurance Act. Furthermore, the Insurance contracts in India had to abide by the Indian contract Act, 1872, and there was often a conflict between the Indian Contract Act provisions and those of the English Marine Insurance Act, 1906. It therefore became essential to draft a legislation to suit the Indian scenario. As a result of this, the Marine Insurance Act was enacted by the Indian Parliament, which came into force from August 1st, 1963.

Maritime Perils (Insured and Uninsured)

Maritime perils can be defined as the fortuitous (it represents an element of chance or ill luck) accidents or casualties of the sea caused without the willful intervention of human agency. There are different forms of perils at sea, of which only a few are covered by insurance while others are not. In this part we will be enumerating both the insured and uninsured perils of the sea.

Marine insurance coverage

- *Fire* – is a common peril at sea.
- *Pirates and Thieves* – according to Carver: “ Piracy is forcible robbery at sea, whether committed by marauders from outside the ship or by mariners or passengers within it.
- *Barratry* – it is an act willfully committed by the master and the crew against the owner or charterer of the ship. Barratry includes fraudulent sale of cargo or deviation of ship, the crew’s refusal to discharge the cargo, etc.
- *Jettison* – this is throwing of cargo overboard due to either a deliberate act or at the wake of grave danger.
- *Taking at sea* – is a situation when the vessel is captured by the enemy or others.
- *Foundering at Sea* – if a ship has been reported lost and after a stipulated time, there is no news of its whereabouts then it is presumed to be lost due to perils of the sea.



- *Stranding* – arises when the ship deviates from its course due to an accident and is stranded in shallow waters and suffers damages.
- *Collision* – is caused when the ship collides with another ship or with other objects, causing damage.
- *All other Perils* – This includes all perils similar in nature to the ones mentioned in the policy.
- *Perils not explicitly dealt with* – there are two other losses the insurer is bound to provide cover for. They are:
 - A) *Insurer's Liability in respect of General Average Loss (Sec 66)* – General average loss is expenditure or loss incurred consciously while countering a peril for saving the ship and /or consignment. This is borne proportionately by all having insurable interests in the marine adventure.
 - B) *Insurer's liability in respect of salvage charges* – These are charges awarded to a salvager for retrieving property from the sea. This is not part of a marine contract. This amount is contributed by all holding insurable interest in the marine adventure. The insurer is liable to cover the salvage charges incurred by the assured. This is treated as part of general average loss.

Uninsured Perils

All losses and damages caused due to reasons not considered as perils of the sea are not provided insurance cover.

- *Wear and Tear* – This is the regular deterioration that inflicts the vessel due to the corrosive action of the sea, action of winds and other maintenance problems caused to the body of the ship due to sailing. This includes perishable commodity that is transported.
- *Leakage* – If a leak develops in a vessel then insurance does not provide cover for the loss caused, unless the leak is caused by an accident. Ordinary leakage of liquid cargo is also not covered.
- *Breakage of goods* – Goods damaged due to movement of the ship are not covered by insurance. But goods damaged by the violent action of the waves are covered, as this is treated as a peril at sea.
- *Inherent Vice* – This refers to the inherent properties of the cargo being transported. Thus, the insurer cannot be made liable for perishable commodity, which has an inherent process of decomposition. This would apply to fruits, vegetables, meat, etc.
- *Loss by Rats and Vermin* – This loss is not considered as a peril of the sea. (e.g. *Hamilton v Pandrof*- a rat gnawed a hole in a pipe, causing damage to the cargo of rice by seawater, there was no negligence. The insurer was not held responsible).

- *Loss by Delay* – This means that the insurer of the vessel and the cargo cannot claim for loss caused due to delay, even if the delay is caused by a peril of the sea, which is covered by insurance. (Normally, coverage till completion of transit/ reaching destination and not defined in terms of date/days – except in case of annual declaration policies).

Types of Losses

Different kinds of loss incurred during a marine adventure are enlisted in the Marine Insurance Act, 1963 from Section 55 to Section 63.

According to Sec 55 (1) of the Act, the insurer is liable for any loss caused only due to perils of the sea, which has an insurance cover. (2) According to this sub section, the insurer is not liable for any loss incurred due to a malpractice by the assured, but the insurer is liable if the loss is proximately caused by a peril of the sea even if it could have been avoided by competent crew and the master. The sub section also excludes delay, wear and tear, leakage, etc from the insurance cover, unless the policy otherwise provides for it.

Losses are primarily divided into three categories. They are Partial loss, Total Loss and Expenses. Total loss is further classified into:

- Actual Total Loss** [Sec 57 (1)] - This situation arises when the insured object is irretrievably lost, that is it is completely damaged and does not resemble the object that had been insured prior to the marine adventure.
- Missing Ship** (Sec 58) - Actual total loss can be presumed if the ship under question is missing beyond the stipulated time.
- Constructive total loss** [Sec 60 (1)] - This section says that there is constructive total loss when the insured object has to be abandoned as; actual total loss is inevitable that is the object is damaged beyond repair and repair would cost many fold when compared to the saved object. [Sec 60(2)] – this states that there is a constructive total loss when the insured is deprived of the object, and when he is unlikely to recover the object, and when the cost of recovery of the object would exceed the value of the recovered object.

Types of Partial loss: When the loss is not constructive or actual then it is termed as partial loss. Partial loss is classified into two categories:

- General Average (Sec. 66)** – This refers to the loss incurred by the sacrifice made during extreme circumstances for the safety of the vessel and the cargo. This loss has to be borne by all the parties who have an interest in the marine adventure. General average compensation and liability are completely independent of marine insurance.

Conditions that qualify for general average contribution: loss must be incurred for common safety; loss must be at the face of impending danger; the



intention behind the loss should be general safety; expenditure caused as a result should be extraordinary, the expenditure at the face of danger should have been judiciously incurred, the imperilled subject matter should be saved; and the person responsible for the danger cannot claim a share in the contribution.

Example: The master of a ship saw smoke coming from the hold of the ship, and presumed that the hold had caught fire. He ordered high-pressure steam to be let into the hold to extinguish the fire. This damaged the cargo of resins being transported by the ship. When the insurance claim was put through on the grounds of General Average loss, the court rejected the claim. This is because the court held that the loss was not due to general average loss and the peril was not real but imagined.

- b) Particular Average** – This is a partial loss of the insured property, by a peril it is insured against. For example if a ship is damaged due to turbulent weather the loss incurred is a particular average loss. This loss may be on the ship, cargo or the freight.

Types of Expenses: These are the expenses incurred by the ship owner for labour, salvage, etc. They are discussed below:

- a) Particular Charges [Sec. 64 (2)]** – Expenses other than General average charges and salvage charges are called Particular charges. It is the loss incurred consciously to safeguard the insured subject matter. Particular charges are however, not included in Particular Average.
- b) Sue and Labour Charges (Sec. 78)** – This can be explained citing the following example. A ship is transporting hide. But during the trip it is found that seawater has damaged the hide. So the expenses incurred in reconditioning the hide at an intermediate port would qualify for sue and labour charges. This however does not include general average loss, salvage charges, expenses caused in averting an uninsured loss.
- c) Salvage charges (Sec. 65)** – This is the amount payable to a salver for recovering or salvaging property from sea.

MARINE POLICY

Different aspects of a marine policy are dealt with from Section 24 to Section 34 of the Marine Insurance Act, 1963. According to this act a marine contract is not acceptable if it is not embodied in a marine policy (Sec. 24). A marine policy should contain the specifications mentioned in this act (25), they are:

1. Name of the assured, or someone representing him;
2. The object being insured and the perils against which the insurance cover is sought;

3. The voyage, period of time, or both;
4. Insured sum;
5. Name of insurer.

Types of policies

- a) **Time and Voyage Policy (Sec. 27)** – The voyage policy is the one used to insure a subject matter ‘ at and from or from one place to another. This policy covers the subject matter irrespective of the time factor. It covers the subject matter from the port from where the voyage commences (terminus quo) till the port where the voyage ends (terminus ad quem).

The time policy on the other hand covers a subject matter for a specific period of time.

- b) **Valued Policy (Sec. 29)** – This kind of policy specifies the settled value of the subject matter that is being provided cover for. According to this policy unless there is a fraud, the value decided by the insurer and the assured is irrefutable, whether the loss is total or partial. A valued policy is in consonance with a wagering contract, that is in case the subject matter is over- valued, then a valued policy becomes a wagering contract because a marine insurance contract is a contract of indemnity (that is there is no scope of making a profit out of such a contract). For a marine contract to become a wagering contract it has to be proved that the over- valuation was fraudulent.
- c) **Unvalued policy (Sec. 30)** – This policy does not fix the value of the subject matter being insured.
- d) **Floating policy (Sec. 31)** – This kind of policy includes only the general insurance terms. It does not include the name of the ship and other details. The other details are required to be furnished through subsequent declarations, which should be eventually endorsed on the policy. This kind of policy is helpful for the assured who does not know the name of the ship transporting his goods, or by carriers, warehousemen with limited interests in the goods.
- e) **Open Policy:** Open policy and Open cover are different. Open policy is for transit within India. Premium is collected in advance at the commencement of the one year period based on the expected total declaration value i.e., sum insured. Only declaration sheets are sent by the insured and open policy is stamped with Re.1/- as it is inland. Open cover is for import/export. No sum insured mentioned in open cover document. Individual certificates are issued and insurance stamps affixed based on the sum insured of respective values.

An open cover is issued in the case of import/export. The indigenous purchases/ sales can be covered under an open policy for a continuous automatic cover. An open policy, unlike an open cover is a stamped document with necessary



clauses attached. It is issued for a period of 12 months and all consignments cleared during the period are covered by the Insurer.

Warranties

Sections 35-43 of the Marine Insurance Act, 1963 deal with the warranties. There are two types of warranties, those warranties that simply denote the insurance cover provided, and the second being promissory warranties that are a promise by the insurer that the warranties will be upheld.

There are two types of warranties [Sec 35 (2)]; they are Express warranties and Implied warranties.

Breach of Warranty is only permitted under three conditions that are listed (Sec 36) in the Marine Insurance Act, 1963. According to this section a breach can be excused:

- a) If the warranty is rendered unlawful by a subsequent law, that is *by statute*
- b) If due to changed circumstances the warranty loses relevance
- c) If the insurer waives the breach, that is *by volition*.

Express Warranties

This form of warranty may be any form of word that serves as an inference of warrant. An express warranty must be included in the policy or incorporated into the policy by reference if it is contained in any other document.

Warranty of Neutrality (Sec. 38)

Subsection (1) 'This states that insured property, whether goods or ship is expressly warranted neutral'. This implies that as far as the assured can control the insured property is deemed neutral. This is to ensure neutrality of the vessel and the goods in case of a war situation.

Subsection (2) deals with the neutrality of the ship alone. It states that the ship should be properly documented, and should produce necessary documents to establish neutrality. It also states that the ship should not suppress documents or falsify them. The insurer is not liable if there is a breach.

Warranty of Good Safety (Sec. 40)

"Where the subject-matter insured is warranted "well" or "in good safety" on a particular day, then it is sufficient if it be safe at any time during that day.

Implied Warranties:

Warranty of Seaworthiness of ship (Sec. 41)

- (1) This states that at the commencement of a marine adventure there is an implied warranty in the voyage policy that the ship is seaworthy. However, this does not apply to the cargo.

- (2) There is an implied warranty that while a ship is at a port before embarking on the marine adventure, the ship should be able to withstand the common perils of the port.
- (3) A voyage has different stages, thus there is an implied warranty that the ship should be seaworthy (with respect to equipment, crew, etc) for every stage she has been insured for.
- (4) A ship is considered seaworthy when she is capable of countering the common perils of the sea, for that marine adventure, which has insurance cover.
- (5) There is no implied warranty of seaworthiness of the ship in a time policy. But if the assured sends the ship in an unseaworthy condition then the insurer is not liable.

Warranty of Legality (Sec. 43)

This section states that there is an implied warranty that the insured marine adventure should be lawful. An adventure that is insured should abide by local and foreign laws, or it is deemed illegal. Similarly, the adventure should be carried out in a lawful manner, unless the assured can prove that the misdemeanour crept in without his knowledge, and that it was beyond his realm of control.

For example: In *Pipon v Cope* the ship was arrested in England for the act of smuggling, and it was found that the master and the owner were hand in glove in the entire act. The insurer was not held responsible.

Freight Insurance

'Freight' is defined as the profit that a ship owner makes by transporting his own cargo or the cargo of another person. Types of freight:

- **Prepaid Freight** – This is paid in advance by the owner of the goods, at his own risk. He covers this cost while insuring the goods, but in case of failure of delivery the freight is not refundable.
- **Freight Payable “ship or cargo lost or not lost”** – this is also considered as prepaid freight.
- **Freight payable on delivery** – This is paid once the goods are delivered. If the carrier fails to deliver the goods, then they are not entitled to the freight. But they are entitled to the freight if the goods are delivered in a damaged state.
- **Lump sum Freight** – This is under certain conditions (when a huge consignment is being transported), when the carrier is not required to deliver the entire cargo to receive the lump sum of freight, but a sizeable amount of the cargo should be delivered.
- **Time charter hire** – This is paid to the ship owner by the owner of the goods for making use of the ship for transporting his goods. But if due to any cause the ship is not operational for more than 24 hours then the payment ceases.



Hull Insurance

'Hull' in marine insurance refers to ocean going vessels (ships, trawlers, barges, fishing vessels, etc), its hull and machinery. This also covers "builders risks", that is when the ship is under construction.

Ships are the subject matter of hull insurance. There are different kinds of ships with respect to design, which decides the purpose of the ship. The design and construction of a ship is regulated by the respective Classification societies. They scrutinise the material used for construction, steel, engines, boilers, etc. Once the ship is constructed it has to be registered in compliance with the Merchant Shipping Act. The Indian Register of Shipping (IRS) deals with the registration of ships. This society provides the certification after assessing the mechanical and structural fitness of the ship.

Certain terms used to measure a ship

GRT (Gross Register Tonnage): This is calculated by dividing the volume in cubic ft of the hull, below the tonnage deck, plus all spaces above the deck with permanent means of closing by 100.

NRT (Net Register Tonnage): This is the space that is meant only for the carriage of goods. It is therefore the gross tonnage excluding space occupied by machinery, ballast space, accommodation of crew, etc.

DWT (Dead Weight Tonnage): Is the amount of cargo in tons required to load a ship to her maximum.

Types of vessels

- **Ocean going or general cargo vessels** – These vessels are in the 5,000 to 15,000 GRT range.
- **Dry bulk carriers** – These vessels range from a few thousand to over 70,000 GRT. Mostly employed in carrying coal, bauxite, iron, other ores, food grains, phosphates, etc.
- **Tankers or Liquid bulk carriers** – They are used to transport liquid shipments. They also have super tankers for carrying huge consignments.
- **Combination carriers** – These vessels are designed to carry dry cargo as well as oil. They are of two types: OBO's (ore/bulk/oil)- 70,000 to 150,000 DWT, and Oil/ore vessels – 150,000 to 250,000 DWT.
- **Container vessels** – These vessels are employed to transport containers laden with goods.
- **LASH (Lighter Aboard Ship)** – This vessel and a Sea Bee vessel are mother ships that transport floating containers as barges up to 1000 tons displacement. These barges are lowered into the water at a port from where it is towed to its destination.

- **Roll on – Roll off vessels** – These vessels facilitate the transport of trucks, lorries etc. These vehicles carrying the cargo are loaded, without cranes, by using side doors or stern. At the destination port these trucks drive out of the vessel to deliver the goods to the consignee.
- **Passenger vessels** – These are liners or cruise vessels or pleasure crafts.
- Fishing vessels Trawlers
- Coastal/High seas

Types of Hull Policies:

1. **Hull and Machinery Insurance:** This policy is to protect the ship owner from loss, like partial, total loss (actual total loss or constructive total loss). This also covers the ship owners contribution in case of a general average loss and also bears expenses like salvage charges, liability towards other vessels in case of collisions, labour charges etc. It provides cover to the hull, equipment, engines, boilers, other machinery, stores etc. But this policy does not provide cover to the consignment being shipped.
2. **Disbursement and Increased Value Insurance:** This policy provides insurance for all those items not included in the hull insurance estimation. This insured value can amount to 25 percent of the hull insurance value. This is meant to cover the charges borne by the ship owner while preparing the ship and stocking the ship before embarking on the marine adventure. But this amount can be insured only if freight insurance is not already put up. This policy also provides protection to the ship owner from loss, which may be partial or total (actual total loss or constructive total loss). This also covers the ship owners contribution in case of a general average loss and also bears expenses like salvage charges, liability towards other vessels in case of collisions, labour charges etc.
3. **Premiums of Insurance:** This is also called the premium reducing policy. The amount of insurance cover provided for a marine adventure is very high, therefore the premiums also amount to a considerable amount. So, it is safe to insure the premium on these covers, including the premium of the premium reducing policy. This is applicable only to a total loss situation, whereby the amount of indemnity depreciates by one-twelfth every month.
4. **Returns of Premium:** This policy is also applicable for a total loss situation. It is to insure the prospective returns in case of total loss.
5. **Loss of Hire Insurance:** This policy protects the owner from the loss incurred by him incase the ship is stranded due to some failure in machinery or anything else that is covered in the hull and machinery policy.
6. **Loss of Profits Insurance:** This is also to protect in case of total loss. This cover protects the Charterer's loss of profits. This is provided over the period the ship



is chartered for in case the ship is time chartered, or for the voyage if the ship is on hire for a voyage.

7. **Ship Repairer's Liability:** Even when the ship is being repaired, there is a chance of expenses other than the repairs, if there is negligence or an accident. Thus, the repairer is liable to the ship owner in case something happens while the repair work is in progress. This insurance provides cover to the repairer against such a situation.
8. **Builders' Risk Policy:** Like the previous policy, this covers the risk of the builders. It covers the builders from the beginning of construction, till the delivery. It also includes all the test and trials conducted before the delivery of the vessel to the concerned buyers.
9. **Charterer's Liability Policy:** When a vessel is chartered, if some damage is caused to the ship due to the fault of the charterer, then the charterer is held responsible. This policy provides cover against such a loss.
10. **War Risks:** The Government war risks scheme covers loss under policies like hull and machinery, reducing premium, freight, disbursement, in case of war and strikes. But this policy does not provide cover against policies like loss of hire, etc.

Cargo Insurance

Cargo insurance is codified under the Institute of Cargo Clauses (A), (B) and (C). Under each of the three clauses the provisions are categorised as follows:

Risks Covered

Risks covered under the three Institute Cargo Clauses (ICC) are different.

Risk Clause

This clause lists the different types of risks covered by ICC (A), (B) and (C).

ICC (A) –

- This clause provides cover for all perils, which are capable of causing loss or damage to the insured subject, and excludes perils that are not specified in the policy.
- It covers the general average charges and salvage charges caused as a result of perils included in the policy only.
- It also provides cover to the assured in case of a collision, where both the ships are to be blamed.

ICC (B) and ICC (C) –

- The risks covered under these two clauses are enumerated below.

- Fire – This clause states that any damage caused as a result of a fire or an explosion (heating, smoke, etc.), including damage caused while extinguishing the fire are covered by insurance. However, this does not apply to a situation where the fire is caused due to a peril, which is excluded (not covered under the insurance). Cargo that is affected is also not covered.
- Covers a ship that is sunk or stranded or capsized.
- Loss caused due to land conveyance.
- Collision with another vessel or with any other object from land or air – this does not cover loss caused due to movement of goods in the ship due to turbulent weather. Likewise, it does not cover damage caused to goods due to jolting, while being transported by rail or road.
- Disposal of cargo at a port of distress
- General average loss
- Jettison – This states that jettison (to throw property overboard) done with the intention of countering an imminent danger can be classified as a general average sacrifice. But in a situation like this if the cargo and the ship belong to different owners then a claim for general average sacrifice can be put up. Whereas, if the ship and the cargo belong to the same owner then there is only one interest involved, so it does not qualify as general average sacrifice, the loss is however covered under the policy.

The loss and damage caused due to the above mentioned is provided cover under both ICC (B), and ICC (C). But apart from the listed risks ICC (B) provides cover against some other risks They are:

- Lightning, earthquakes, loss caused due to volcanic activity.
- Washing overboard - It has to be proved beyond doubt that the cargo was washed overboard and not lost overboard to claim after such a loss.
- Loss caused due to incursion of water (sea, river or lake) into the vessel that may damage engine, cargo, storage, etc.
- It also covers the loss incurred when a package is lost or is damaged in the loading and unloading process – this is also called sling loss.

The difference between the ICC (A), (B) and (C) is that ICC (A) covers all risks except the ones specifically excluded from the policy. For cover under ICC (A), the assured has to show that loss of cargo was during the period for which the insurance cover was provided. If the insurer thinks otherwise then he has to prove that an excluded peril was involved in causing the loss.

On the other hand ICC (B) and (C) cover only specific risks. For cover under ICC (B) and (C), the assured has to prove that the loss was caused within the time frame of



the policy and that the loss was caused by a listed peril. Unless the insurers are able to prove otherwise, the assured is entitled cover.

The Risk Clauses listed in the three sets of the Institute of Cargo Clause are different and also, there are some differences in the General Exclusions Clauses. Other than this all the other clauses are the same.

General Average Clause (Clause 2)

- This says that the General Average and Salvage Charges are covered by insurance only if the loss is caused due to perils that are included in the policy.
- The assured has to make a contribution towards a common fund, in case of loss of goods due to average general sacrifice.
- The insurer is liable to cover the entire contribution of the assured in case of general average contribution. But the insurer is not liable to cover the contribution in case of under insurance.
- Salvage charges can be recovered under the policy.
- If a salvage award is given then the beneficiaries of such an award are to make a contribution for the same. But the contribution of each should be in proportion to the saved interest.
- The insurer is liable to salvage charges incurred by the assured. That is the insurer is liable to cover the contribution made by the assured towards such a contribution.

“Both to Blame Collision” Clause (Clause 3)

This states that the insurer is liable to cover loss incurred by the assured in case of a collision, as under the contract of affreightment.

Exclusions

These are the perils or risks that are excluded from a marine insurance policy, that is they are not provided insurance cover.

Statutory Exclusions: These are described under Section 55 of the Marine Insurance Act, 1963.

According to Section 55 (1) of the Act the insurer is liable for any loss caused only due to perils of the sea, which has been provided insurance cover. (2) According to this sub section the insurer is not liable for any loss incurred due to a malpractice by the assured, but the insurer is liable if the loss is proximately caused by a peril of the sea even if it could have been avoided by competency from the crew and the master. The sub section also excludes:

- Delay,
- Wear and tear,
- Leakage,
- Loss due to rats and vermin,
- Loss due to inherent vice of the insured subject matter,
- Damage to machinery not caused due to perils of the sea.

From insurance cover, unless the policy otherwise provides for it. It is pertinent to discuss statutory exclusions, before going into the other exclusion clauses embodied in the Institute Cargo Clauses. The different Exclusions under ICC are:

General Exclusions Clause (Clause 4) - *This is applicable to ICC (B) and (C)*

This clause enumerates the different types of loss/damage/expense that are excluded from a policy. Sub clauses dealing with the exclusions are as follows:

- 4.1 – Loss attributable to willful misconduct of the assured
- 4.2 – Ordinary leakage, breakage, wear and tear
- 4.3 – Loss due to improper or insufficient packing of the insured cargo
- 4.4 – Loss due to inherent vice of the subject matter: If goods are stored close to goods that possess an inherent vice that causes loss then it is covered by insurance.
- 4.5 – Loss caused due to delay, even if the delay is caused due to an insured peril of the sea. This however, does not apply to general average and salvage charges.
- 4.6 – Loss due to financial default on behalf of the owners, charterer's, etc.
- 4.7 – Willful destruction or damage of the insured subject matter by the act of a person or group.
- 4.8 – Loss due to weapons using nuclear fissile material.

Note: *Except Sub Clause 4.7 all the other sub clauses appear in the General Exclusion under ICC (A). This risk therefore is covered under "all risks" of ICC (A).*

Unseaworthiness and Unfitness exclusion clause(Clause 5): This states that there is an implied warranty as embodied in section 41 of the Marine Insurance Act, 1963 that the ship should be seaworthy at the beginning of each stage of the voyage.

War Exclusion Clause (Clause 6): It states that insurance will not provide cover for loss or damage caused as a result of:

- 6.1 – "war, civil war, rebellion, insurrection or civil strife arising there from, or any hostile act by or against a belligerent power".
- 6.2 – "capture, seizure, arrest, restraint or detainment, and the consequences thereof or any attempt thereat".



6.3 – “derelict mines, torpedoes, bombs, or other derelict weapons of war”

Note: *The above-mentioned clauses are as under ICC (B) and (C). There is one difference with respect to ICC (A) - In sub clause 6.2, piracies are also excluded.*

Strikes Exclusion Clause (Clause 7): This is common to all the three sets of cargo clauses. This clause excludes loss, damage or expenses caused due to strikes, riots, etc from insurance cover.

7.1 – It excludes loss caused by strikes, civil commotion, riots, union uprisings, etc.

7.2 – It excludes loss resulting from strikes, civil commotion, riots, union uprisings, etc.

7.3 – It excludes loss caused by terrorist activity or by disturbances backed by political motivation.

Duration

The period for which the insurance policy lasts is covered by the following clauses:

Transit Clause (clause 8) - This states that the insurance cover is provided for the goods from the time they leave the warehouse or other place of storage or as mentioned in the policy to embark on the voyage, till it is eventually delivered at the destination. The insurance policy expires:

- Once the goods are delivered at the warehouse or storage facility at the destination port as mentioned in the policy;
- On arrival at an intermediary warehouse or storage facility at the will of the assured for storage or distribution; and
- 60 days from the date of discharge of the cargo at the destination port.

If the goods are transported from the destination to another place before the end of the policy, then the cover would last only till the commencement of transit to the next destination.

In accordance to the above clause the insurance cover exists in case of:

- Delay – if the delay is not within the control of the assured then the insurance cover is provided. But, at the same time there is no coverage for damage caused due to delay, even if it is by an insured peril.
- Reshipment and Transshipment – Insurance covers these if mentioned in the contract of affreightment.
- Discharge of goods.
- Deviation – Although the marine insurance clause exempts the insurer from liability in case of a deviation, ICC extends the insurance cover without the need for payment of extra premium or intimation.

Termination of Contract of Carriage (Clause 9): If due to some unforeseen reason the voyage is terminated or if the contract of carriage is terminated at some port other than the destination port then the insurance policy also terminates simultaneously. But if the assured needs cover, then he has to intimate the insurer and ask for continuation.

But the intimation has to be on time and an extra premium has to be paid. Then the insurance cover would continue till the cargo is sold or delivered at any intermediary port, or after 60 days of arrival at any such place or port. The insurer is liable only if the termination is due to an insured peril of the sea.

Change of Voyage Clause (Clause 10): According to the Marine Insurance Act, if the destination of the ship is voluntarily changed, then it is termed as change of voyage. The act also exempts the insurer from any form of liability in case of a change of destination, unless it is mentioned in the policy.

But clause 10 of ICC states that the change in voyage is covered, at a premium and conditions decided on by the insurer on prompt intimation.

Inland Transit Clauses: Manufacturers require transit insurance for the raw materials purchased by them and finished goods supplied to their customers. An open policy is issued to cover a number of incoming and outgoing consignments automatically.

For regular exporters and importers, continuous and automatic insurance protection is afforded by open cover. Open policy is an ordinary cargo policy expressed in general terms and the sum insured is affected for an amount sufficient to cover a number of dispatches. The sum insured is adjusted against each sending and so it is called a floating policy.

The movement of cargo within the country is known as Inland Transit. The inland transit of the cargo may be Rail or Road or Inland water ways and Coastal Shipments. Sometimes sending cargo by Air or Post is also likely.

Inland Transit Rail / Road Clauses: These clauses are attached to policies covering transit by Rail/Road. There are three types of clauses viz.

Inland Transit Rail / Road Clause “C”: This clause covers the perils of Fire and Lightning

Inland Transit Rail / Road Clause “B”: This clause covers the perils of:

- Fire
- Lightning
- Breakage of bridges
- Collision with or by the carrying vehicle
- Overturning of the carrying vehicle
- Derailments or accidents of like nature to the carrying railway wagon / vehicle



INLAND TRANSIT RAIL / ROAD CLAUSE “A”: This clause covers All risks of Loss or damage to the subject matter insured except the excluded risks mentioned below:

COMMON EXCLUSIONS UNDER CLAUSE A/B/C:

- Wilful Misconduct
- Ordinary Leakage/ breakage/ shortage etc. i.e. Ullage Losses
- Insufficiency/ unsuitability of packing
- Delay
- Inherent Vice
- War and allied perils
- Strike, Riot, Civil Commotion & Terrorism (SRCC)*

**Note: SRCC risks can be covered by payment of extra premium.*

COMMON EXCLUSIONS UNDER CLAUSE “B” & “C”: In addition to exclusions 1 to 7 mentioned above, Malicious Damage is also excluded. However, this can be covered by payment of extra premium.

Extention of Cover

● **Under Inland Clause ‘B’/ ICC ‘B’**

Sometimes instead of availing All Risks policy i.e. as per Inland clause ‘A’ for inland transit and Institute Cargo Clause “A” for imports and exports, the insured can take cover a per Clause “B” and extend the same to include various extraneous perils, subject to payment of additional premium. Examples of such perils include:

- Theft, Pilferage, and Non-delivery
- Fresh/rain water damage
- Damage by Hook/ oil/ mud/ acid
- Damage/Leakage (not ordinary leakage)
- Country damage (Cotton)
- Shortage
- Bursting and Tearing of bags
- S.R.C.C Risk

Inland policies ‘A’, ‘B’, ‘C’ can be extended to include SRCC risk subject to SRCC Clause.

- (a) War and SRCC risks: Ocean policies can be extended to include War & SRCC risks with additional premium. Air transit policies can be also extended t include was and SRCC with additional premiums.

Claims

Claim is made in case of loss or damage as specified in a marine insurance contract. But before a claim can come through several queries have to be answered that will validate the claim. These are:

- The proximate cause of the loss or damage;
- Is the cause of the damage or loss an insured peril in the marine contract?
- Finally, what amount of indemnity is payable, with respect to the above?

As soon as the loss is incurred the claimant should intimate the insurer. The available details should be recorded to avoid discrepancies, while passing the claim. When a claim is intimated, the insurer needs to verify certain facts, like:

- If there is a delay in intimation of the claim,
- If valid insurance documents are presented;
- Whether timely payments of premium have been made;
- Whether the loss occurred during the period for which insurance cover was provided.

Procedure

Cargo claims procedures are classified into three:

1) If the insured cargo has suffered loss or damage, when it arrives at the destination port. In such a situation the assured or the consignee has to inform the following:

- a) The insurer – this is done so that the insurer can appoint a surveyor to
- Find out the nature and cause of the damage or loss incurred; and
 - Establish the extent of loss.

(Even unloading survey is arranged in many cases and such survey can establish validity of possible claims.)

This intimation is necessary, as transit cover ceases as soon as the cargo is delivered to the consignee. Thus any loss caused after delivery is not provided cover.

- b) The Representative of the Carrier – This is to enable the consignee to charge the carrier for loss or damage done to the goods.

c) If necessary the Port Authority.

2) If the insured goods have been delivered at an intermediate port – This happens if the carrier has abandoned the voyage, or if the goods are so badly damaged that the transit becomes unnecessary. Under such circumstances the insurance



cover is terminated, even if the situation is beyond the control of the assured. So, the assured has to notify the insurer, and request for continuation of the cover.

- 3) When the insured goods arrive at the destination port, but the loss incurred is due to a General Average – In such a situation the consignee is duly informed by the representative of the carrier, when the consignee presents the bill of lading or other papers entitling him to delivery. The consignee may then be asked to produce General Average Security by means of an Average Bond and an additional security by means of a cash deposit (a percentage of the value of the goods); Bank Guarantee; or Insurer's Guarantee.

In case of a General Average loss, the General Average Adjuster has to be informed so that he can –

- Check whether the loss was incurred due to General Average causes;
- Make appropriate reductions in the contributions in case some amount of damage is caused during the voyage.

(In all marine claims, there is a concept of recovery from the carrier. The claimant should protect the recovery rights of the insurer. Otherwise, the claim will be prejudiced and it may become a non-standard claim where not more than 75% of the admissible claim is paid. The legal procedures to be followed by the insured to protect the recovery rights are prescribed in the respective acts such as railways act, carriers act, carriage of goods by air act, etc. The most important documents are letter of subrogation and special power of attorney to be executed and notarised to be submitted to the insurer before receiving the claims payment).

Exchange control regulations

1. Direct Insurance outside India by residents – Residents of India are not permitted to acquire insurance protection from Insurance companies in foreign countries without prior permission from the Government of India and the Reserve Bank of India in compliance with the General Insurance Business (Nationalisation) Act, 1972.
2. Currencies in which the marine policy can be issued – coastal shipment policies can be issued only in the Indian Currency. Policies on consignments between India and foreign countries can be issued in Indian currency or in that of the foreign country.
3. If a marine claim is payable in India, to either a person or a firm then the amount has to be paid in rupees. If the claimant is abroad then the settlement can be made in a foreign currency. But if the amount is too high then payment can be made by remittance from India, though it requires the sanction of the Reserve Bank of India.

4. Remittance of export claims – Remittance in foreign currency is only possible, if the insurer is able to prove that the person holding insurable interests is a non-resident.
5. Remittance of Import claims – The preferred practice is to settle the claims of the importer in the local currency, but foreign currency settlements are allowed to pay the overseas suppliers, so that goods can be replaced in case of damage. The situation under which such a settlement is allowed is when the import is by the government or a public sector enterprise; and when imports are made against foreign credits by a public sector enterprise.

Customs clearance

For acquiring immediate clearance from customs, documents relating to the shipment should be filed 15 days prior to the arrival of the cargo. For clearance, the importer has to submit an Import Bill of Entry, in addition to an invoice, weight specification, packing list, insurance policy, Bill of lading, and an Import license valid for the goods being imported, etc.

MOTOR INSURANCE

Motor insurance being a contract like any other contract has to fulfil the requirements of a valid contract as laid down in the Indian Contract Act 1872. In addition it has certain special features common to other insurance contracts.

Motor Vehicle Act, 1939

Motor Vehicles Act in 1939 was passed to mainly safeguard the interests of pedestrians. The current act is MV Act 1988.

According to the Act, a vehicle cannot be used in a public place without insuring the third party liability.

Need for Third Party Insurance

No insurer can deny TP cover to any owner of a motor vehicle (Section 146 of MV Act 1988). According to Section 24 of Motor Vehicles Act “no person shall use or allow any other person to use, a motor vehicle in a public place, unless the vehicle is covered by a policy of insurance.”

Compulsory insurance in respect of motor vehicles comprises the following liabilities:

- Liability arising out of bodily injury or death of the third party or arising out of the damage to his property.
- Compulsory insurance of passengers carried on hired vehicles.
- Compulsory insurance of passengers carried by reason of a contract of employment.



- Compulsory insurance of an employee under workmen's compensation act considering the factors such as:
 - Who was driving the vehicle?
 - Whether working as conductor or ticket examiner/coolies
 - Nature of goods carried in the goods carriage

Exceptions

Both the central and state/local body government owned vehicles (public transport corporations also) do not fall under compulsory insurance.

However for the exemption to be effective the concerned government authority must pass an order for such exemption only with a fund established by the concerned government debt/corporate to meet the liabilities arising out of the use of the vehicles.

Limitations of liability (Liability to TP injury / death is unlimited. This is a major change brought in by MV Act 1988 and that is why IRDA has brought in pool arrangement to manage TP portfolio).

Liability coverage is limited to any one accident. The limitations are:

Liability coverage of goods vehicle under workmen's compensation is as per WC Act. Only upto Rs. 1,00,000 and passengers are limited to less than six. This limit is over and above the coverage available to the driver.

Liability coverage limit is upto Rs.15, 000 in case of a hired passenger vehicle. The passengers here also include passengers under contract of employment.

Liability coverage of any vehicle other than the mentioned above is limited to the rupee value of actual liability.

Liability coverage in case of any damage to the property of third party is upto Rs. 6,000.

Commencement

The policy comes into effect from the issuance of certificate of insurance to the proposer or the insured.

Termination

The insurance policy is subject to termination before the policy period comes to end. Accordingly, the insured is required to submit the certificate to insurer within 7 days after termination. And the insurer may withdraw or suspend by notifying the registration authority within 7 days of action. An affidavit should be produced in case of loss of certificate as evidence.

No TP cover can be terminated by any party without proof of existence of another insurance. RTO has to be intimated in such cases and insurance certificate to be called back and cancelled.

Certificate of insurance and cover note

'Certificate of insurance' according to sec.145 (b) refers to a certificate issued by an authorised insurer in pursuance of section 147(3); it also includes a cover note complying with the prescribed requirements.

Under rule 141 of Central Motor Vehicles Rules, 1989 an authorised insurer issues a certificate of insurance to every holder of insurance policy in form – 51 in respect of every vehicle.

The cover note contains the following details:

- The registration mark, Engine no. & Chassis no., Model, Make, etc. and the number of description of the vehicle
- Name and address of the insured
- Date and time of the commencement of the policy
- Date of expiry of insurance
- Persons entitled to drive
- Limitations regarding the usage of the vehicle
- The validity period of the cover note.

Transfer of ownership

In case of any sale of vehicle involving transfer of policy, the insured should apply to the insurer for consent to such transfer. The transfer is allowed, if within 15 days of receipt of application the insurer does not reject the plea. The insurer has to be approached and new certificate of insurance to be issued in the name of the buyer of the vehicle by charging transfer fees.

The transfer is normally allowed but can also be refused in the following cases (However, non transfer of insurance does not affect TP liability cover under the policy)

- Due to the previous record of the transferee driver and policyholder
- Due to a stated condition in the policy providing prohibiting transfer
- Due to rejection of any prior proposal for transfer from the person seeking transfer in his name

The insurers liability towards the insured comes to an end as soon as the old certificate is repudiated. However as per the Act the insurer is liable to third party. The insurer is liable to the new owner for Own Damage Claims (OD claim) only after a fresh proposal form is filled in and the old certificate is cancelled.



Insurer's Duty to Third Party

It is obligatory on the part of the insurer to pay the third party since, the insurer has no rights to avoid or reject the payment of liability to a third party.

The duties of the insurer towards a third party are provided in section (149 of MV Act, 1988) 96 (1). The third party liability is determined by the court and accordingly compensation is paid. The liability is unlimited. It is the right of the insurer to receive the notice of the case proceedings.

Insurer's Rights (section 149(2))

An insurer to whom notice of the bringing of any such proceedings is so given shall be entitled to be made a party thereto and to defend the action on any of the following grounds, namely:-

- (A) that there has been a breach of a specified condition of the policy, being one of the following conditions, namely:-
 - (i) a condition excluding the use of the vehicle-
 - (a) for hire or reward, where the vehicle is on the date of the contract of insurance a vehicle not covered by a permit to ply for hire or reward, or
 - (b) for organised racing and speed testing, or
 - (c) for a purpose not allowed by the permit under which the vehicle is used, where the vehicle is a transport vehicle, or
 - (d) without side-car being attached where the vehicle is a motor cycle; or
 - (ii) a condition excluding driving by a named person or persons or by any person who is not duly licensed, or by any person who has been disqualified for holding or obtaining a driving licence during the period of disqualification; or
 - (iii) a condition excluding liability for injury caused or contributed to by conditions of war, civil war, riot or civil commotion; or
- (B) that the policy is void on the ground that it was obtained by the nondisclosure of a material fact or by a representation of fact which was false in some material particular.

Exception

Due to the wrong usage of vehicle by the insured the insurers cannot escape the liability towards third party. But the insurer can recover the sum paid from the insured.

Rights of Third Parties

When Insured is insolvent

According to Section (section 150 07 MV ACT 1988) 97 in case of an insolvent insured the rights are automatically transferred to the third party. Similarly, the insurer accepts the liabilities of third party.

When Insured is insolvent

- (1) Where under any contract of insurance effected in accordance with the provisions of this Chapter, a person is insured against liabilities which he may incur to third parties, then—
 - (a) in the event of the person becoming insolvent or making a composition or arrangement with his creditors, or
 - (b) where the insured person is a company, in the event of a winding-up order being made or a resolution for a voluntary winding-up being passed with respect to the company or a receiver or manager of the company's business or undertaking being duly appointed, or/of possession being taken by or on behalf of the holders of any debentures secured by a floating charge of any property comprised in or subject to the charge, if, either before or after that event, any such liability is incurred by the insured person, his rights against the insurer under the contract in respect of the liability shall, notwithstanding anything to the contrary in any provision of law, be transferred to and vest in the third party to whom the liability was so incurred.
- (2) Where an order for the administration of the estate of a deceased debtor is made according to the law of insolvency, then, if any debt provable in insolvency is owing by the deceased in respect of a liability to a third party against which he was insured under a contract of insurance in accordance with the provisions of this Chapter, the deceased debtor's rights against the insurer in respect of that liability shall, notwithstanding anything to the contrary in any provision of law, be transferred to and vest in the person to whom the debt is owing.
- (3) Any condition in a policy issued for the purposes of this Chapter purporting either directly or indirectly to avoid the policy or to alter the rights of the parties thereunder upon the happening to the insured person of any of the events specified in clause (a) or clause (b) of sub-section (1) or upon the making of an order for the administration of the estate of a deceased debtor according to the law of insolvency shall be of no effect.
- (4) Upon a transfer under sub-section (1) or sub-section (2), the insurer shall be under the same liability to the third party as he would have been to the insured person, but –



- (a) if the liability of the insurer to the insured person exceeds the liability of the insured person to the third party, nothing in this Chapter shall affect the rights of the insured person against the insurer in respect of the excess, and
- (b) if the liability of the insurer to the insured person is less than the liability of the insured person to the third party, nothing in this Chapter shall affect the rights of the third party against the insured person in respect of the balance.

The two possibilities in this case are:

- If the insured's liability to third party may exceed unlike under the policy in such a case the insurer bears upto the liability agreed upon and the balance is payable by the insured.
- If in case the insured's liability to a third party is less than the one agreed upon between the insurers and insured the third party's rights are not affected. Therefore, the balance is paid by insured.
- According to Section 102 the third parties claim can be met in case of the insured's death from his estate i.e. from his legal heir or insurer. Further the representative of the insured is indemnified by company as per the policy.
- Any settlement of claims between insurer and insured is considered invalid if the third party's rights are diminished. Therefore, in case of decree against the insured by third party he will be compensated by the insurer directly
- According to Section 98, it is a duty of every person incurring third party liability to disclose the particulars related to insurance. The third party also has the right to get the details from insured and may also examine the policy along with other documents of insurer
- According to Section 109 all the particulars regarding identification marks, name and address of the user at the time of accident must be disclosed by the registration authority or the officer in charge, which is essential for the insured and the third party.

The motor tariff in India has been revised from time with the latest revision, taking place with effect from 1st July, 2002. This tariff supersedes all earlier tariffs and it lays down that the policies insuring motor vehicles are to be issued only as per the standard form(s) given in Sec.6 of the tariff. Now motor OD is detariffed and only motor TP premiums are administered by IRDA.

Types of Motor Policies

There are two types of policies:-

1. **Liability only policy** – This covers third party liability and/or death and property damage. Compulsory personal accident cover for the owner in respect of owner driven vehicles is also included.

2. **Package policy** – This covers loss or damage (OD or Own Damage) to the vehicle insured in addition to 1 above.

The insurance company covers the Motor Car and/or its accessories for the following perils:

- I. Fire, explosion, self ignition or lightning
- II. Burglary, house-breaking or theft
- III. Riot and Strike
- IV. Earthquake (Fire and Shock damage)
- V. Storm, Tempest, Flood, Inundation, Typhoon, Hurricane, Cyclone, Hailstorm, Frost
- VI. Accidental External Means
- VII. Malicious Act
- VIII. Terrorist Activity
- IX. Whilst in transit by road, inland waterway, lift elevator or air
- X. Landslide/Rockslide

(A motor policy is an All Risk cover with named exclusions only. Anything not specifically excluded in the policy are covered).

Subject to a deduction for depreciation at the rates mentioned in the schedule for parts replaced:

1. For all rubber, nylon, plastic parts, tyres and tubes, battery and air bags – 50%
 2. For Fibre glass components – 30%
 3. For all parts made of glass – NIL
- (all these can vary from insurer to insurer)

Exclusions

The company will not be liable to make payment in respect of

- Consequential loss, depreciation, wear and tear, mechanical and electrical breakdown, failures or breakages
- Damage to tyres and tubes (normally 50% is allowed if proved that the damage is only due to the mishap)
- Any accidental loss or damage suffered whilst the insured or any person driving with the knowledge and consent of the insured is under the influence of intoxicating liquor or drugs. (for that matter breach of any warranty which has a bearing on the mishap will invalidate the claim).



Proposal Form

A proposal form is to be collected from the insured at the time of the inception of risk for the first time.

Rating

Rates provided under this Tariff only for Third Party premiums, the rates are administered by IRDA. For Own Damage cover, Tariff has been abolished. Hence, each Insurance Company can have its own rates. Loading on tariff premium rates upto 100% may be applied for adverse claims experience of the vehicle insured and individual risk perception as per the insurer's assessment. If the experience continues to be adverse, a further loading upto 100% on the expiring premium may be applied. No further loading shall apply.

Extension of Geographical Area: The Geographical Area of Motor Policies may be extended to include Nepal and Bhutan.

This can be done by charging a flat additional premium of Rs.500 per vehicle / 100 per vehicle irrespective of the class of vehicle for package policy and liability policy respectively.

Such geographical extensions, however, specifically exclude cover for damage to the vehicle/ injury to its occupants/ TP liability in respect of the vehicle during air passage/ sea voyage for the purpose of ferrying the vehicle to the extended Geographical Area.

Valued Policies

Under an Agreed Value Policy a specified sum agreed as the insured value of the vehicle is paid as compensation in case of Total Loss/Constructive Total Loss of the vehicle without any deduction for depreciation.

The motor tariff permits the issue of such policies only for vintage cars. A Vintage car is any car manufactured prior 31/12/1940 and duly certified by The Vintage and Classic Car Club of India.

The **Insured's Declared Value (IDV)** of the vehicle will be deemed to be the 'SUM INSURED' for the purpose of this tariff and it will be fixed at the commencement of each policy period for each insured vehicle.

The IDV of the vehicle is to be fixed on the basis of manufacturer's listed selling price of the brand and model as the vehicle proposed for insurance at the commencement of insurance/renewal and adjusted for depreciation (as per schedule specified below).

AGE OF THE VEHICLE	% OF DEPRECIATION FOR FIXING IDV
Not exceeding 6 months	5%
Exceeding 6 months but not exceeding 1 year	15%
Exceeding 1 year but not exceeding 2 years	20%
Exceeding 2 years but not exceeding 3 years	30%
Exceeding 3 years but not exceeding 4 years	40%
Exceeding 4 years but not exceeding 5 years	50%

Note: IDV of vehicles beyond 5 years of age and of obsolete models of the vehicles (i.e. models which the manufacturers have discontinued to manufacture) is to be determined on the basis of an understanding between the insurer and the insured.

Total loss – A vehicle is considered as a constructive total loss where the aggregate cost of repairs exceeds 75% of IDV.

Geographical Zones

For the purpose of rating, the whole of India has been divided into the following zones depending upon the location of the office of registration of the vehicle concerned.

- (i) Private Cars/ Motorized Two Wheelers/ Commercial Vehicles rateable under Section 4.C.1 and C.4.

Zone A: Ahmedabad, Bangalore, Chennai, Hyderabad, Kolkata, Mumbai, New Delhi and Pune.

Zone B: Rest of India

- (ii) Commercial Vehicles excluding vehicles rateable under Section 4. C.1 and C.4.

Zone A: Chennai, Delhi / New Delhi, Kolkata, Mumbai

Zone B: All other State Capitals

Zone C: Rest of India

Period of Insurance – This is generally for one year and can be extended for a few months, if such extension is required for a specific purpose. Premium payable will be on a prorata basis provided the extended policy on expiry is renewed for a further period of twelve months.

Premium Rates for Short Period Cover

Short Period Cover/Renewal may be granted for periods less than twelve months at the following short period scale:



SHORT PERIOD SCALE

PERIOD	% OF ANNUAL PREMIUM RATE
Not exceeding 1 month	20%
Exceeding 1 month but not exceeding 2 months	30%
Exceeding 2 months but not exceeding 3 months	40%
Exceeding 3 months but not exceeding 4 months	50%
Exceeding 4 months but not exceeding 5 months	60%
Exceeding 5 months but not exceeding 6 months	70%
Exceeding 6 months but not exceeding 7 months	80%
Exceeding 7 months but not exceeding 8 months	90%
Exceeding 8 months	Full annual premium/ rate

N.B.: 1. Extension of short period covers/short period renewals, for any reason, can be granted only by charging the premium for such extensions at the above mentioned short period rates.

N.B.: 2. Short period covers/short period renewals for Liability Only Policies are not permissible.

Premium computation along with discounts allowed is to be shown clearly on the policy.

Payment of Premium

The full premium is required to be collected before commencement of cover. It is not permissible to collect premium in installments.

Minimum Premium

The minimum premium applicable for vehicles specially designed or modified for use of the blind, handicapped and mentally challenged persons will be Rs.25/- per vehicle. For all other vehicles, the applicable minimum premium per vehicle will be Rs.100/-.

Transfers

On transfer of ownership, the Liability Only cover, either under a Liability Only policy or under a Package policy, is deemed to have been transferred in favour of the person to whom the motor vehicle is transferred with effect from the date of transfer.

The transferee shall apply within fourteen days from the date of transfer in writing under recorded delivery to the insurer who has insured the vehicle, with the details of

the registration of the vehicle, the date of transfer of the vehicle, the previous owner of the vehicle and the number and date of the insurance policy so that the insurer may make the necessary changes in his record and issue fresh Certificate of Insurance.

In case of Package Policies, transfer of the "Own Damage" section of the policy in favour of the transferee, shall be made by the insurer only on receipt of a specific request from the transferee along with consent of the transferor. If the transferee is not entitled to the benefit of the No Claim Bonus (NCB) shown on the policy, or is entitled to a lesser percentage of NCB than that existing in the policy, recovery of the difference between the transferee's entitlement, if any, and that shown on the policy shall be made before effecting the transfer.

A fresh Proposal Form duly completed is to be obtained from the transferee in respect of both Liability Only and Package Policies.

Transfer of Package Policy in the name of the transferee can be done only on getting acceptable evidence of sale and a fresh proposal form duly filled and signed. The old Certificate of Insurance for the vehicle, is required to be surrendered and a fee of Rs.50/- is to be collected for issue of fresh Certificate in the name of the transferee. If for any reason, the old Certificate of Insurance cannot be surrendered, a proper declaration to that effect is to be taken from the transferee before a new Certificate of Insurance is issued.

Change of Vehicle

A vehicle insured under a policy can be substituted by another vehicle of the same class for the balance period of the policy subject to adjustment of premium, if any, on pro-rata basis from the date of substitution.

Where the vehicle so substituted is not a total loss, evidence in support of continuation of insurance on the substituted vehicle is required to be submitted to the insurer before such substitution can be carried out.

Vehicles subject to hire purchase agreements, vehicles subject to lease agreements and vehicles subject to hypothecation: Motor policies are not issued in joint names. The financial interests are only recorded by attaching/ invoking the respective endorsement nos. in the name of the financier – Hire Purchase/ Hypothecation/ etc.

Cancellation of Insurance and Double Insurance

A. Cancellation of Insurance

- (a) A policy may be cancelled by the insurer by sending to the insured seven days notice of cancellation by recorded delivery to the insured's last known address and the insurer will refund to the insured the pro-rata premium for the balance period of the policy.



- (b) A policy may be cancelled at the option of the insured with seven days notice of cancellation and the insurer will be entitled to retain premium on short period scale of rates for the period for which the cover has been in existence prior to the cancellation of the policy. The balance premium, if any, will be refundable to the insured. Refund of premium will be subject to:
 - i) there being no claim under the policy, and
 - ii) the retention of minimum premium as specified in the Tariff.
- (c) A policy can be cancelled only after ensuring that the vehicle is insured elsewhere, at least for Liability Only cover and after surrender of the original Certificate of Insurance for cancellation.
- (d) Insurer should inform the Regional Transport Authority (RTA) concerned by recorded delivery about such cancellation of insurance.

B. Double Insurance

When two policies are in existence on the same vehicle with identical cover, one of the policies may be cancelled. Where one of the policies commences at a date later than the other policy, the policy commencing later is to be cancelled by the insurer concerned.

If a vehicle is insured at any time with two different offices of the same insurer, 100% refund of premium of one policy may be allowed by canceling the later of the two policies. However, if the two policies are issued by two different insurers, the policy commencing later is to be cancelled by the insurer concerned and pro-rata refund of premium thereon is to be allowed.

If however, due to requirements of Banks/Financial Institutions, intimated to the insurer in writing, the earlier dated policy is required to be cancelled, then refund of premium is to be allowed after retaining premium at short period scale for the period the policy was in force prior to cancellation.

In all such eventualities, the minimum premium as specified in the tariff is to be retained.

In either case, no refund of premium can be allowed for such cancellation if any claim has arisen on either of the policies during the period when both the policies were in operation, but prior to cancellation of one of the policies.

Cancellation and issuance of fresh Certificate of Insurance

Following any changes in the policy during its currency, affecting the information shown on the Certificate of Insurance, the Certificate of Insurance is required to be returned to the Insurer for cancellation and a fresh Certificate incorporating the changes is to be issued.

Information regarding change of number of Engine and/ or Chassis of the vehicle, is required to be intimated to the insurer immediately for effecting necessary changes in the policy, provided such changes are duly endorsed on the Registration Certificate. The Certificate of Insurance is also required to be returned immediately for issuance of fresh Certificate of Insurance incorporating the changes.

Remittance of Rs. 50/- is required to be made to the insurer for each issuance of fresh Certificate of Insurance.

Classification of Motor Vehicles

As per the Motor Vehicles Act for the purpose of insurance the vehicles are classified into three broad categories such as.

- Private cars
- Motor cycles
- Commercial vehicles

Private vehicles

- a) Private Cars – vehicles used only for social, domestic and pleasure purposes
- b) Private vehicles – Two wheelers
 - 1) Motorcycles/Scooters
 - 2) Auto cycles
 - 3) Mechanically assisted pedal cycles

(C) Commercial vehicles

- Goods Carrying vehicles
- Trailers
- Vehicles used for carrying passengers on hire or reward
- Miscellaneous & Special types of vehicles
- Tariff for motor trade risks – load transit risks
- Tariff for motor trade – road risk
- Tariff for motor trade – internal risks

The tariff provides for 48 general regulations.



Liability only policy

According to the new Section 147(1) the liabilities incurred by the user of the motor vehicle should be covered by insurance in order to satisfy the requirements of chapter XI of the 1988 Act. These liabilities are also referred as Compulsory insurable risks.

According to chapter XI of 1988 Act, it is necessary for a motor vehicle to be insured against user's liability for death or bodily injury to third party. The policy amount is fixed by the Act.

Illustration:

A motorist while parking his vehicle unintentionally hit the compound wall resulting in third party liability.

Liability only policy

This policy covers the risks mentioned in the Motor Vehicles Act. This policy provides coverage even if the value of the property is high. It means the compensation provided by the insurer may be upto the value of insurance, which could be higher than the minimum amount, prescribed under the Act. This policy normally covers risks under Fatal Accident Act 1855, and common law.

Package policy

This policy covers all the risks under liability only policy and includes compensation for the damage to the vehicle as well.

Policy Renewal

In case of policy renewal a notice of one month in advance before the date of expiry is issued by the insurers. The notice gives the details of premium payable for renewal. No claim bonus if earned is indicated. A claim may arise between the date of notice and the expiry of insurance. Premium renewal is subject to adjustment. The insured is informed of the change in the IDV of the car and about the revision of the sum insured of motorcar.

Renewal Receipt

This document is issued in lieu of policy at renewal (but new certificate is to be issued). The issue of receipt shows that insurer has received the renewal premium and has the policy renewed for further one year. A fresh policy has to be taken if the renewal is not under the same conditions as the old policy.

Claims

Claims arise when:

- The insured's vehicle is damaged or any loss incurred
- Any legal liability is incurred for death of or bodily injury or damage to the property of a third party caused due to the usage of insured vehicle.

Duties when claim arises

1. Insured's

When there is a claim in respect of a motor accident it is the duty of the insured to intimate the insurer about the accident as soon as possible. He must also furnish the information required by the insurer such as names and addresses of the witnesses of the accident etc.

- The insured should not make any admission of liability or promise of payment without the insurers consent
- The insured must attend the damaged vehicle and simultaneously take utmost care that the damages or losses are made good before usage of such a damaged vehicle
- Any repair to the damaged vehicle can be undertaken by the insured within the stated amount. But the repair charges must be immediately intimated to the insurer. The insurer can also check about the repairs carried out to satisfy himself that the cost of repair is reimbursable.

2. Insurers

It is the duty of the insurer to gather the relevant facts about the accident from the insured in order to indemnify the insured. The insurer through a form sent to insured collects the relevant information required. The insurer may gather information through other means if the information furnished is not complete.

Rights of the insurer when a claim arises

- The insurer may settle or defend the claim for his own benefit and the insured is required to cooperate and give the necessary information
- The insurer has the option to either repair, reinstate the vehicle or replace any of the parts or pay in cash the amount of loss or damage not exceeding the declared value or the value at the time of loss which-ever is less
- The insurer is entitled for subrogation and in case of double insurance he cannot contribute more than the rateable proportion of loss
- If the insurer disputed the amount of claim the matter should be arbitrated within 12 months.



Claims Settlement

Claims under motor insurance for own damage are settled in three phases:

- Preliminary scrutiny
- Assessment of loss
- Settlement

Preliminary Scrutiny

The preliminary scrutiny involves certain procedure such as:

- a)
 - (i) The insured gives a notice of loss to the insurer
 - (ii) The insurer checks whether the policy is in force
 - (iii) Checks whether the loss falls within the scope of policy
 - (iv) Checks whether the claim form is issued and surveyor is appointed.
- b) A detailed estimate of the repairs is to be submitted by the insured as prepared by the repairer. The surveyor inspects the damages and scrutinises the repairs estimate. The insurers normally accept such estimates prepared by the repairer but another estimate may be asked for especially.

Assessment of loss

The loss is assessed by the automobile surveyors assigned. They are given a copy of the policy, claim form and final repairer estimate. They inspect the damaged vehicle, discuss the cost of repair or replacement with the repairer and based on this the survey report is submitted.

A surveyor is not appointed in case of any minor damages. The survey (upto Rs.20,000) is handled by the engineers or the insurance officials themselves.

Settlement

Claims are settled on the basis of the survey report. The report is examined and accordingly the settlement is made. The practice followed is that the repairer gets a letter from the insurer and is paid only after the repairs are made. A voucher to this effect is given by the insured that he is satisfied with the repairs.

The insured can also make the payments for repairs direct by In such cases the insured is later reimbursed.

Claims settlement procedure in respect of third party claim.

In respect of a notice regarding a third party claim to the insurer the following steps are taken:

- Make an entry of notice received from (MACT) the third party regarding damages in claims register. (Normally for TP death / injury, claims are only through MACT whether out-of-court or Lok Adalat or after the award. For TP property damage, third party can also directly claim from insurer)
- Appointment of advocate by the company
- Send a letter to MACT for obtaining details of the claim
- Call for copy of panchnama report or accident and the police report
- Obtaining a copy of 'own damage' claim from the insured if there is one
- Obtain information regarding the liability of the insured
- Estimate the quantum of damages
- Obtain legal opinion in the case
- Motor accidents claims tribunal will decide the case if no settlement is worked by the parties by mutual agreement.

Claims payment

The payment of claim to the third party is based on the position relating to the following.

- No fault liability
- Law of negligence and nuisance (is the insured legally liable to the third party?)
- Motor Vehicles Act (is the insurer liable to indemnify the insured?).

Law of negligence and nuisance:

As per the terms of the policy the insurer has to indemnify the insured. If the insured's conduct is negligent or amounts to nuisance, he is liable to pay the third party. Negligence refers to breach of duty. Negligence arises when the driver:

- Indulges in dangerous and reckless driving without any concern for the safety of pedestrians
- Breaks traffic rules and regulations
- Is careless while driving
- Uses a defective vehicle

(These are not grounds for absolving the insurer of their liability)



Knock-for-Knock agreement

This is applicable to a situation where there is a collision involving two vehicles. The insurers of two parties involved in this case come to a settlement that there is no need to go into the question as to whose negligence caused the accident and agree to indemnify their respective insured's against loss. The subrogation right too is not exercised. On the contrary each insured is indemnified as per the policy conditions by the insurers. The benefits of this agreement being

- It avoids litigation
- Insured is benefited through a quick settlement
- Each insurer compensates his insured directly
- Insurers save on legal costs, which results ultimately on reduction in premium rates.

Motor Accidents Claims Tribunal

Motor Accident Tribunal was set up with the object of providing less expensive and quicker settlement of third party claims to the victims of motor vehicle accidents. The tribunal is a substitute of civil courts and has all the powers of a civil court for the purpose of taking evidence. The provisions relating to claims tribunal, procedure, awards, powers, compensation and appeals are contained in sections 169 to 176 of Motor Vehicles Act, 1988.

A motor tribunal is established in areas notified in the official gazette by the state government. These tribunals have no jurisdiction of civil courts.

The claims tribunal adjudicates upon claims preferred by injured parties for compensation in case of accidents causing bodily injury and loss or damage to third party due to the use of motor vehicle.

The provision has been omitted from the Motor Vehicles Act, 1988 stating that a victim in case of damage to the property exceeding Rs. 2,000 has the choice to go to a civil court and thereafter the tribunal will not have any jurisdiction.

The victim in case of compensation u/s 166 of the Motor Vehicles Act, 1988 has an option to either claim under Motor Vehicles Act or under Workmen's Compensation Act but not under both.

Procedure to file a claim in tribunal

An application for compensation can be filed in an MACT (Motor Accidents Claims Tribunal) any time after the accident without any time limit. The injured person can himself file an application or in case of a deceased person any of the legal representatives or any authorised agent of the victim can file the application.

If the injured or the deceased person has insurance for his vehicle, the insurer will be a party to the proceedings.

The tribunal is empowered to make an award for determining the compensation payable and mentioning the amount payable to the concerned person by the insurer or owner or driver of the offending vehicle.

In case of damages: The damages awarded by tribunal are of two types – special and general damages.

This distinction of damages helps the tribunal in determining whether the damages awarded are correct or invalid. The tribunal is also empowered to direct interest payments.

There can be no appeal in the tribunal if the amount awarded is less than Rs. 2000. But any other appeal to the tribunal should be made within 90 days (from the order copy is made ready by the tribunal). The High court can approve (delay condonation) the filing if the delay is supported with reasonable cause.

According to the provisions of section 173 of the Motor Vehicles Act, 1988 no appeal will be considered by the High court of a person who has to pay any amount in terms of award, unless the party liable for payment pays Rs. 25,000 or 50% of the amount awarded whichever is less.



IRDA RATES FOR MOTOR THIRD PARTY INSURANCE IN DE-TARIFF SCENARIO

Schedule of Premium Rates for Motor Third Party Liability Only Cover

(Effective from 1st January 2007 for fresh insurances and renewals of motor insurance policies)

		1	2
	Class of vehicle	Premium	
	Private Car		
	Cubic Capacity of the vehicle	(Rs)	
	Not exceeding 1000 cc	670	
	Exceeding 1000 cc but not exceeding 1500 cc	800	
	Exceeding 1500 cc	2500	
	Two Wheeler		
	Cubic Capacity of the vehicle		
	Not exceeding 75 cc	300	
	Exceeding 75 cc but not exceeding 150 cc	300	
	Exceeding 150 cc but not exceeding 350 cc	300	
	Exceeding 350 cc	620	
A1	Goods Carrying Vehicles- Public Carriers (other than 3 wheelers)		
	Gross Vehicle Weight (GVW)		
	Not exceeding 7500 Kg	5580	
	Exceeding 7500 Kgs but not exceeding 12000 Kgs	5920	
	Exceeding 12000 Kgs but not exceeding 20000 Kgs	6090	
	Exceeding 20000 Kgs but not exceeding 40000 Kgs	6260	
	Exceeding 40000 Kgs	6770	
A2	Goods Carrying Vehicles- Private Carriers (other than 3 wheelers)		
	Gross Vehicle Weight (GVW)		
	Not exceeding 7500 Kg	5000	
	Exceeding 7500 Kgs but not exceeding 12000 Kgs	5300	
	Exceeding 12000 Kgs but not exceeding 20000 Kgs	5440	
	Exceeding 20000 Kgs but not exceeding 40000 Kgs	5610	
	Exceeding 40000 Kgs	6050	

A3	Goods Carrying Motorized Three Wheelers and Motorized Pedal Cycles - Public Carriers	1530	
A4	Goods Carrying Motorized Three Wheelers and Motorized Pedal Cycles - Private Carriers	1450	
B	Trailers	Agricultural Tractors upto 6 HP	Other vehicles incl Miscellaneous & Special Type of vehicles (Class D)
		350	550
	For each trailer		
(For more than one trailer, please multiply by the number of trailers)			
C1a	Four wheeled vehicles used for carrying passengers for hire or reward with carrying capacity not exceeding 6 (six) passengers	Premium	Premium (Per licensed Passenger Capacity)
		(A)	(B)*
	Cubic Capacity of the vehicle		(Rs)
	Not exceeding 1000 cc	1650	350
	Exceeding 1000 cc but not exceeding 1500 cc	2330	350
	Exceeding 1500 cc	2840	350
<i>*TP Premium is the total of a basic amount (A) plus an amount derived by multiplying the licensed carrying capacity by an amount B</i>			
C2	Four or more wheeled vehicles with carrying capacity exceeding 6 passengers for hire or reward	3160	235
C1b	Three wheeled vehicles used for carrying passengers for hire or reward with carrying capacity not exceeding 6 (six) passengers	510	315
<i>*TP Premium is the total of a basic amount (A) plus an amount derived by multiplying the licensed carrying capacity by an amount B</i>			
C3	Motorized three wheeled passenger carrying vehicles for hire or reward with carrying capacity exceeding 6 but not exceeding 17 passengers	1560	315
<i>*TP Premium is the total of a basic amount (A) plus an amount derived by multiplying the licensed carrying capacity by an amount B</i>			
C2	Three wheelers with carrying capacity exceeding 17 passengers.	3160	235
<i>*TP Premium is the total of a basic amount (A) plus an amount derived by multiplying the licensed carrying capacity by an amount B</i>			



C4	Motorized Two Wheelers used for carrying passengers for hire or reward		
	Cubic Capacity of the vehicle		
	Not exceeding 75 cc	300	
	Exceeding 75 cc but not exceeding 150 cc	300	
	Exceeding 150 cc but not exceeding 350 cc	300	
	Exceeding 350 cc	680	
D	Special Types of Vehicles		
	i) Pedestrian controlled Agricultural Tractors with Horse Power rating not exceeding 6 HP; Hearses and Plane Loaders	400	
	ii) Other Misc & Spl types of vehicles	800	
E	Motor Trade (Road Transit Risk)		
	i) Distance not exceeding 2400 Kms	500	
	ii) Distance exceeding 2400 Kms	600	
F	Motor Trade (Road Risk) (Excluding Motorized Two Wheelers)	Premium	
	Named Driver or Trade Certificates		
	1st named driver or certificate	550	
	For additional Drivers/Certificates upto 5	265/- per Driver/ Certificate	
	For additional Drivers/Certificates exceeding 5 but not exceeding 10	175/- per Driver/ Certificate	
	For additional Drivers/Certificates exceeding 10 but not exceeding 15		
	Motor Trade (Road Risk) (For Motorized Two Wheelers)		
	Named Driver or Trade Certificates		
	1st named driver or certificate	300	
	For each additional Drivers/Certificate	150	

Questions



1. Define fire insurance. What are the characteristics of a fire insurance contract?
2. What is a standard policy? Are consequential losses covered by a standard policy?
3. What do you mean by fire and loss by fire? List the special perils of fire.
4. Why do insurers rarely exercise the reinstatement option? Elucidate.
5. What is the claim settlement procedure followed for a fire insurance policy?
6. What is meant by 'perils of the sea'? List any five perils that can be insured.
7. What is General Average Loss? Explain with an example.
8. Briefly describe the different types of losses.
9. Discuss general exclusions covered under ICC (A), (B), and (C).
10. Discuss how the needs for passing the 'Marine' Insurance Act, 1963 arise.
11. Is third party insurance a must under Motor Vehicles Act or is the Act only policy sufficient?
12. What is Knock-for-Knock agreement? List out the benefits of the agreement.
13. Discuss the role of MACT?

CHAPTER – 7

ENGINEERING INSURANCE

OUTLINE OF THE CHAPTER

- Introduction
- Storage-Cum-Erection Insurance Policy
- Contractors all risks Insurance Policy
- Contractor's Plant and Machinery Insurance Policy
- Boiler and Pressure Plant Insurance Policy
- Machinery Breakdown Insurance Policy
- Machinery Loss of Profits Insurance Policy
- Electronic Equipment Insurance Policy
- Advance Loss of Profits Insurance policy
- Questions

LEARNING OBJECTIVES

- To examine the loss exposures at the constructional phase as well as operational phase for the purpose of insurance
- To study the scope of engineering insurance policies as a risk mitigation tool for industrial loss exposures
- To understand the general conditions and exclusions applicable to engineering insurance policies

INTRODUCTION

Rapid industrialization has led to increasing use of machines in industry. The major thrust is now in the infrastructure development, which in turn is contributing to the socio-economic development. Infrastructure comprises projects ranging from

- Airports to bridges
- Dams to tunnels to off-shore structures
- Refineries to reservoirs
- Pipelines to power stations

- Factories to hospitals

All this involves huge capital, human resources, and technical expertise. However, these project assets are exposed to

- Physical losses involving accidental breakdown, repair, replacement, loss of production,
- Financial losses in terms of loss of incomes,
- Third – party liability affecting a number of parties such as owner, the financial institutions and the turnkey contractor.

Basically, General Insurance can be broadly divided into two categories –

- (1) Commercial Insurance and
- (2) Personal Insurance

Whilst the Personal Insurance takes care of the insurance requirements of the individual, the Commercial branch of insurance takes care of the needs of industrial and business houses – Examples of Commercial Insurance are, Fire Insurance covering Building, Plant & Machinery, Consequential loss insurance and the group of insurance schemes that come under the broad title 'Engineering Insurance'.

ORIGIN OF ENGINEERING INSURANCE (EI)

The origin of EI dates back to the early part of the Industrialization Revolution in the UK, where frequent explosions of steam boilers involved loss of life and property. In India the New India Assurance Company was the first company to introduce Engineering Department in the fifties followed by the Oriental Insurance Co. In the eastern region a syndicate of five companies, some British and some Indian, was formed to transact this class of business.

Engineering insurance also involves technical expertise in the areas of risk management with special focus on the issues like Risk inspection, Risk improvement, Rating and Underwriting.

Engineering Insurance schemes primarily aim at protecting business houses from eventualities that could give rise to a loss and disrupt their day-to-day functioning. Such losses arise due to the failure of machineries, explosion of boilers and breakdown of computers and sophisticated electronic equipment. A major breakdown due to mechanical failure could also result in consequential loss of profits. All these risks can be covered under various engineering policies.

In addition to the above, Engineering Insurance covers are available at the time of putting up of a factory or even during an expansion. These insurance covers are the Storage-cum-erection policies for industrial risks, the Contractors all risk policy for civil works and the Contractors plant & machinery policy, which takes of the Contractors



Insurance, requirements. The Advance loss of profits policy is a sophisticated insurance cover, which takes care of losses arising out of delay in completion of a project well beyond the stipulated period where the delay is caused by an insured peril.

ENGINEERING INSURANCE POLICIES

All Engineering insurance policies take into consideration all the risk exposures of industrial establishments and have suitable policies to cover these loss exposures at two stages, namely:

1. Construction Phase Insurance policies

- Contractors All Risk policy (CAR)
- Erection All Risks insurance policy (EAR) or (SCE)
- Marine- cum-Erection Insurance policy (MCE)
- Contract Works insurance policy (CW)
- Advance Loss of Profits policy (ALOP)
- Delay in start up insurance policy (DSU)

2. Operational Phase Insurance Policies

- Machinery insurance (MI)/ Machinery Breakdown insurance policy (MB)
- Boiler and Pressure Plant insurance policy (BPP)
- Machinery Loss of profits policy (MLOP)
- Contractor's Plant and Machinery insurance policy (CPM)
- Civil Engineering Completed Risks insurance policy(CECR)
- Electronic Equipment insurance policy (EEI)
- Deterioration of Stocks insurance policy (DOS)

While the construction phase policies are issued for the period of the project i.e. period or 'one time' policies, the operational insurance's are annual policies renewable at expiry

(Normally, one time policies of MCE / MCSCE are converted into annual policies of Fire insurance – P & M – after completion and commencement of the project)

All engineering policies provide cover on "All Risks" basis subject to general and special exclusions, if any loss is the result of

- Wilful negligence
- Cessation of work
- War and kindred perils and nuclear risks

1. Perils covered under construction phase include

The constructional phase insurance policies cover any loss or damage to property if caused due to the following perils namely,

- Fire, lightning, explosion
- Flood, inundation
- Windstorm of any kind
- Earthquake, landslide, subsidence etc.
- Theft and Burglary
- Accidental damage, bad workmanship, lack of skill, negligence, malicious damage or human error
- Collapse, impact damage
- Act of terrorism

Exclusions

However, no liability under the policy is covered in respect of:

- The amount of loss shown as excess
- Loss discovered at the time of inventory
- Normal wear and tear, rusting, etc.
- Cost of correction of any error during construction unless resulting in physical damage
- Files, drawings, currency, cheques
- Packing materials
- Penalties and fines
- Loss or damage due to faulty design
- Cost of repair or replacement of defective material or workmanship
- Vehicles licensed for general use, or waterborne vessels or equipment mounted on such vessels

Sum Insured and Period of cover under constructional phase

The sum insured required by the policy is to be equal to the Estimated Completed Erected Value of the contract works inclusive of landed cost of materials, wages, construction costs, freight, customs duties, and items supplied by the principal. The period of cover shall commence from the commencement of work or unloading of the property insured at site, whichever is earlier. The cover expires when the completed part is taken over, or put in service.



2. Operational Insurance Policies

Insurable property includes:

- Boilers
- Electrical equipment – generators, switchgears, transformers etc.
- Mechanical plants – engines, turbines etc
- Lifting equipment – cranes, conveyors, lifts etc.

These policies covers unforeseen and sudden physical damage by any cause to the insured property:

- While it is at work or at rest
- While being dismantled or clearing or overhauling
- During cleaning or overhauling operations
- When being shifted within the premises
- During subsequent erection.

The loss events could be:

- Electrical – short circuits, failure of insulation, etc.
- Mechanical – faulty material, design, casting, maladjustments, abnormal stress, explosion, etc.
- External – entry of foreign bodies, impact, collision etc.

Exclusions

These policies do not cover any loss or damage caused due to the following perils:

- Fire and special perils
- War and civil wars
- Nuclear risks
- Experimental loss due to over loading or tests

Sum Insured and Basis of Indemnification under operational phase

Sum insured of each item should represent its current new replacement value including cost to site, custom duties, and all installation costs. The basis of Indemnification is Restoration of the costs incurred or the Market value in case of total loss.

Let us now take a look at some of the important policies:

I. Storage-Cum-Erection Insurance Policy

Successful commissioning of any project according to schedule necessarily calls for a sound planning on various fronts and competent execution. A public authority or a private corporation commissioning a project will have to reckon with various risks to which the project may be exposed and these risks have to be managed. Broadly, these risks are either 'speculative' or 'pure'. The Storage-cum-erection insurance makes an attempt to take care of the 'pure' or physical risks connected with such activity. The construction of a factory involves preparation of site, laying of foundation and other incidental civil works and erection of plant and machinery. Erected plant and machinery have to be tested for proper mechanical functioning and later under load conditions and thereafter commissioned for commercial activity.

Industrial projects generally take a long time to complete extending from 2 to 5 years and throughout this period the materials connected with the project are continuously exposed to various types of risks like fire, explosion, storm, flood, earthquake, subsidence, rockslides, theft, pilferage etc. The aggregate value of the plant and machinery and materials at site gradually build up from the time of arrival at site of the first consignment and reaches its peak when the plant is ready for its test run. During the period of testing, the value of risk is maximum and during hot / load testing, the degree of exposure is the highest. The sum insured under a Storage cum erection policy should be the anticipated completed value of the project.

A big project generally involves several parties. The principal who conceives and ultimately owns the project, the contractor who executes the project along with the sub-contractors who assist him, the manufacturer of a machinery who may some times directly undertake to erect the machinery and the financiers who extend financial aid.

- Parties to the contract

A project may be subject to a turnkey contract or separate works contract directly with various contractors or manufacturers. The contract wording will determine who is responsible for loss/damage caused to property which ultimately go into the project. It is necessary to realize that each of the parties to the project has a stake in the successful completion of the project. It is open to each of the parties to take out separate insurance covers to take care of their share of exposure. However, it is far more efficient to arrange for one policy covering the entire project in the joint names of principal/contractor, sub-contractor, manufacturer and financier for their respective interest.

- Scope of cover

A Storage-cum-erection policy gives a combined and continuous cover, which can take care of the risks exposure of all the parties to the contract. It eliminates gap in cover. The SCE policy is also called the Erection All Risks cover and as the name suggests it is an omnibus cover against all risks.



II. Erection All Risks Insurance Policy

Under erection all risk insurance the company indemnifies the insured against sudden and unforeseen physical loss of or damage to the property insured in the manner and to the extent provided.

- General Exclusions

The company will not indemnify the insured in respect of loss, damage or liability directly or indirectly caused by or arising out of or aggravated by –

- a) War, invasion, act of foreign enemy, hostilities or war like operations etc.
- b) Nuclear reaction, nuclear radiation or radioactive contamination.
- c) Willful act or willful negligence of the insured or of his responsible representative
- d) Cessation of work whether total or partial.

- Period of Cover

If any specific date is not mentioned in the schedule, the liability of the company shall commence with the unloading of the property (specified in the schedule) on the site and shall continue until immediately after the first test operation or test loading is concluded (whichever is earlier). But in no case the period shall extend beyond four weeks once the trial running has been done or completion (readiness) of work has been declared by the contractor, whichever is earlier.

If there are several machines or parts in the plant, the liability of the company for the parts/machines ceases, as they are declared ready.

If the actual erection period is shorter than the period indicated in the schedule, no refund of premium shall be allowed, unless specifically allowed by insurers.

In the case of second-hand/used property, the insurance hereunder shall however, cease immediately on the commencement of the testing.

At the latest, the insurance shall expire on the date specified in the schedule but if the work of erection and test operations included in the insurance is not completed within the time specified hereunder, the company may extend the period of insurance but the insured shall pay to the company additional premium at agreed rates. Premium can be paid in quarterly installments in advance.

- General Conditions

All the conditions are same as those specified for boiler and explosion insurance policies (as the name itself suggests, they are “general conditions”). Two points worth mentioning here are:

- (A) Just like boiler and explosion policy, the insured is required to notify the company in the event of any occurrence that might give rise to a claim under this policy. Upon notification being given to the company under this condition, the insured may carry out the repair or replacement of any minor damage not exceeding Rs. 7,500.
- (B) This insurance may be terminated at the request of the insured at any time in which case the insurers will refund appropriate premium amount subject to the following conditions.
- i) Claims experience under the policy as on date of cancellation should be less than 60 % of reworked premium.
 - ii) The unexpired period is not less than 3 months or 25% of the policy period, whichever is less.
 - iii) Testing period should not have commenced.

This insurance may also at any time be terminated at the option of the insurer with 15 days notice to that effect being given to the insured in which case the insurers shall be liable to repay on demand a ratable proportion of the premium for the unexpired term from the date of cancellation.

SECTION I – MATERIAL DAMAGE

The company would reimburse any loss caused to the items specified in the schedule. The compensation would not exceed the limits specified in the schedule, both for individual items as well as total sum.

The company will also reimburse the insured for the cost of clearance and removal of debris following upon any event giving rise to an admissible claim under this policy but not exceeding in all the sum (if any) set opposite thereto in the schedule.

EXCLUSION TO SECTION – I

The company, shall not, however, be liable for:-

- a) The first amount of the loss arising out of each and every occurrence shown as excess in the schedule.
- b) Loss discovered only at the time of taking an inventory.
- c) Normal wear and tear, gradual deterioration due to atmospheric conditions or otherwise, rust, scratching of painted or polished surfaces or breakage of glass.
- d) Loss or damage due to faulty design, defective material or casting, bad workmanship other than faults in erection.

This exclusion shall be limited to the items immediately affected and shall not be deemed to exclude loss or damage to other insured items resulting from such excluded perils.



- e) The cost necessary for rectification or correction of any error during erection unless resulting in physical loss or damage.
- f) Loss of or damage to files, drawings, accounts, bills, currency, stamps, deeds, evidence of debt, notes, securities cheques, packing materials such as cases, boxes, crates.
- g) Any damage or penalties on account of the Insured's non-fulfilment of the terms of delivery or completion under his contract of erection or of any obligations assumed there under including consequential loss of any kind or description or for any aesthetic defects or operational deficiencies.

PROVISIONS APPLYING TO SECTION – I

There are six memos attached to section I explaining the provisions applying to it regarding sum insured, premium adjustment, basis of loss settlement, construction plant and machinery, surrounding property, major perils/acts of god claims.

Memo 1 – SUM INSURED

The sum of insurance stated in the schedule couldn't be less than the completely erected value of the property inclusive of freights, customs duty, erection cost.

(Sum of insurance stated in the policy) \geq (Completely erected value of the property)

- + Freights
- + Customs duty
- + Erection cost

Any change in sum due to rise or fall in the level of wages or prices can be incorporated with the knowledge of the company.

If it is found that the sum insured (representing the completely erected value of the property and/or of particular items involved) is less than the amount required to be insured the amount recoverable by the insured under the policy shall be reduced in such proportion as the sum insured bears to the amount required to be insured.

Memo 2 – PREMIUM ADJUSTMENT

After the completion of the project, the difference in premium (what should have been charged and what is charged) due to difference in estimated and actual cost will be adjusted on the basis of the actual values to be declared by the insured in respect of freight and handling charges, customs dues and costs of erection. Any increase or decrease in prime cost of plant and equipment shall not be the subject matter of premium adjustment.

Memo 3 – BASIS OF LOSS SETTLEMENT

In the event of any loss or damage the basis of any settlement under this policy shall be -

- a) In the case of damage which can be repaired, the cost of repairs necessary to restore the items to their condition immediately before the occurrence of the damage less salvage
- b) In the case of a total loss the actual value of the items immediately before the occurrence of the loss less salvage

If the costs involved in the latter were lower than those in the former, the company would replace the item instead of repairing it.

The cost of any provisional repairs will be borne by the company if such repairs constitute part of the final repairs and do not increase the total repair expenses.

The cost of any alterations, additions and/or improvements shall not be recoverable under this policy.

The cover can be extended on payment of additional premium to include charges for overtime, work on holidays, express freight (including air freight), which are not covered by this insurance, unless agreed upon at an additional premium.

Memo 4 – CONSTRUCTION PLANT AND MACHINERY

Loss of/or damage to construction plant and machinery excludes loss or damage directly caused by its own explosion or its own mechanical or electrical breakdown or derangement.

Memo 5 – SURROUNDING PROPERTY

- 1. The loss to the surrounding property belonging to/or held in care, custody or control of the Principal(s) or the Contractor (s) shall only be covered if
- 2. Occurring directly due to the erection, construction or testing of the items insured under Section - I
- 3. Happening during the period of cover, and
- 4. Provided that a separate sum therefore has been entered in the schedule

This cover does not apply to construction/erection machinery, plants and equipment.

Memo 6 – MAJOR PERILS/ACTS OF GOD CLAIMS

The Major Perils/Acts of God claims shall mean the claims arising out of:-

- a) Earthquake - Fire and shock
- b) Landslide/ rockslide/ subsidence,
- c) Flood/inundation
- d) Storm/ tempest/ hurricane/ typhoon/ cyclone/ lightning or other atmospheric disturbances.



SECTION II – THIRD PARTY LIABILITY

The company will indemnify the insured against -

- a) Legal liability for accidental loss or damage caused to property of other persons including property held in trust by/or under custody of the Insured for which he is responsible excluding any such property used in connection with erection thereon
- b) Legal liability (liability under contract excepted) for fatal or non-fatal injury to any person other than the insured's own employees or workmen or employees of the owner of the works or premises or other firms connected with any other erection work thereon, or members of the insured's family or of any of the aforesaid; directly consequent upon or solely due to the erection of any property described in the schedule.

Provided that the total liability of the company during the period of insurance under this clause shall not exceed the limits of indemnity set opposite thereto in the schedule.

In respect of a claim for compensation to which the indemnity provided herein applies, the company will, in addition, indemnify the insured against:-

- a) All cost and expenses of litigation recovered by any claimant from the insured
- b) All costs and expenses incurred with the written consent of the company.

The exclusions contained in paragraphs (d), (f) & (g) in Section I of this policy shall apply to this section also.

EXCLUSIONS TO SECTION II

The company will not indemnify the insured in respect of:

1. The excess stated in the schedule to be borne by the insured in any one occurrence related to property damage.
2. Expenditure incurred in doing or redoing or making good or repairing or replacing anything covered or coverable under Section I of this policy.
3. Liability consequent upon—
 - a) Bodily injury to/or illness of employees or workmen of the Contractor(s) or the Principal(s) or any other firm connected with the project which or part of which is insured under Section I, or members of their families;
 - b) Loss of/or damage to property belonging to or held in care, custody or control of the Contractor(s), the Principal(s) or any other firm connected with the project which or part of which is insured under Section I, or an employee or workman of one of the aforesaid;

- c) Any accident caused by vehicles licensed for general road use or by waterborne vessels or aircraft;
- d) Any agreement by the insured to pay any sum by way of indemnity or otherwise unless such liability would have attached also in the absence of such agreement.

CONDITIONS APPLYING TO SECTION-II

1. The insured should not make any admission, offer or promise or payment to settle the claim without the consent of the company. On the other hand, company can do so and the insured is required to fully cooperate with the company in its action.
2. The total amount insured decreases with each compensation made.

General conditions

The tariff applies to “erection all risks/storage cum erection insurance” with sum insured up to Rs.100 crores. For policies of sums exceeding Rs.100 crores but below Rs.1500 crores, separate guidelines were issued on 1st January, 2001. The jurisdiction of the tariff is the whole of India. (All are detariffed and these specifics may only be indicative at the most as each insurer is free to have its own rates and conditions).

The tariff contains the rules and regulations of erection all risks insurance in combination with marine insurance. Additional rates are fixed for covering earthquake perils, fire protection, express freight (air freight excluded, air freight only, dismantling charges and overtime rates of wages).

III. CONTRACTORS ALL RISKS INSURANCE

The Contractors All Risks Cover is similar to the Erection All Risk Insurance. This policy can be extended to the following kinds of work:

1. All Civil Engineering works, including massive dams.
2. Housing Developments, Industrial Buildings, Offices or Flats.
3. Water Treatment Plants, Canals, Roads.
4. Bridges, Tunnels, Docks.
5. Cooling Towers, Storage Tanks, Dams, Reservoirs, Piers – In short, for all kinds of civil construction work, including Residential and Office Buildings, and Factories and Civil Engineers Power Plants, Projects, Tunnels, Water Supply and Drainage System, Harbours, Roads, Railways and Airport Canals. The policy can be issued in the name of; (a) Principal or (b) The Contractors engaged in the Project, including Sub-contractors.



IV. CONTRACTOR'S PLANT & MACHINERY INSURANCE POLICY

This is a comprehensive policy available against unforeseen and sudden physical damage to the property by any cause, which has not been specifically excluded.

This applies to the insured plant and machinery whether at work or at rest, while being dismantled, or in the course of such operations themselves or while being shifted, re-erected etc., while such items are at the erection site.

The sum insured should be equal to the cost of replacement of insured property by a new property of the same kind and capacity.

- **Basis of Indemnity**

Actual value plus freight, customs duty etc., will be paid in case of total loss. In case of damage, necessary repair charges including dismantling and re-erection will be admitted.

- **Rating**

The rates and excess are governed by tariff. For risks exceeding Rs.5 crores, reference to TAC is necessary.

- **Extensions**

Extensions are available on payment of additional premia for third party liability cover, owner's surrounding property and removal of debris, inclusion of express freight, holiday wages, overtime pay, air freight etc.

V. BOILER AND PRESSURE PLANT INSURANCE POLICY

The boiler and pressure plant insurance is an important policy that fills in the loophole of the fire and allied perils insurance. Boilers and pressure vessels are commonly used in production plants like cotton mill, paper mill, petrochemical plant, etc. Even though the boilers are regularly inspected, still there are certain defects that go undetected. In such cases the explosion of the boiler would cause huge damage. Not only the boiler but also the surrounding property, which when damaged can cause huge losses. Hence it is always prudent on the part of the producer to go for boiler and pressure plant insurance.

While studying the boiler explosion policy it is important to keep in mind that it does not cover the losses covered by the fire policy. Its role and scope is restricted by this.

First of all we will clarify the different terms used at different places in the policy:

Definitions:-

The terms used in this policy have been explained below:

1. A 'Boiler' is defined as any fired closed vessel or a combined container piping system in which steam is generated under pressure.
2. 'Pressure plant' means any unfired closed container under steam gas or fluid pressure.
3. 'Explosion' is the sudden and violent rending or tearing apart of the permanent structure of a boiler or pressure plant or any part or parts thereof by force of internal steam gas or fluid pressure causing bodily displacement of the said structure and accompanied by the forcible ejection of its contents.
4. 'Collapse' is the sudden and dangerous distortion of any part of boiler or pressure plant by bending or crushing caused by steam gas or fluid pressure whether attended by rupture or not. It shall not mean any slowly developing deformation due to any cause.
5. 'Flue gas explosion' is the explosion of ignited gases in the furnaces or flues of the boilers, economisers and super heaters.
6. 'Chemical explosion' means an explosion arising out of chemical reaction in any plant.

The document that contains the details of the policy is called the schedule. Beginning with policy number and date, the schedule contains details of amount insured, annual premium, period of policy, boiler and pressure plants insured, surrounding property insured, legal liability to third parties as well as additional perils covered. Steam or feed water piping, separate super heaters, separate economizers etc. have to be mentioned specifically in the schedule. The term 'boiler' does not include them.

Let us see in detail the different perils the policy covers:

1. Damage (other than by fire) to the boilers and/or other pressure plant or surrounding property described in the schedule.
2. Liability arising due to death of or bodily injury to any person provided he is not employed or under apprenticeship with the insured.
3. Liability arising from damage to any property whether the insured is responsible for it or not

The damages listed above must be caused by and solely by explosion or collapse of any boiler or other pressure plant described in the schedule occurring in the course of ordinary working.



General Exceptions

1. As we stated in the beginning, the damages arising directly or indirectly from fire that from explosion or collapse or any other cause.
2. Damages caused by war, hostilities or war- like operations, natural calamities etc. Similarly damages from nuclear reaction, nuclear radiation or radioactive contamination are excluded.
3. If the explosion results from any experiment requiring overloading or abnormal conditions.
4. Defects that are gradually developing and would require repairs at some future date are not covered under this policy. Suppose what would happen if such defects would be covered? Every insured would try to get his boiler well serviced before the expiry of the policy.
5. Defects like wearing away or wastage of materials of any part of the boiler or failure of individual tube (if there are multiple tubes in the boiler). This is because such damages are not the result of explosion.
6. Damages due to negligence.
7. Consequential losses.
8. Damages due to flaws known but not disclosed by the insured.

Warranties

To prevent the insured from getting careless about the safety of boilers, these warranties are required on his part:

1. Annual inspection of boilers by appropriate authorities.
2. Only certified competent people will handle the boiler.
3. The boiler must work under permissible pressure limits.

Conditions

There are general conditions like the policy and the schedule that together form the contract. If any specific meaning is attached to any term in either of them, it will apply to whole of the policy. The pressure on the safety valves should not exceed the limit permitted in the latest inspection or the limit specified in the schedule, whichever is lower. If there is any change in the type of fuel used in the boiler the details should be intimated to the insurer and the terms of the policy revised accordingly.

Any fraudulent means that are resorted to, in order to benefit from the policy or if the claim is rejected and no action taken within 3 months, the benefits under the policy would be forfeited. The insured cannot make any admission, promise, payment or indemnity without the written consent of insurer. On the contrary, insurer may act to

settle the claims arising and the insured is bound to disclose all the relevant information to him in such circumstances.

If at the time of loss, the boiler or pressure plant turns out to be of greater value (including freight, custom duty and erection costs), the insurer will bear a rateable share of the loss.

Basis of indemnity differs when the item can be repaired and when it has to be replaced. In the first case, the insurer will pay the repairing cost and the incidental cost incurred in restoring the item to conditions prior to damage. The value of the salvage would be deducted. If the item is destroyed, the company will pay the value as assessed immediately before the accident. It will also pay the incidental charges (to the extent provided in schedule) incurred in setting it up in the premises. The company shall deduct depreciation and salvage value. The charges for extra work necessitated shall be paid only if mentioned in writing in the schedule.

Obligations of the insured are more or less same as warranties. The insured should carry out the points listed in the warranties attached in the standard policy. Besides, he should give the insured the right to inspect the boilers anytime. Moreover he is obliged to make all arrangements for the inspection. This includes stopping, cleaning, emptying the boiler.

If there is any material change in the subject matter of the policy, the same would be rendered invalid unless revised and endorsed by the company.

In case of an accident the insured is expected to observe the following duties:

- a) Immediately notify the company by telephone or telegram as well as in writing, giving an indication as to the nature and extent of loss or damage.
- b) Take all reasonable steps within his power to minimise the extent of the loss or damage or liability.
- c) Preserve the damage or defective parts and make them available for inspection by an official or surveyor of the company.
- d) Furnish all such information and documentary evidence as the company may require. The company shall not be liable for any loss or damage of which no notice is received or company has not received completed form within fourteen days of its occurrence.

Upon notification of a claim being given to the company the insured may proceed with the repair of any minor damage not exceeding Rs.2, 500.

If the liability due to claim is covered under some other insurance policy as well, the company will pay only its ratable proportion of such liability.

As far as the position of the insured after claim is concerned, he cannot abandon any property to the company once the claim is settled. Secondly the amount insured shall decrease with each compensation unless it is otherwise reinstated.



As we studied, the change in the subject of the policy renders it invalid. So is the case with ownership. If the interest in the property is transferred to some other party (except by will or operation of law), the insured should get the policy reinstated and endorsed by the company.

The policy can be terminated by:

- a) The insured at request
- b) The insurer by notice of 15 days

In case of termination, the company will retain the premium for the period the policy had been in force.

Regarding recourse, the insured reserves the right to perform any act necessary to obtain relief from the claims arising under the policy.

In case of dispute or differences between the insured and the insurer, regarding the quantum to be paid under the policy, the matter is solved through arbitration. If both the parties do not agree on a single arbitrator within 30 days, three arbitrators will be appointed, one by each party and the third by the two arbitrators.

It is clearly agreed and understood that no difference or dispute shall be referable to arbitration as herein before provided, if the company has disputed or not accepted liability under or in respect of this policy.

General Regulations

1. No policy to be issued on first loss basis.
2. No policy to be issued with a bonus clause.
3. Projects located outside India to be out of the jurisdiction of the committee.
4. Sum insured: It is a requirement of the policy that the boiler and pressure plants are covered for their present day new replacement value with a view to avoid under-insurance.

In addition, cover against damage to owner's existing surrounding property or selected limits of indemnity can be availed of. Likewise, damage to third party property and/or personal injury can also be covered for selected limits of indemnity.

5. Boiler and pressure plant insurance policy cannot be issued on agreed value basis.
6. Escalation benefit shall not be allowed under a boiler and pressure plant policy.
7. Short period scale of premium rates has been laid down in the policy that is applicable if the policy period is less than 12 months or if it is cancelled before this period at the request of the insured.

8. Refund of premium for standstill period:- Refund of premium for standstill period can be considered under this policy.

There should be minimum 3 months continuous standstill period for consideration of refund of premium.

Causes of standstill for complete plant should be as under:

- a) Due to non-availability of raw materials, acute power shortage, shortage of water supply and similar inputs.
- b) Standstill items like boilers, TG sets, steam engines and diesel generating sets, in lieu of sufficient standby equipments being available in the plant.
- c) In case of continuous process plant, due to a major breakdown of any item the whole plant cannot be run and as such refund to be considered. However refund of premium for the repair of the affected equipment should not be considered.

The table for the scale of refund for standstill period has been laid down in the policy.

It has also been laid down in the policy that the risks will be eligible for the standstill discount only when the claims experience under the policy for which the discount is sought, is less than 60 % and that the standstill discount will not apply during overhauling period (including hydraulic testing of boiler tubes under BPP policies).

No such refund is allowed for seasonal industries like sugar factories. However, the rate applicable for machinery shall be 95% of the rate for equipments for such seasonal factories. The decision of applying 95% of the rate for equipment in respect of seasonal factories is applicable for policies issued on annual basis only.

9. Rounding of Rates: It is not permissible to round off rates in boiler and pressure plant insurance policies.
10. Mid-Term Increase in Sum Insured: If the sum insured is increased during the currency of the policy.
- a) Short period scale of rates shall apply to increased amounts.
 - b) If the policy is renewed thereafter for 12 months for an amount not less than the increased sum insured, the difference of premium between short period scale of rate and pro-rata rate may be refunded.
11. Mid-Term decrease in Sum Insured: If the sum insured is decreased during the currency of the policy, short period scale of rates shall apply on the reduced sum insured.



VI. MACHINERY BREAKDOWN INSURANCE POLICY

The policy covers the damage caused to the machinery whether they are at work or at rest or even when dismantled for repairing or overhauling. Similarly damages caused during shifting them from one place to another or subsequent re-erection are also covered.

General exceptions

The company shall not be liable under this policy in respect of:–

1. Loss, damage and/or liability caused by or arising from or in consequence, directly or indirectly of fire or natural calamities, impact of land borne or waterborne or airborne craft or other aerial devices and/or articles dropped thereof.

Any loss or damage by fire within the electrical appliances and installation insured by this policy arising from or occasioned by overrunning, excessive pressure, short circuiting, arcing, self heating or leakage of electricity, from whatever cause (lightning included), is covered; provided that this extension shall apply only to the particular electrical machine; apparatus fixture fitting or portions of the electrical installation so affected and not to other machines, apparatus, fixtures fittings or portions of the electrical installation which may be destroyed or damaged by fire so set up.

2. Loss damage and/or liability caused by or arising from or in consequence, directly of:
 - a) War, invasion, act of foreign enemy, hostilities or war like operations (whether war be declared or not). Civil war, rebellion, revolution, insurrection, mutiny, riot, strike, lockout and malicious damage, civil commotion, military or usurped power, martial law, conspiracy confiscation, commandeering by a group of malicious persons or persons acting on behalf of or in connection with any political organisation, requisition or destruction or damage by order of any government *de-jure* or *de facto* or by any public, municipal or local authority.
 - b) Nuclear reaction, nuclear radiation or radioactive contamination.
3. Accident, loss, damage/and/or liability resulting from overload experiments or tests requiring the imposition of abnormal conditions.
4. Gradually developing flaws, defects, cracks or partial fractures in any part not necessitating immediate stoppage, although at some point of time in future repair or renewal of the parts affected may be necessary.
5. Deterioration of/or wearing away or wearing out any part of any machine caused by or naturally resulting from normal use or exposure.

6. Loss, damage and/or liability caused by or arising out of the willful act to willful neglect or gross negligence of the insured or his responsible representatives.
7. Liability assumed by the insured by agreement unless such liability would have attached to the insured notwithstanding such agreement.
8. Loss, damage and/or liability due to faults or defects existing at the time of commencement of this insurance and known to the insured or his responsible representative but not disclosed to the company.
9. Loss of use of the insured's plant or property of any other consequential loss incurred by the insured.
10. Loss, damage/ and/ or liability due to explosions in chemical recovery boilers, other than pressure explosions for e.g. smelt, chemical, ignition, explosions etc.

Special exclusions

The Company shall not be liable for:

1. The excess, as stated in the schedule, to be first borne by the insured out of each and every claim; where more than one item is damaged in one and same occurrence, the insured shall not, however, be called upon to bear more than the highest excess applicable to any one such item.
2. Loss of/or damage to belts, ropes, chains, rubber tyres, dies, moulds, blades, cutters, knives or exchangeable tools, engraved or impression cylinders or rolls, objects made of glass, porcelain, ceramics, all operating media (e.g. lubricating oil, fuel, catalyst, refrigerant, dowtherm) felts, endless conveyor belts or wires, sieves, fabrics, heat resisting and anti-corrosive lining and parts of similar nature, packing material, parts not made of metal (except insulating material) and non-metallic lining or coating of metal parts unless loss or damage to the equipments/machinery is indemnifiable in terms of the policy.
3. Loss or damage for which the manufacturer or supplier or repairer of the property is responsible either by law or contract.

In any action, suit or other proceeding where the company alleges that by reason of the provisions of the exceptions or exclusions above, any loss, destruction, damage or liability is not covered by this insurance, the burden of proving that such loss, destruction, damage or liability is covered shall be upon the insured.

Provisions

1. **SUM INSURED**

It is the requirement of this insurance that the sum Insured shall be equal to the cost of replacement of the insured property by new property of the same kind and same capacity which shall mean its replacement cost including freight and customs duties, if any, and erection costs.



2. BASIS OF INDEMNITY

- a) In cases where damage to an insured item can be repaired, the company will pay expenses necessarily incurred to restore the damaged machine to its former state of serviceability plus the cost of dismantling and re-erection incurred for the purpose of effecting the repairs as well as ordinary freight to and from a repair shop, customs duties if any, to the extent such expenses have been included in the sum insured. If the repairs are executed at a workshop owned by the insured the company will pay the cost of materials and wages incurred for the purpose of the repairs plus a reasonable percentage to cover overhead charges.

No deduction shall be made for depreciation in respect of parts replaced except for (i) wear and tear parts and (ii) parts for which manufacturers have specified a fixed life for use and the like but the value of any salvage will be taken into account.

If the cost of repairs as detailed herein above equals or exceeds the actual value of the machinery insured immediately before the occurrence of the damage the settlement shall be made on the basis provided for in (b) below.

- b) In cases where an insured item is destroyed, the company will pay the actual value of the item immediately before the occurrence of the loss including costs for ordinary freight erection and customs duties if any provided such expenses have been included in the sum insured, such actual value to be calculated by deducting proper depreciation from the replacement value of the item. The company will also pay any normal charges for the dismantling of the machinery destroyed but the salvage will be taken into account.

Any extra charges incurred for overtime, night-work, work on public holidays, express freight are covered by this insurance only if especially agreed to in writing.

In the event of the makers' drawings, patterns and for boxes necessary for the execution of a repair not being available, the company shall not be liable for cost of making any such drawing patterns or core boxes.

The cost of any alterations, improvements or overhauls shall not be recoverable under this policy.

The cost of any provisional repairs will be borne by the company if such repairs constitute part of the final repairs and do not increase the total repair expenses.

If the sum insured is less than the amount required to be insured as per provision 1 hereinabove, the company will pay only in such proportion as

the sum insured bears to the amount required to be insured. Every item if more than one, shall be subject to this condition separately.

The company will make payments only after being satisfied, with the necessary bills and documents that the repairs have been effected or replacements have taken place, as the case may be. The company may, however, not insist for bills and documents in case of total loss where the insured is unable to replace the damaged equipments for reasons beyond their control. In such cases claims can be settled on 'indemnity basis'.

3. INSPECTION OF TURBINES AND TURBO GENERATORS–

All mechanical and electrical parts of any steam turbine, gas turbine or generator upto 30,000 KW shall be inspected and overhauled thoroughly under the supervision of maker's representatives, in a completely opened up state at least every two years: for turbines or generators exceeding 30,000 KW such inspection and overhaul shall take place after 32,000 hours of operation or every four years. The cost of inspection and overhauling shall be borne by the Insured and a copy of the report issued by the maker's representative on such inspection and overhauling shall be furnished to the company immediately after the work has been carried out.

The conditions laid down in the policy are similar to those of other engineering policies.

VII. MACHINERY LOSS OF PROFITS INSURANCE

Under this policy the company makes good the losses arising from unforeseen and sudden damages to any machinery described in the schedule, during the period of policy. The following requirements should be met:

- The liability of company for claims remains within the limit specified in the schedule.
- The accident should happen during period specified in the policy and should be covered by standard machinery insurance policy or boiler & pressure plant insurance policy.
- The terms and conditions of the policy have been fulfilled.
- The statements and answers in the proposal form are true.

The cover provided under this policy shall be limited to loss of gross profit due to:

- (a) Reduction in output and
- (b) Increase in cost of working and the amount payable as indemnity there under shall be
 - In respect of reduction in output
 - In respect of increase in cost of working



The reduction in fixed charges if any during the period business is disrupted, shall be deducted from the compensation amount.

Definitions

1. Gross Profit

The sum produced by adding to the net profit the amount of the insured standing charges or if there be no net profit, the amount of the insured standing charges less such a proportion of any net trading loss as the amount of the insured standing charges bears to all the standing charges of the business.

2. Net Profit

The net trading profit (exclusive of all capital receipts and accretions and all outlay properly chargeable to capital) resulting from the business of the insured at the premises after due provision has been made for all standing and other charges including depreciation but before the deduction of any taxation chargeable on profits.

3. Output

The quantity of _____ produced at the premises, measured in units of _____

4. Indemnity Period and Time Excess

The period not exceeding the indemnity period limit stated in the list of machinery and plant insured commencing with the occurrence of the accident during which the results of the business are affected in consequence of such accident. Provided always that the insurers are not liable for the amount equivalent to the rate of gross profit applied to the standard output during the period of time excess (in terms of days) stated in the policy.

5. Rate of Gross Output

- a) Rate of Gross Profit: Rate of Gross Profit per unit earned on the output during the financial year immediately before the date of damage.
- b) Standard Output: Output during that period in 12 months immediately before the date of damage which correspond to indemnity period.
- c) Annual Output: The output during 12 months immediately before the date of damage.

Provisions

The following memos are attached with the standard policy:

1. Memo 1 – Benefits from Other Premises

If during the indemnity period goods are sold or services are rendered elsewhere than at the premises for the benefit of the business either by the insured or by others acting on his behalf, the money paid or payable in respect of such sales

or services shall be taken into account in arriving at the turnover during the indemnity period.

2. Memo 2 – Relative Importance

The term relative importance referred to in the list of machinery and plant insured shall be the percentage effect which a breakdown of a particular machine will have on the total gross profit, disregarding any loss minimising measures.

If in the event of an accident affecting an insured item of machinery, the percentage of relative importance stated in the list of machinery and plant insured for this item is lower than the actual percentage of relative importance subsequently arrived at for the period of interruption, the company shall only be liable to indemnify the proportion which the percentage of relative importance stated in the list of machinery and plant insured bears to the actual percentage.

3. Memo 3 – Returns of Premium

If the insured declares in the latest twelve months after the expiry of any policy year that the gross profit earned during the accounting period of twelve months most nearly concurrent with any period of insurance as certified by the insured's auditors was less than the sum insured thereon, a pro-rata return of premium not exceeding one half of the premium paid on such sum insured for such period of insurance shall be made in respect of the difference.

If any accident has occurred giving rise to a claim under this policy, the amount of such claim shall be added to the revised gross profit as certified by the insured's auditors before calculating the proportion of return of premium.

4. Memo 4 – Overhauls

In calculating the loss, due allowance shall be made for the time spent on any overhauls, inspections or modifications carried out during any period of interruption.

5. Memo 5 – Reinstatement of sum Insured

For the period following the occurrence of an accident up to the end of the policy period, the sum insured shall be reinstated by payment of an additional premium on a pro-rata basis. Such additional premium shall be adjusted against the net claim amount payable and such premium shall be calculated for that part of the sum insured, which corresponds to the indemnity paid. The agreed sum insured shall remain unaltered.



Exclusions

The company shall not be liable for any loss resulting from interruption of/or interference with the business directly or indirectly attributable to any of the following causes:

- i) Willful act or willful neglect or gross negligence of the insured or his responsible representatives.
- ii) Loss or damage to machinery or other items, which are not listed in the list of machinery insured even if the consequence of material damage to an item indicated in the list of machinery insured is involved.
- iii) Loss or damage caused by any faults or defects existing at the time of commencement of this insurance within the knowledge of the insured or his responsible representatives whether such faults or defects were known to the company or not.
- iv) Shortage, destruction, deterioration and spoilage of/or damage to raw materials, semi finished or finished products or catalyst or operating media (such as fuel, lubricating oil, refrigerant, heating media and the like) even if the consequence of material damage to an item indicated in the list of machinery insured is involved.
- v) Any restrictions on reconstruction or operation imposed by any public authority.
- vi) An extension of the normal repair period for more than 4 weeks on account of-
 - a) The inability to secure or delays in securing replacement parts, machines or technical services.
 - b) The inability to carry or delays in repairs.
 - c) The prohibition to operate the machinery due to import and/or export customs & other restrictions or by statutory regulations.
 - d) Transport of parts to and from the insured's premises.
- vii) Alterations improvements or overhauls being made while repairs or replacements of damaged or destroyed property are being carried out.
- viii) Loss damage and/or liability caused by or arising from or in consequence Directly or indirectly of: -
 - a) War, invasion, act of foreign enemy, etc.
 - b) Nuclear reaction, nuclear radiation or radioactive contamination.

General Regulations

1. The insurers should not quote a rate lower than Rs. 1.40 even provisionally when they underwrite new proposals in respect of fertiliser risks.
2. Policies are normally issued on turnover basis. The policies can be issued on 'output' basis for loss of profits cover following machinery breakdown and/or boiler explosion only to manufacturers having single end products. For manufacturers having multiple end products individual proposals must be submitted to Tariff Advisory Committee for approval before granting LOP cover on 'output' basis.
3. Insurers can extend MLOP Cover on DG Sets subject to adequate re-insurance support.
4. With regard to the issuance of MB (LOP) policies in the first year of operation such proposals will be considered by the committee on case-to-case basis and the rates will be decided by the committee.
5. Rules for Cancellation: For cancellation of insurance during the currency either wholly or in part
 - a) At the option of the insurer, a pro-rata refund of premium may be allowed for the unexpired term on demand.
 - b) At the insured's request, refund of premium may be allowed after charging premium for the time insurance was in force on short period scale as defined in the All India Fire Tariff subject to the retention of minimum premium by the insurer.

However, if, a new annual policy replaces the old one, covering identical equipment/machines for sum insured not less than the respective sums insured under the cancelled policy, refund of premium may be allowed on pro-rata basis subject to retention of minimum premium.

If the risk is insured under short period scale, refund may be calculated at pro-rata of the short period scale premium provided such cancellation is followed by an annual policy for sum insured not less than the sum insured under cancelled policy. Otherwise, retention of premium shall be on short period scale.

For the sum insured not replaced in the renewed policy after cancellation, refund must be calculated after charging premium on such sum for the time insurance was in force on short period scale subject to retention of minimum premium by the insurer.

For the policy issued or renewed for periods shorter than 12 months, the premium rate shall be charged as per the short period scales prescribed under CPM Tariff. The short period scale of rates under CPM Tariff shall



also be followed in respect of cancellation of policies during the currency of the policy by the insured.

- c) In case of revision of tariff rates/excess, it is not permissible to cancel the policy and allow a refund of premium whereby an insured pays lower premium for an insurance than is payable at the rates applicable at the commencement of the policy.
6. Increase in Sum Insured: If the sum insured is increased during the currency of the policy.
- i) Short period scale of rates shall apply to increased amounts.
 - ii) If the policy is renewed thereafter for 12 months for an amount not less than the increased sum insured, the difference of premium between short period scale of rates and pro-rata rate may be refunded.
7. Minimum Time Exclusion under LOP Policies:
- i) 14 days for Power Plants (both captive and public), fertilizer plants, petroleum refineries, petrochemical plants, explosive manufacturing plant.

Insurers may accept 7 days 'time excess' for all MLOP proposals for fertilizer risks with adequate reinsurance support.
 - ii) 7 days for all other industries.

Note - *The time exclusion for boiler will follow the industry in which it is installed.*

8. Rating: Rates under this tariff will be decided at insurers discretion.
9. Rounding off rates: Premium rates shall not be rounded off in case of MLOP policies.

Conditions

- a) This Policy shall be avoided due to one of these:
 - i) The business be wound up or carried on by a liquidator or receiver or permanently discontinued.
 - ii) The insured's interest ceases otherwise than by death.
 - iii) Any alteration be made whereby the risk of an accident is increased.
 - iv) The retention of standby or spare machinery or any other loss minimising factors in existence when this insurance was effected be reduced or discontinued unless its continuance is admitted by an endorsement signed by or on behalf of the company.

The insured shall be obliged to keep complete records. All records e.g. inventories, production and balance sheets for the three preceding years shall be held in safe keeping or as a precaution against their being simultaneously destroyed the insured shall keep separate sets of such records.

In the event of a claim being made under this policy not later than thirty days after the expiry of the indemnity period or within such further time as the company may allow in writing at his own expense deliver to the company a written statement setting forth particulars of his claim together with details of all other policies covering the accident or any part of it or consequential loss of any kind resulting thereof and the insured shall at his own expense also produce and furnish to the company such books of accounts and other business books e.g. invoices, balance sheets and other documents, proofs, information, explanation and other evidence as may reasonably be required by the company for the purpose of investigating or verifying the claim together with if required - a statutory declaration of the truth of the claim and of any matters connected therewith.

No claim under this policy shall be payable unless the terms of this condition have been complied with and in the event of non-compliance therewith in any respect any payment already made on account of the claims shall be repaid to the company forthwith.

Midterm increase in sum insured

'If the sum insured is increased during the currency of the policy -

- i) Short period scale of rate shall apply to the increased amount.
- ii) If the policy is renewed thereafter for twelve months, for an amount not less than the increased total sum insured, the difference of premium between the short period scale of rates and pro-rata rate, may be refunded, or a new policy for the full increased sum insured, may be issued, at the tariff rate (annual or short period, as required) canceling the old insurance and allowing a pro-rata refund for the unexpired period of the cancelled policy'.

Departmental clause – Applicable when business has separate sections or departments, each earning a different rate of gross profit.

If the business be conducted in departments, the independent trading results of which are ascertainable, the provision of clauses (a) & (b) of item 1 of the specification shall apply separately to each department affected by the damage; provided that if the sum insured by the said item be less than the aggregate of the sum produced by applying the rate of gross profit provided for each department of the business (whether affected by the accident or not) to the relative annual output thereof, the amount payable shall be proportionately reduced.

In no case whatever shall the company be liable in respect of any claim under this policy after the expiry of –



- i) One year from the end of the indemnity period or if later.
- ii) Three months from the date on which payment shall have been made or liability admitted by the company covering the accident giving rise to the said claim unless the claim is the subject of pending action or arbitration.

Every notice and other communication required by these conditions must be written or printed.

Endorsement: time excess clause is available as endorsement

VIII. ELECTRONIC EQUIPMENT INSURANCE

This is an omni bus cover against all risks for electronic equipment. In addition to break down cover, it provides protection against fire and allied perils, burglary, terrorism etc.

Sum insured

It is a requirement of this insurance that the sum insured shall be equal to the cost of replacement of the insured by new property of the same kind and same capacity which shall mean its replacement cost including freight, dues and customs duty, if any, and erection cost.

The policy covers the following:

- a) Material damage.
- b) Damage to external Data Media

IX. ADVANCE LOSS OF PROFITS INSURANCE (Also known as Business Interruption Insurance)

● Suitability

This policy covers monetary losses due to delayed commissioning of the project as a result of a loss during construction/erection which is covered under a project insurance policy (MCE/EAR/CAR).

The policy is suitable for:

- a) The principal who shall be deprived of the anticipated earnings in the event of delay in commencement of operations and
- b) The financial institutions to the extent of their interest in the project.

● Salient Features

The policy offers cover against loss of anticipated earnings/profits due to the delay in commissioning of the project following a loss covered under the project insurance policies.

The costs covered are:

1. Loss of gross profits – based on anticipated sales, cost and prices.
2. Loss of gross earnings – sales value of production less consumed stocks, supplies and services purchased.
3. Increased cost of working – costs involved in minimizing the effects of the delay.
4. Principal and interests – lending institutions' interest in the portion of gross profit.
5. Loss of rent – as a result of premises not being ready to earn rent.
6. Special expenses – costs involved because of delay such as advertisement campaign etc.

● **Benefits**

The policy is operational during the whole or part of the preparatory period of a new venture. In case of any accident or damage during this period which delays commencement of trading beyond the starting date, this policy covers loss of trading income, loan interest and other charges which are payable despite lack of income and increase in expenses incurred in reducing or avoiding the delay in startup. The indemnity period shall be the duration between the dates of actual commencement of insured's business and the date of scheduled commencement had there not been a delay.

There is a time excess of 30 days for this policy.

The changed industrial scenario led to the growing demand for insurance of loss of anticipated earnings, due to delays in commissioning of projects. Foreign financial institutions have also made the 'advance loss of profit' cover an essential condition for disbursing assistance to Indian clients. It is thus vital for mega projects with substantial financial involvement to have advance loss of profits cover together with cover for project during its erection.



Questions



1. List the general exceptions under the boiler and pressure plant insurance.
2. What are the warranties required under the boiler and pressure plant insurance from the insured?
3. What additional coverages can be secured through endorsement under the boiler and pressure plant insurance?
4. Under what insurance is the Refund of Premium for standstill period available?
5. What is meant by reinstatement of sum insured?

CHAPTER – 8

MISCELLANEOUS INSURANCE

OUTLINE OF THE CHAPTER

- Introduction
- Crop insurance
- Aviation Insurance
- Personal Accident Insurance
- Travel Insurance
- Overseas Travel Insurance
- Golfer's Insurance
- Crime Insurance
- Burglary Insurance
- Baggage Insurance
- Bankers' Indemnity Insurance
- Plate Glass Insurance
- Fidelity Guarantee Insurance
- Questions

LEARNING OBJECTIVES

After reading this chapter you should be able to:

- Classify the risks covered by miscellaneous insurance
- Understand the need for workmen's compensation insurance
- Describe the objectives and salient features of crop insurance
- Understand personal accident insurance
- Appreciate the importance and types of aviation insurance
- State the various policies available under burglary insurance
- Describe the risks covered under banker's indemnity insurance



- Explain the meaning of plate glass insurance
- Have a good understanding of fidelity guarantee insurance
- Determine the scope and future of Directors and officers insurance

INTRODUCTION

The insurance industry is developing rapidly, not only in the scope of activities covered but also by the various new insurance covers that are being introduced. One area that saw rapid growth in a short span is miscellaneous insurance, also called accident insurance in England and casualty insurance in USA.

According to Section 2(13B) Indian Insurance Act, 1938 Miscellaneous Insurance Business is “the business of effecting contracts of insurance which is not principally or wholly of any kind or kinds included in Fire, Life and Marine Insurance business.”

The risks covered by miscellaneous insurance are classified into four main categories concerning

- Person
- Property
- Pecuniary risks, and
- Liabilities.

The first category includes insurance for individuals and groups against health risks such as accidents and hospitalization & critical illness.

- Property risks relate to burglary, housebreaking, etc., and include other classes like livestock, plate, glass, money in transit and others.
- Pecuniary risks refer to fidelity and other credit or financial guarantees
- Liability insurance includes personal liability insurance, commercial general liability, professional indemnity, product liability and other similar policies.

CROP INSURANCE

In India crop insurance cover is not very widespread. We will look into the reasons for such a condition but before that it is necessary to have an idea of the crop insurance policy.

Crop Insurance Schemes in India

In order to provide a boost to the agriculture in India, a number of experimental crop insurance schemes have been introduced in the Country. The first ones of the experimental crop insurance schemes has been a Pilot Crop Insurance scheme. This was introduced by GIC from the year 1979.

Some of the important features of the scheme were that the scheme was based on "Area Approach". This scheme covered crops such as Cereals, Millets, Oilseeds, Cotton, Potato and Gram. The scheme was confined to loanee farmers only and on voluntary basis. The risk was shared between General Insurance Corporation of India and State Governments in the ratio of 2:1. The maximum sum that could be insured under the scheme was 100% of the crop loan, which was later increased to 150%.

- a) Under this scheme, 50% of the subsidy was provided for insurance charges which was payable to the small/marginal farmers by the State Government & the Government of India on 50:50 basis.
- b) Among the earlier crop insurance schemes that were introduced was a comprehensive Crop Insurance Scheme. The Government of India introduced the Comprehensive Crop Insurance Scheme with effect from 1st April 1985. This scheme was introduced with the active participation of State Governments. The Scheme was optional for the State Governments.

Objectives

The objectives of the scheme are as follows: -

1. To provide insurance coverage and financial support to farmers in the event of natural calamities, pests and diseases.
2. To encourage the farmers to adopt progressive farming practices, high value inputs and higher technology in agriculture.
3. To help stabilise farm incomes, particularly in disaster years.

Salient features of the scheme

- Crops covered

The crops in the following broad groups in respect of which i) the past yield data based on Crop Cutting Experiments (CCEs) is available for adequate number of years, and ii) requisite number of CCEs are conducted for estimating the yield during the proposed season:

- a) Food crops (Cereals, millets and pulses)
- b) Oilseeds
- c) Sugarcane, cotton and potato (annual commercial/annual horticultural crops)

Other annual commercial/horticultural crops subject to availability of past yield data will be covered in a period of three years. However, the crops, which are covered next year, will have to be specified before the close of preceding year.



- Farmers to be covered

All farmers including sharecroppers, tenant farmers growing notified crops in notified areas are eligible for coverage.

The scheme covers the following groups of farmers:

- a) On a compulsory basis:** All farmers growing notified crops and availing Seasonal Agricultural Operations (SAO) loans from financial institutions i.e. loanee farmers.
- b) On a voluntary basis:** All non-loanee farmers growing notified crops who opt for the scheme.

- Risks covered and exclusions

Comprehensive risk insurance will be provided to cover yield losses due to non-preventable risks (natural perils) like, fire and lightning, storms, hailstorm, cyclones, typhoon, hurricanes, tornados, as also floods, landslides, droughts, pests/diseases etc.

Losses arising out of war and nuclear risks, malicious damage and other preventable risks shall be excluded.

- Sum insured /limit of coverage

The Sum Insured (SI) may extend to the value of the threshold yield of the insured crop at the option of the insured farmers. However, a farmer may also insure his crop beyond the value of threshold yield level upto 150% of average yield of notified area on payment of premium at commercial rates.

In case of loanee farmers the sum insured would be atleast equal to the amount of crop loan advanced.

Further, the insurance charges shall be additional to the Scale of Finance for the purpose of obtaining loan.

In matters of crop loan disbursement procedures, the guidelines of RBI/NABARD shall be binding.

- Premium rates go to the maximum 3.5% for *bajra* and oilseeds.

- Premium subsidy

A 50% subsidy in premium is allowed in respect of small farmers (a cultivator with a land holding of 2 hectares [5 acres] or less) and marginal farmers (a cultivator with a land holding of 1 hectare or less [2.5 acres]) to be shared equally by the Govt. of India and State Government/Union Territory. The premium subsidy will be phased out on sunset basis within a period of three to five years subject to

review of financial results and the response of farmers at the end of the first year of the implementation of the scheme.

- Risk will be shared by the implementing agency and the Government. The quantum of risk to be assumed by each is listed down in the policy.

- Area approach and unit of insurance

The scheme would operate on the basis of 'area approach' i.e., defined areas for each notified crop for widespread calamities and on an individual basis for localised calamities such as hailstorm, landslide, cyclone or flood.

- Estimation of crop yield

The State Govt/UT will plan and conduct the requisite number of Crop Cutting Experiments (CCEs) for all notified crops in the notified insurance units in order to assess the crop yield. It maintains single series of Crop Cutting Experiments (CCEs) and resultant yield estimates, both for crop production estimates and crop insurance.

- Levels of indemnity and threshold yield

Three levels of indemnity, viz. 90%, 80% and 60%, corresponding to low risk, medium risk and high risk areas shall be available for all crops (cereals, millets, pulses and oilseeds and annual commercial/ annual horticultural crops) based on Coefficient of Variation (C.V.) in the yield of past 10 years' data. However, the insured farmers of unit area may opt for higher level of indemnity on payment of additional premium based on actuarial rates.

The threshold yield (TY) or guaranteed yield for a crop in an insurance unit shall be the moving average based on past three years' average yield in case of rice and wheat and five years average yield in the case of other crops, multiplied by the level of indemnity.

- Nature of coverage and indemnity

If the 'actual yield' (AY) per hectare of the insured crop for the defined area [on the basis of requisite number of Crop Cutting Experiments (CCEs)] in the insured season, falls short of the specified threshold yield, all the insured farmers growing that crop in the defined area are deemed to have suffered shortfall in their yield. The scheme seeks to provide coverage against such contingency.

'Indemnity' shall be calculated as per the following formula:

(Shortfall in yield / threshold yield) X Sum insured for the farmer

{Shortfall = "Threshold yield – Actual yield" for the defined area}



- Procedure for approval and settlement of claims

Once the yield data is received from the State Govt/UT as per the prescribed cut-off dates, claims are worked out and settled by Implementing Agency (IA).

The claim cheques along with claim particulars will be released to the individual nodal banks. The bank in turn, shall credit the accounts of the individual farmers and display the particulars of beneficiaries on their notice board.

- Financial support towards Administration and Operating (A & O) expenses

The A & O expenses would be shared equally by the Central Government and the respective State Governments on sunset basis [100% in 1st year, 80% in 2nd year, 60% in 3rd year, 40% in 4th year, 20% in 5th year and 'zero' percent thereafter].

- Corpus fund

To meet catastrophic losses, a corpus fund shall be created with contributions from the Govt. of India and State/UT on a 50:50 basis. A portion of calamity relief fund (CRF) shall be used for contribution to the corpus fund.

The corpus fund shall be managed by an Implementing Agency (IA).

- Implementing Agency (IA)

An exclusive organisation is to be set up in due course, for implementation of crop insurance. Until such time the GIC of India will continue to function as the Implementing Agency.

Scenario in India

Crop insurance that offers efficient and comprehensive protection to farmers has been under discussion since Independence. A Pilot Crop Insurance Scheme (PCIS) was in place between 1979-80 and later from 1984-85. A comprehensive crop insurance scheme was introduced in April 1985. The National Crop Insurance Scheme was started from 1999-2000 rabi season. All these schemes were group insurance schemes, aimed at farmers taking crop loans from banks.

The premiums were minimal — 1-3 percent. The risk was shared by the Centre, the State governments and the General Insurance Corporation. The financial results of the three schemes indicated that none succeeded in correctly estimating the actuarial probability of the risk covered. The claims paid were almost six times the premiums collected in the comprehensive schemes. They would be more than six times higher under the National Crop Insurance Scheme.

The block nature of the crop insurance schemes and the fact that the premium has no actuarial basis, takes away the business character of the schemes. It encouraged those wanting to take undue advantage of the schemes. It would appear that in many cases where the actual loss was serious, little or no compensation was paid. There are also cases where there was little loss but the compensation was based on block experience.

As India moves towards world-class agriculture and is becoming increasingly market-oriented, a dependable crop insurance scheme has become a necessity. The agricultural sector primarily depends on monsoon, which is known for its erratic character. Furthermore, the low capital utilisation and the small size of holdings make agriculture in India fraught with risk.

A study comparing model yields of 15 crops showed that the risk of loss is as high as 40-60 percent. The model yields in India are much lower than the actual yields in many other countries; and the actual yields are still lower. It would appear that if crop insurance is to give protection at the present model yields after deducting a basic loss, the premium might be as high as 30 percent. Thus, a crop insurance scheme based on a premium of 1-3 percent of the amount covered cannot provide effective insurance cover.

Agriculture Insurance Company of India Ltd., New Delhi is the exclusive agency for implementing crop insurance in India now. It started functioning from 1.4.2003. The Company enjoys the distinction of being the largest crop insurance provider in the world in terms of the number of farmers insured annually. During 2005-06, more than 167 lakhs farmers were brought under the crop insurance umbrella. The main product i.e. "National Agricultural Insurance Scheme" [NAIS] is presently implemented in 23 States and 2 UTs by the company and it is also making continuous efforts to bring the remaining States/UTs into its fold.

The Company presently operates through its 17 Regional Offices located in State Capitals across the country, under the supervision & control of Head Office at New Delhi. The company envisages to bring more and more farmers into the insurance net by offering them varied and tailor-made products and services. Of late, great emphasis is being laid on risk management in agriculture too.

A Working Group has been set up under the Planning Commission, to look into the various aspects relating to agriculture & allied activities, including Credit & Insurance, so as to identify the various kinds of risks and the various ways and means to address to them, including extensive as well as intensive enhanced insurance coverage under NAIS. The company also appointed Prof. V. S. Vyas and his team at The Institute of Development Studies, Jaipur to carry out a comprehensive study of the working of the Crop Insurance program. The findings of the study are still being examined by the company. Further, to adopt a more realistic and market-based approach based on sound insurance principles, the Company is also taking the assistance from the



World Bank for designing and pricing of area based yield product. The World Bank conducted the study through reputed international Actuaries particularly in the areas of designing and rating of Weather Insurance Products and the Company's Risk Portfolio Management.

Agriculture scenario

Ironically, even though agriculture's share in Gross Domestic Product has steadily declined to 18.5% during 2006-07, till today, more than half of the population directly depends on this sector and that is the reason why agriculture is so crucial in the socio-economic fabric of the country. It is well known that a vast majority of the farmers cultivate their crops in rain-fed conditions during monsoon season which impacts every stage of agricultural operations from land preparation to selection of seed variety, timing of sowing, transplantation, schedule of irrigation, fertilizer application, usage of pesticide, harvesting, etc.

It is in this context that the agricultural risk management products, viz. insurance, particularly for the small and marginal farmers, are of critical importance. Study reveals that 'variability in rainfall' accounts for more than 50% variability in crop yields. It is also found that the negative impact of excess rainfall is not as high as the adverse impact of deficit rainfall. In this backdrop, the 2006 monsoon rainfall was at 99% of the long period average but distribution over time and space was uneven which affected east India, north-west India and south peninsula.

National Agricultural Insurance Scheme (NAIS)

The National Agricultural Insurance Scheme, which is being implemented by the Company, on behalf of the Union/State/UT Governments, is the main business of the Company. The Company's emphasis is towards educating the farmers and creating Crop Insurance awareness. During the year 2005 -06, the number of farmers insured under NAIS grew by 3.08% to 167.18 lakhs farmers, with corresponding increase in Premium booked by 3.72%.

New Products Launched

Some of the new products introduced by the company with the sustained R&D efforts include the following:

- Sookha Suraksha Kavach
- Coffee Insurance
- Mango Weather Insurance

- **Sookha Suraksha Kavach**

The Company had launched another rainfall index based insurance product, specially designed for the State of Rajasthan. It was implemented in a few districts for the benefit of farmers in drought-prone areas. The product has been designed to cover popular and widely grown crops like Guar, Bajra, Maize, Jowar, Soyabean and Groundnut which are grown in the semi-arid climate of Rajasthan.

- **Coffee Rainfall Index & Area Yield Insurance**

Coffee Rainfall Index & Area Yield Insurance has been introduced on a pilot basis in the State of Karnataka, to indemnify the coffee growers against the likelihood of diminished coffee yield resulting from either shortfall in actual rainfall index within a specified geographical location and a specified time period, and/or yield losses due to other non-preventable natural factors. In all 58 coffee planters, covering an area of 514.21 hectares was insured for Rs. 169.43 lakhs against a Premium of Rs. 3.66 lakhs. No Claims have so far been reported.

- **Mango Weather Insurance**

The Company has come out with a product to insure the Mango crop under weather insurance. The Mango crop is extremely vulnerable to weather factors like excess rainfall, frost, temperature-fluctuations, and wind-speed. The Company has designed Mango Insurance for a few districts of Andhra Pradesh, Maharashtra and Uttar Pradesh on a pilot basis. The product is unique in the sense that, as many as four weather parameters are used as triggers for indemnity. The product has been designed after an extensive field study and discussions with the scientists working on Mango cultivation.

Awareness & Publicity Program

The Company undertakes extensive awareness and publicity activities through print and electronic media, posters, wall paintings, bus panels and mobile-vans, awareness workshops at State and District levels where farmers, bank officials, district level government functionaries and other interested parties are briefed about the services.

A massive awareness campaign for NAIS called “**Krishi Bima Kisan Tak**” [KBKT] was undertaken to touch 1,00,000 villages in 3,600 tehsils, across 400 districts of 23 states & 2 UTs, with the objective to make the farmers aware of crop insurance and the benefits available there under.



Micro Level Marketing Strategy

Further, to reach out to the farmers at their doorstep, the Company has made plans to launch “Krishi Bima Sansthan” [KBS], which conceptualizes utilization of rural entrepreneurs to market crop insurance products, especially to non-loanee farmers. The KBSs are proposed to be established at district levels, backed by the work-force of Agents/Micro-Agents.

IRDA regulations on micro insurance provides for servicing of micro insurance products through micro insurance agents to be selected from SHGs, MFIs & NGOs.

Product Development

The Company has undertaken studies to design various farmer-friendly, tailor-made, affordable products, in accordance with the sound actuarial principles to cater to the specific needs of different farmer groups. Some of the products are:-

Rainfall Insurance

Rainfall Insurance product, more popularly known as Varsha Bima, was developed to combat the impact of adverse rainfall incidence. The product was aimed at mitigating some of the adverse financial effects of rainfall variation on crop yield. A correlation between the deviation in crop output and the deviation in the adverse rainfall is established and payout structures are created and the insured farmers are accordingly compensated. The main advantage of the product is quick settlement of claims on the basis of rainfall data obtained from the designated Rain Gauge Stations.

Rabi Weather Insurance for Field Crops

The Company designed a tailor-made weather index based insurance product for Rabi season for the farmers serviced by ‘e-chaupals’ of ITC in the States of Madhya Pradesh, Maharashtra, Rajasthan & Uttar Pradesh. The product covered potato, wheat, barley, lentil, gram etc.

Bio-Fuel Tree / Plant Insurance

The Company designed a named peril product to insure six different species commercially grown for bio-fuel production. The annual policy is being sold to corporates / institutions involved in commercial production of bio-fuel.

Potato Crop Insurance

There has been a demand from potato growers for an ‘individual farm’ based potato insurance against natural calamities, pests & diseases. Considering this, AIC has designed “Potato Crop Insurance (Input) Policy”. The product has been designed after a careful study of package of practices, lending arrangements and buy-back arrangements by the agencies. Initially, during Kharif 2006 season, the product was tried out in and around Pune.

Modified Products

Poppy insurance

Poppy insurance introduced during Rabi 2005-06 season has been modified on the basis of experience and review; and got it approved as 'Micro Insurance Product' for Rabi 2006-07 season. This policy was made available to the licensed poppy growers in the States of Madhya Pradesh, Rajasthan & Uttar Pradesh.

Wheat Crop Vigor & Weather Insurance

Wheat Crop Vigor & Temperature based insurance product piloted in a few districts of Haryana & Punjab during Rabi 2005-06 season has been modified on the basis of the review. We have also added a new trigger in terms of 'unseasonal rainfall'. The product is being marketed as 'Wheat Crop Vigor & Weather Insurance' product from Rabi 2006-07 season.

If the actuarial insurance premia are to be as high as 30 per cent, any effective crop insurance company would be several times bigger than LIC and would not be feasible unless the element of risk is substantially reduced by improving availability of irrigation and the systems of weather forecasting.

If the actuarial risk factor is computed into the calculations of the cost of production and, consequently, in the statutory minimum price, during years when the contingent risk does not arise, the farmers will be able to keep aside sums that can accumulate over the years, until the contingent risk actually occurs. This will amount to self-insurance. It is only after a system of self-insurance has worked for a number of years that it will be possible to establish a scientific scheme of insurance for crops, which is a gamble not only because of uncertain monsoon, but due to so many other factors as well.

Recently as seen above Agricultural Insurance Corporation is looking after the crop insurance schemes. Earlier GIC of India has been managing crop insurance on behalf of Central Government. Now GIC is converted to National reinsurer, a separate organisation.

AVIATION INSURANCE

Aviation industry is vulnerable to risks of devastating losses. If a single aeroplane crashes, lives of hundreds of people are lost along with the aircraft besides the damage caused to the place where the accident occurs. Insurance is hence of paramount importance for this industry. The most common coverages of aviation insurance are:

- Aircraft liability insurance
- Hull coverage
- Personal accident



The premium rate for each aircraft is driven by international reinsurance markets, mainly @ UK, based on the world trend in claims experience during the preceding years.

Aircraft Liability Insurance

The liability in case of aviation insurance is divided into two categories:

- Passenger liability
- Death and injury to third parties

There are some policies that cover both these categories as well as property damage with a single limit to cover all three of them (like floating policies in fidelity guarantee).

Admitted liability

Here specific amounts are allocated beforehand to the various kinds of injuries like the loss of a limb, eye or life. The policy is written on 'per seat' basis. In case of an accident the insurer offers the payment along with the release of liability against the insured. The injured party is required to sign the release against the insured if he wants payment from insurer. Otherwise he will have to obtain compensation on his own. As the insurer voluntarily offers compensation on the occurrence of accident, this policy is also called "voluntary settlement charge".

Medical Payments

The aircraft liability insurance also provides coverage of medical payments for injuries sustained while travelling in or entering or alighting from the aircraft. This policy coverage is available only if the policy includes passenger bodily injury liability.

Hull coverage

Hull refers to the body and machinery of the aircraft. Some policies provide open perils coverage both on ground and in flight whereas others restrict the open perils coverage to ground only. In flight policies do not cover crash or collision. They cover perils of fire, lightning or explosion in air.

In India the following are the important policies available in aviation insurance.

- Aircraft Hull and Spares All Risks Aviation Liability Insurance (Airlines)

This policy is best suited for scheduled airlines.

Covered Risks: Accidental physical loss or damage to the aircraft/aircraft spares, legal liability to third parties towards bodily injury/death and property damage, passenger(s) bodily injury/death baggage, cargo and mail. Premises, hanger keepers, catering and vehicle liability on airports also can be covered.

- **Aircraft Hull/Liability Insurance Policy**

This policy is meant for the owners/operators of smaller aircrafts used for private pleasure, training, industrial aid, business, commercial, offshore operations etc.

Covered risks: Accidental physical loss or damage to the aircraft. Bodily injury/ death of the passenger(s), loss of passenger's baggage and bodily injury/death and property damage to the third parties.

- **Aviation Fuelling/Refuelling Liability Insurance Policy**

This policy is meant for the suppliers of ATF (Aviation Turbine Fuel).

Covered risks: Legal liability to third parties arising out of injury/death and property damage.

- **Aviation personnel accident (Crew members)**

This policy is meant for pilots and other crew members.

Covered risks: Accidental bodily injury, disablement (temporary / permanent) and death. Policy operates worldwide.

- **Loss of license insurance**

This policy is meant for operating crew, pilots, co-pilots and flight engineers.

Covered risks: Suspension or termination of license due to disease, sickness or accident. Policy operates worldwide.

PERSONAL ACCIDENT INSURANCE

Personal accident insurance provides protection to the insured person financially, if he is injured. This policy provides monetary compensation in case of death or disablement resulting from accidental injury arising out of EXTERENAL, VIOLENT AND VISIBLE MEANS. Medical expenses incurred for treatment of injuries from such accident are also reimbursed to a certain extent on payment of additional premium. The policy also pays a pre-determined sum if death occurs as a result of an accident. All of us are exposed to the risk of accident, which is a threat to our financial security, and therefore it is prudent to have adequate personal accident cover to manage this contingency. For handling accident risks, personal accident policy, janata personal accident policy and gramin personal accident policies are available in India. Other personal accident policies are offered to particular groups like students, NRI's, women etc.

Scope of cover

Personal accident policy pays compensation to the insured in the event of happening of one or more of the following listed below which may be selected by insured at the time of taking policy:



- On death
- On permanent total and partial disability and
- On temporary total disability

In case of accidental death during the policy period, normally, the policy, in addition covers funeral expenses of the insured person. (some companies even provide removal of mortal remains). Permanent total disablement occurs when an individual is unable to perform his regular duties for the remaining part of his life. (loss of both eyes, upper limbs, lower limbs etc. are treated as total disability).

Table of Benefits

Sl. No.	Benefit Description	Table	Benefits Covered
1	Death only (100% of CSI)	I	I
2	Loss of two limbs or loss of one limb & loss of sight of one eye (100% of CSI)		
3	Loss of one limb or loss of sight of one eye (50% of CSI)		
4	Permanent Total Disablement from injuries other than named above (100% of CSI)	II	I to 4
5	Permanent Partial Disablement	III	I to 5
6	Temporary Total Disablement Weekly 1% of CSI upto 100 weeks (max. Rs. 5000/- per week)		

Additional benefits without additional premium

1. **Education Fund:** in case of death or permanent total disablement of the insured person due to accident, in addition to the compensation certain percentage of the sum insured is paid towards the education of the dependent children.
2. **Expenses for Carriage of dead body:** in case of the death of the insured away from his/her place of residence due to accident, such expenses for carriage of the dead body to the place of residence are paid upto 2% of the CSI subject to Rs. 2500/- maximum.
3. **Cumulative bonus:** at the time of renewal of the policy, in case of no claim having been reported under the earlier policy, then the policyholder is entitled to an increase in the compensation payable for death and permanent disablement by 5% each year up to a maximum of 50% of CSI.

The policy is effective for a period of one year from the payment of premium. The cover is operative on a 24 hours and worldwide basis.

When an individual is injured in an accident and as a result he is unable to perform his normal duties for a certain period we can describe it as temporary total disablement i.e. weekly benefits are paid @ 1% of sum insured). This policy can also be extended to reimburse the medical expenses due to accidents up to 10% of the insured amount or 25% of the claim amount or expenses incurred for treatment of the insured person whichever is less. (this can vary from insurer to insurer)

In 1989, a new clause was added to personal accident tariff (now all detariffed) namely education fund. According to this clause, in case of death or permanent total disablement of insured person, it provides additional compensation to the insured's children for their education. The dependent children should be below 23 years on the date of accident of insured person.

- If there is only one dependent child then 10% of CSI (Capital Sum Insured) and a maximum of Rs.5000.
- If there is more than one dependent child then 10% of CSI and a maximum of Rs.10,000/-.

The above compensation will be paid along with the capital sum insured to the dependent or the person who is entitled to receive the claim amount.

Personal accident insurance covers the following perils. The option is given to the insured to take cover for one or all of the risks. All accidents are covered subject to named exclusions of suicide, intentional self injury, nuclear, etc. are covered. Even a murder is an accident.

- Accidental injuries, drowning, poisoning
- Injured by snake bite, dog bite, etc.
- Accidents during transit
- Injuries while engaged in sports
- Injuries occurring in course of construction of buildings, offices etc.
- Accidental injuries due to slipping or collision

Personal accident policy does not cover injuries resulting out of war, self-inflicted injury, diseases or insanity, death due to war operations, attempted suicides, accidents in armed forces, aircraft accidents, accidents due to nuclear weapons etc.

Underwriting

Like life insurance policy, personal accident policy will pay the predetermined benefits or compensation if the accident occurs. This is an agreed value policy and not an



indemnity policy. So even in case of multiple policies, the claim can be made from all the policies. Only the underwriter has to be careful in not granting over insurance. It is a contract to pay benefits, which are fixed, but not a contract of indemnity. There is a condition in personal accident policy that if insured wants to take another similar policy he has to take written permission from the insurance company with which he is already insured. The financial position of the insured determines the insurance amount. If the insured reaps more benefits from the policy that places him in a better position than he was, it will force the insured to become intentionally disabled. So, it is necessary to take the insured's income into consideration and also the income he loses due to an accident. An acceptable limit has to be followed for additional expenses incurred by insured as a result of disablement. In temporary total disablement, the claim is limited to weekly earnings of insured.

Capital sum fixation

Capital Sum Insured (CSI) is the maximum amount the insured can claim from the insurer under the policy. The amount of capital sum insured under personal accident policies is fixed on the basis of income or salary. In order to fix the capital sum, the income levels of insured are categorised under first, second and third levels. These levels are applicable to those persons who undertake more than one policy. The policy issuing office should see that insured person's income is proportional to CSI. (The indicative limits are 75 times the monthly salary for table- i.e., death only / total permanent disability cover and 60 times for table-2 i.e., permanent partial disability and 36 / 25 times for table-3 i.e., weekly benefits.) The existing personal accident policies should be observed by policy issuing office so as to make sure that the sum mentioned at different levels are not exceeded. The personal accident policy will be applicable to those persons who possess good health (physical and also mental conditions).

Permanent disablement of any part of body is decided based on the capacity and utility of that particular part.

Premium Rates

Generally PA policies are issued to insured between age group of 5 yrs to 70 yrs and the upper age may be relaxed on merit. The premium rates of personal accident policy are fixed based on the nature of occupation of the insured. The occupations are classified into three categories. The Personal Accident risks are classified into three groups.

Risk Group – I: Accountants, Doctors, Lawyers, Architects, Consulting engineers, Teachers Bankers, Executives.

Risk Group – II: Builders, Contractors and Engineers engaged in superintending functions, veterinary doctors, paid drivers, garage and motor mechanics, machine operators, athletes, sportsmen, wood working mechanists, cash carrying employees.

Risk Group – III: Persons working in underground mines, explosive magazines workers involved in high tension supply electric installation, Jockeys, Circus personnel, persons engaged in hazardous sports activity.

Classification of Personal Accident Insurance

- Individual personal accident insurance
- Group personal accident insurance

Individual Personal Accident Insurance

An individual between 16 and 65 is eligible for this. This policy offers cover all through the year. This policy covers consequences of accidents such as death, permanent total disability and medical reimbursement. Under individual personal accident insurance, each individual should submit a standard proposal form with relevant information required by the insurers. Fresh forms will have to be given only after two renewals. Proposal forms should mention the income level and state of health of the insured. During the policy period, the capital sum fixed should not be changed or altered and the sum is fixed at the commencement of the policy. Rs.30 is the minimum premium amount charged under this policy.

The compensation will increase by 5% after every claim-free year during the currency of the policy and this cumulative bonus will not exceed more than 50% of the capital sum fixed. If the insured person is an employee in any organisation and if personal accident is restricted only to duty hours then the premium is reduced to 75%. In addition to these benefits, the policy will provide for medical expenses up to 10% of insured amount or 25% of claim amount whichever is less. This policy also reimburses the funeral expenses of the insured to the extent of 2% of sum insured or Rs.2500 whichever is less.

Group Personal Accident Insurance

Group Personal Accident policy covers a group of persons. The group discount is based in the size of the group. The group discount ranges from 5% to 30% depending on the size of the group. Any person irrespective of sex occupation, and profession in the age group of 10 to 70 years may be covered.

Group policies are categorised into two levels. A premium rate for this policy is fixed based on the category to which an individual belongs. First level consists of all named and unnamed employees of companies, industries, firms and associations and second level comprises of members of association, institution, society etc. In the first level, employer will decide the group of employees to be insured.

The minimum amount of premium to be paid under group policy is limited to Rs.100 (depends on the company's policy). Cumulative bonus is not allowed under group policies. The employer can take cover for his workers who may be injured by accidents



during the period of employment. Group discount is allowed only if number of individuals insured exceeds 25 (again depends on the insurer). Reimbursement of medical expenses will be the same as in the case of individual personal accident policy. For group policy exceeding 500 people, it is possible to customise the policy according to the requirements of the group.

In PA policies, the geographical area is worldwide.

OVERSEAS TRAVEL INSURANCE

Travel Insurance covers travel related accidents also. While travelling outside India, individuals face risks such as loss of baggage, accidents involving injuries, illnesses and medical emergencies requiring hospitalisation treatment. Unless adequate precautions are taken, these contingencies will pose serious consequences to the overseas traveller. A prudent person should therefore carefully examine the risks that he is exposed to and secure the required coverages before leaving his home country (many countries do not allow people without medical insurance).

In India, today, travel insurance has become popular among international travelers and their insurance requirements are met by the nationalised insurance companies as well as the new entrants into the General Insurance industry. Now let us take a look at the various coverages offered by the insurance companies of India to meet the requirements of the overseas travellers.

Coverage

The following are the coverages offered under travel insurance policies in India:

- Flight life Insurance, which covers only single flight and travel accident insurance.
- Lost baggage insurance, which provides security to valuable items carried during the trip. Insurer pays the value of the missing items.
- Overseas health insurance.
- Reimbursement of overseas medical expenses.
- Trip cancellation and interruption insurance provides for the huge non-refundable prepayments made when an individual is unable to take trip due to illness or any other emergency conditions.
- Delay in arrival of baggage.
- Delay in departure.
- Public liability at the foreign land.

Overseas Travel Insurance

Overseas travel insurance, provides protection against all risks while travelling abroad. Accidents and mishaps can happen anytime and at any place and therefore it is essential for an individual to identify the travel related risks in advance and insure these risks. Both private and public sectors insurers sell travel insurance products.

Example: When an individual on an overseas tour is hospitalised after an accident, the medical expenses would be so high that an average person cannot meet them. If he is insured under travel accident insurance, the insurer will reimburse the medical expenses up to policy limit.

Travel insurance products can also be purchased from travel agents or from tour operators wherever it is convenient. Today the importance of travel insurance is fully recognised and therefore it is often said that this product is purchased not sold. Types of travel insurance policies are Individual, Corporate frequent travelers, students, family.

All Risks

‘All risks policy’ as the name suggests does not cover all the losses or damages. ‘All risks’ insurance policy covers only those losses or damages, which arise due to fire or burglary or theft. It also covers losses due to accidental or unexpected circumstances. Since all risks policy covers a wide range of risks and perils, it is difficult for the insured to prove that he has incurred the loss.

This type of policy is especially suitable for valuables like jewellery, gold and silver articles, art and painting works, cameras, clocks, and other valuables. It is difficult in all risks policy to estimate the value of risks covered under the policy like art and paintings. In such case, the valuables are insured on value agreed by insured and insurer and claims are settled on this basis after deducting depreciation.

But the value of items like jewellery, gold and silver plates is calculated by consulting a professional appraiser. The policy can be limited to a single article or set of articles.

If inventory and valuation clause is included in the policy, then there is no need for insured to show the invoices and to prove cost. In this case, the claims are settled according to the values assessed by professional valuer and mentioned in the policy.



GOLFER'S INDEMNITY INSURANCE

While playing a sport like golf, if a person accidentally injures other persons, then he is responsible for the other person's injuries. Golf indemnity insurance provides protection against losses or damages to the golf players and to golf equipment. It also provides protection against public liability resulting in death or disability.

All golf players or sports persons can insure themselves under golfer insurance policy in order to protect their rights and interests as sports persons.

Coverages

The following risks are covered under golfer insurance:

- Any material damages to golf equipment while transporting the equipment, which includes breakage of golf clubs.
- Injury to third party who is not a family member or employee of insured person.
- If the insured is injured during the golf course in India, he is entitled to receive personal accident benefit up to Rs.25,000.

Exclusions

The golf indemnity insurance does not cover the following losses:

- Losses due to war or invasion, nuclear perils, riots.
- Damages due to earthquakes, floods etc.
- Loss or damage brought about by the insured either directly or indirectly.
- Any consequential losses, losses due to depreciation and wear and tear.

In India, National Insurance Company (NIC), Oriental Insurance Company (OIC), United India Insurance Company (UIIC) and New India Assurance Company (NIAC) and other private insurance companies, offer Golf insurance.

CRIME INSURANCE

Crime is one thing that all the countries in the world want to eliminate but are unsuccessful. Crime has also become one of the most serious problems of the recent times. Unfortunately crime is also the field that has received less than the required attention from the insurance companies. A study reveals that in US less than 10% of loss from the ordinary crime is insured. Imagine then, in a new market like India.

Looking at the grave necessity of crime insurance, U.S. federal government itself started extending burglary and robbery insurance.

There are two types of financial protection that are available against the losses caused by crime. They are fidelity and surety bonds and burglary, robbery and theft insurance.

Bonds and insurance are very much alike. A bond is a legal instrument in which a third person (surety) ensures the performance of a contract properly by the principal or the obligator. He does this by promising reimbursement of damages in case of default in the performance of the contract by the principal. For example, if a contractor is asked to deposit a bond by the owner of any building, it means the surety will pay the damages in case the contractor is not able to complete the project. Hence to a great extent bonds sound just like insurance. Yet it is not insurance. We will see the difference between insurance and bonds after going through them.

The classification of bonds and insurance is shown in the figure above. So in the coming section only the definitions of these terms are given.

Fidelity bonds deal with assurance of bonafide behaviour by an employee during the course of his employment. In fidelity bond, as the word itself suggests the surety assures the employer of trustworthiness and honesty of the employee and agrees to pay the damages that arise due to the dishonest acts of that employee.

If the fidelity bond is meant for a single individual, his name is mentioned in the bond and it is called individual bond. Whereas if the bond mentions a class and indemnifies the acts of all the employees falling in that class, it is called the schedule bond.

Surety bonds, also called the financial guarantee bonds, are the bonds in which the surety promises to make good any loss arising from the default of the principal in fulfilling his liabilities towards the obligee. The example of the contractor we cited in the beginning of the topic falls under this category. To be more specific, it is an example of the construction bond and the bid bond. In contract construction bond the contractor guarantees that the bidder will sign the contract if it is awarded to him at his bid.

Now let us go through the insurance covers available against crime. While reading them, think of the basic difference between the type of perils covered by them and those covered by the bonds.

Insurance cover is available basically for burglary, robbery and theft. It is necessary to see the meaning of each to differentiate them from one another.

When somebody forcefully enters the business premises and unlawfully takes any property, the act is called burglary. The 'forceful entry' is a prerequisite to burglary. Hence if a customer hides in the business premise until it closes, steals something and leaves without forcing the door or the windows to open, the act would not be considered a burglary.

Personal contact is a prerequisite for robbery. It covers the acts of unlawful taking of any property from any person by force, threat of force or violence. Therefore pick pocketing or the theft of luggage of a person while he was sleeping, would not be classified as robbery. Here the personal contact is there but the force, threat of force or violence is missing.



Theft is a wider term that includes all the crimes of stealing, whether or not covered by burglary or robbery. Acts like passing false cheques come under forgery.

Now that we have gone through the various crime bonds and the crime insurance covers, did you notice any difference between the perils covered by the bonds and the insurance? The bonds cover the losses that arise due to the dishonesty or incapacity of the person entrusted with some work, money or property, whereas, insurance covers the losses due to stealing or theft by strangers, the people who are not trusted by the work, money or property. The crimes committed by the insured, officers, employees or the directors of the insured do not come under the purview of burglary, robbery or theft i.e. they are not covered by crime insurance but by fidelity bonds.

This is the specific difference between fidelity bond and crime insurance. The general differences between a bond and insurance are as follows:

- In bonding, the surety does not expect the loss to actually happen and if the loss happens and he is required to pay for it, he reserves the right to recover it from the defaulting principal. Whereas the insurer is prepared to pay for the loss and works on the principal of spreading this loss over the group of insured people.
- The nature of risk is different, as we have seen in case of fidelity bonds and insurance. Usually, the matter covered by bonds is under the control of the insured and the losses covered by insurance are matters outside the control of the individual.
- The insurance contract is cancellable, usually, by either of the parties. The bonds cannot be cancellable until all the obligations of the principal are fulfilled.
- Insurance contract involves two parties, whereas bonds involve three.

BURGLARY INSURANCE

Burglary insurance is as common in business houses as fire insurance. It involves forceful and illegal entry into the business premises for the purpose of stealing. "Forceful entry" is the prerequisite for burglary. It is necessary to differentiate it from theft, robbery or housebreaking.

Robbery requires a forceful personal contact. It is an aggravated form of burglary where force is used against a person. Housebreaking is entering the house for the purpose of committing any crime. Six ways of entry that come under the purview of burglary have been listed in the Penal Code. Theft is a wider term and includes whatever is covered or not covered under burglary or robbery.

The other way to understand the scope of any policy is to look at what is not included in it. But before going through the exclusions let us get more acquainted with the policy.

Burglary insurance is not only for the goods owned by the person but also for the goods he is responsible for like those held in his trust. It also includes the relationship of bailment or agency regarding the goods.

Under burglary insurance, various types of schemes are available. The policy with wider cover excludes the items that are specifically covered under other policies. For example, if the jewels of a person are covered under jewellery and valuables policies and he avails all risk policy of burglary insurance; jewellery would not be covered under it.

Moral hazard is of special significance in burglary insurance, especially in the private dwellings policies. Fraudulent or exaggerated claims may be presented to the insurer to avail the benefits of the policy. The value of the property may be misrepresented to take advantage in the amount of premium charged. These things might happen in other insurance policies also but the burglary insurance is more susceptible to moral hazards.

The main policies available under the burglary insurance are:

- i) Burglary business premises insurance policies
 - ii) Burglary private dwellings insurance policies (theft covered)
 - iii) Combined fire and burglary insurance policies
 - iv) All risk insurance policies
 - v) Baggage insurance policies
 - vi) Jewellery and valuables insurance policies
- i) Burglary business premises insurance policies, that insures the stock-in-trade and other goods, can be issued on the basis of:
- Full value
 - i. Non declaration policies
 - ii. Declaration policies.
 - First loss
 - Inventory and valuation
 - Floating policies

Think over the terms and you can make out the difference. There are certain goods that can be stolen as a whole like jewellery or any small machine. But some goods like sulphur, rock phosphate etc. (bulk commodities) cannot be lost all at a time. Full value policies cover the former category of goods and the latter are covered by "first loss" policies.



In first loss basis policies, the maximum likely loss on one occasion is assessed (specified as percentage say 10% or 15% of full value) and insured. A notable feature of this type of policy is that the pro-rata condition of average is not applied, though the insurance is not for the full value. But in a sense the policy is not free of average, as in the event of the sum insured not measuring upto the stipulated percentage of full value of stocks held by the insured on the date of loss, average would still be applicable to the extent of the difference in percentage of the full value. This is known as the 'condition of partial average'.

In full value policies, the goods are insured for their full value. This includes the original cost price and overheads. The consideration of profit is not included. One thing noticeable here is that the level of inventory might not remain the same always. In goods like food grains, cash crops etc. the level of inventory varies greatly over a period of time. As the level of stock decreases, the loss that the burglary could cause would also decrease.

For goods whose inventory levels vary at different points of time, there is a 'declaration policy'. In declaration policies the maximum value of the stocks is estimated in the beginning. The insurance is based on this amount and premium is charged on 75% of this amount on provisional basis. Later the stock is valued and declared at the end of every month. At the termination of the policy period, the average stock during the year is calculated and the actual premium payable is arrived at. The difference between the premium payable and premium paid is then adjusted (paid or refunded) accordingly.

The declaration provides insurance cover at cheaper rates. A policy buyer needs to keep in mind the following points:

- In case the insurer fails to declare the stock for any month, the maximum value is taken as the stock value for that month.
- An alteration in the maximum value is possible only with the consent of both the parties.
- The condition of averages is applicable whereby the insurer pays only pro-rata loss, if the value on the date of the loss is in excess of the maximum value for which the cover is operative.

In non-declaration policies, the amount of inventory need not be declared every month and the premium is charged on the full value recorded in the proposal. If the full value of the stock changes, it can be given effect through endorsement by insurer.

The floating policies are meant for the situations when the stock lies in more than one location. The subject matter should be the same in all the locations and these locations must be within the same city, town or village. This policy cover is extended only to few well-known clients of the company.

For items like paintings, stamps, antiques, etc. sometimes the sentimental value is more than the intrinsic value. For such items, 'valued policy' is available. In this policy the insurance amount is decided in the beginning and whenever the loss occurs during the period of the policy, that value is paid to the insured. As the value of loss is not determined at the time of its occurrence it appears that the principle of indemnity is violated in valued policy. But some experts argue that the indemnity is decided in advance, instead of at the time of occurrence of damage. Hence the principle is followed.

We have seen that in valued policy the valuation of items is done beforehand. This removes the cumbersome procedure of establishing the value of the stolen property after the burglary. Otherwise being a contract of indemnity, burglary insurance requires the valuation of stock that is stolen. The insured needs to give evidence and produce invoices in order to establish his claim. This complication can be removed by adding an 'inventory and valuation' clause in the policy. The clause requires the valuation of inventory by experts in the beginning and the claim is settled on the basis of this valuation afterwards. This happens in valued policies too. However, the difference lies in the provision of depreciation and appreciation in the inventory and valuation clause. There is no such consideration in valued policy. Secondly the nature of subject matter also differs in the two policies.

Exclusions to burglary business premises insurance policy:

Besides the usual exclusions like war and allied risks, riots, wear and tear and consequential risks etc, the other noticeable exclusions are:

- Loss or damage in which the employee of the insured or any other person who can lawfully be present on the premises, is involved.
- Loss covered by fire and allied perils, motor or glass insurance policy.
- Loss or damage to deeds, bonds treasury notes, cash, medals, securities for money, cheques, unless they are otherwise included in the policy.

ii) Burglary private dwellings insurance policies

These policies, which are available to households require great care in execution. They are contracts of indemnity and establishing the value of the lost articles may become difficult due to a variety of reasons like the invoice not being available, the item may have been gifted with the donor dead or untraceable, or the owner might exaggerate the value because of personal attachment. Hence the surveyor needs to be very skilful to establish the claims.

The exclusions to the burglary private dwellings insurance policies are the same as those of business premises. Referring to the first exclusion mentioned in the burglary business premises policy, the person who can lawfully remain present within the premises include the tenant, lodger or any member of the insured family.



iii) All risk policies

We have a fair idea of all risk policies. The all risks insurance policies of burglary insurance provide protection against loss by burglary, housebreaking, theft, fire and allied perils. A few significant points about this policy are:

- If the premises were left vacant for more than 60 days in aggregate during the policy period, the benefits of the policy would not be provided.
- Similarly the insured property should not be shifted to other place or premises for more than 60 days in aggregate during the policy period.
- The value of any item should not exceed 5% of the total sum insured. This clause is not enforceable to furniture, and musical instruments like organ or piano.
- For items that are in pairs or sets, the claim will be paid in proportionate to the loss caused to the pair or set. The entire value of the set would not be awarded for damage to its part.

BAGGAGE INSURANCE

This policy covers the baggage carried during a journey and temporary stay in any hotel or rest house during the course of the journey. The cover includes apparels, wrist watches, fountain pens and other items but excludes articles like jewellery and valuables, cameras, opera glasses etc. the maximum sum that can be insured depends upon the insurance company's underwriting policy. Pilferage is not covered under this policy.

Claims

A separate department deals with the claims of the burglary insurance policy. As soon as the insured intimates information of burglary to the insurer, a bank claim form is sent to him along with the suggestion to file a police complaint, if not filed yet. The claim form is required to be filled and returned to the insurer within a week with the copy of FIR attached.

The claim form contains the details of the burglary. Examples: the description and value of property stolen, the details of the burglary and premises, the ownership of the property, other insurance policies covering the lost or damaged property, previous losses if any and the details of the notice to the police (if notice has not been given, the reasons for it).

After the claim form has been submitted a thorough investigation of the case is carried out by a professional claim investigator. They work in cooperation with the police and check various details like:

- The authenticity of the claim
- Whether the event that has caused the loss was an insured peril

- If the loss was excluded in the policy
- Whether the property was insured under the policy
- Whether the insured followed the conditions and warranties stated in the policy, etc.

A mere disappearance of articles does not constitute a valid claim. The article should not have been recovered even after bonafide search measures have been undertaken.

The amount to be awarded in the claim is arrived at after a proper valuation. The insured submits various evidences to establish the intrinsic value of the property lost.

Intrinsic value means that the profits on the insured items would not be included. Only the cost will be refunded.

The insurer reserves the right to reinstate, replace or repair the property instead of making the cash payment. Lastly if the loss exceeds the insured amount, the insured bears a rateable share of it. For example, if the stock in trade was insured for Rs.10, 000 with its actual value at Rs.20,000. and the loss occurs for Rs.4000, the insurer would pay only Rs. 2000 and the rest would be borne by the insured.

After the claim is settled, the rights and remedies of the insured against third parties will get transferred to the insurer. For instance, if any property is recovered from the burglar or any third party, the insurer will have the right to it. However this right of subrogation is restricted to the extent of loss indemnified by the insurer.

On payment of the claim, the amount of claim paid automatically reduces the sum insured, but it can be reinstated to the previous level by payment of additional premium. Generally, after settlement, the insurer suggests additional measures of safety to the insured on the basis of the experience of past burglary.

BANKERS' INDEMNITY INSURANCE

This is also referred to as bankers' blanket cover, and accordingly it provides insurance against fire perils, burglary, cash in transit, fidelity guarantee and marine insurance. This policy provides comprehensive insurance cover to the banking sector.

Coverage

This policy covers the direct losses of money and/or securities discovered during the period specified in the policy. More specifically, it covers the following losses:

Premises - By fire, riot and strike, burglary or house breaking or hold up resulting in loss to money/securities at the premises.

Transit - Lost, stolen, mislaid, misappropriated or made away either due to negligence or fraud of employees of the insured whilst in transit.

Forgery - Loss by bogus, fictitious or forged or raised cheque/drafts/FDRs or forged endorsements.



Dishonesty - Loss of money and/or operations due to dishonesty.

Hypothecated goods - By fraud and/or dishonesty or criminal act of the insured employees.

Registered postal sending - Loss of parcels by robbery, theft or by other causes to the parcels insured with the post office.

Appraisers - Infidelity or criminal acts by appraisers on the approved list.

Janata agents - Infidelity or criminal acts by Janata agents/Chhoti Bachat Yojana Agents/Pygmy collectors.

Meaning of terms used: “Money” includes bank notes (signed and unsigned), bullion, coins, currency, jewellery, ornaments, postage & revenue stamps (uncancelled) and stamp papers.

“Securities” include acceptances, air consignment notes, bank money orders, bills of exchange, bills of lading, bonds, CDs, certificates of shares/stock, cheques, coupons, debentures, DDs, express postal orders, FDR issued by the insured, lorry receipts, lottery tickets, postal receipts, promissory notes, railway receipts, time drafts and the like.

“Employee” refers to all existing types of employees and apprentices on the payroll of the bank at all of its offices. It excludes any director or partner other than those salaried.

Exclusions

These include losses due to:

1. Default of Director or partner of the insured other than salaried
2. War and allied risks
3. Acts of God
4. Incendiaries
5. Direct or indirect nuclear reactions
6. Acts of omission by the concerned employee after discovery of a loss in which the said employee was involved
7. Losses of money, securities or personal property of the insured, the nominal value and description of which have not been ascertained by the insured before loss
8. Trading losses, and
9. Losses sustained or discovered beyond the period specified in the policy.

Premium

The insured has to bear certain percentage of loss according to its type.

Points as in coverage listed above	% Loss borne by the insured
1,2 and 3	Flat excess
4, 5	25% subject to a minimum limit
6,7 and 8	25%

Special Reinstatement Clause

The bankers' indemnity insurance contains a special reinstatement clause that facilitates the automatic reinstatement of the sum insured each time a claim is paid. As this is a blanket policy, the claims might arise rather frequently. The clause saves time and effort needed to get the amount reinstated every time. An additional premium is charged for this facility that is paid indirectly in the form of deduction made from the claim amount.

The bankers might take the undue advantage of special reinstatement clause. As this clause reinstated the amount to the previous level, whenever it reduces, the bankers might purchase the policy of small amount. This is because the policy is not going to be exhausted anyway. That is why an upper limit has been put on the total policy amount (original amount + reinstated values or value of the claims paid). This limit is twice the sum originally insured. In case of liability insurance it is equal to the sum insured.

PLATE GLASS INSURANCE

Do not judge a book by its cover – the adage does not apply to marketing. In fact window dressing plays a vital role in marketing. The more the glasses, the bigger and better the shop. The glasses of the display windows and showcases of commercial establishments though are expensive. Plate glass insurance covers the damages caused to these glasses. However, it indemnifies only the actual breakage of glass. The policy does not cover superficial damages or scratches. Nor does it cover cracked or imperfect glass or loss arising from the interruption of the insured's business in the period between breakage and replacement.

The policy specifically indemnifies damages to glass, lettering or ornamentation described in the schedule caused by breakage or by accidental chemical spills or acids. The policy also covers repairer replacement of sashes or frames, boarding up or protecting windows in the event of unavoidable delay in replacements, and removal of fixtures or other obstructions to replace the glass. Policies may cover breakage of other than "regular" glass, such as neon signs, half-tone screens, memorial windows, glass bricks, and fluorescent lights. A rider is also available in return for a reduced premium giving the company the option to substitute two panes for one while replacing a plate of glass at least 100 feet square in size.



The policy excludes the following risks:

- Fire or explosion
- Earthquakes
- Riots, strikes, war and kindred risks

The policy considers the increase in the prices of glass. It also has a provision of automatic reinstatement each time the claim is paid. The insurer has the right of subrogation. But isn't useful as it is very difficult to trace the guilty. The insurer also has the right for salvage.

Prior to policy insurance, a company representative or an inspector from the cooperative inspection bureau inspects the designated glass.

The premium of the policy is decided on the basis:

- **Size:** This determines the cost of the glass and hence the expected loss when it is damaged. A table of premium rates is laid down in the standard form of policy on the basis of size.
- **Cost:** The policy considers the price fluctuations of glass.
- **Kind and use:** In the standard policy, only the rates of 'plain glass' are listed. In actuality other varieties of glass are also used viz., leaded glass, opaque glass and wired glass to name a few. The rates for these other types of glass are determined either by increasing the rates of plain glass by a few percentage points or doubling, tripling and so on.
- The first method of deciding the rates is called *valued basis* and the second is called the *multiplier basis*. Art glass, for example, is decided on a valued basis (applicable rate is 10% more than the standard rate). And so are Opalite and Argentine. Glass not set in frames, bent glass (applicable rate is 2-5 times the standard rate); interior glass, showcases etc are rated according to the multiplier model.
- **Location:** The location of the glass, obviously influences its exposure to risk. Display windows stand to face a higher risk than glass above the ground floor. These factors come into play while deciding the percentage of increase or decrease over the standard rates.
- **Type of occupancy:** Mercantile buildings form the majority of policyholders. Glass used in residences, churches, banks, office buildings etc are written at a discounted price against the premium charged on mercantile locations.
- **Territory:** This has a two-pronged influence on the premium. The cost of the glass includes the freight from the factory. Further, the risk of breakage is relatively higher in some territories. The risks differ between cities and the countryside and urban districts and the suburbs. Differentials in the form of percentage are given accordingly.

The insurer can settle the claim by cash payment or replacement. The liability of the insurer is limited to the amount stated in the policy. If any changes were made in the structure of the premises, the policy would cease to be effective. Similarly, any changes in occupancy, tenancy or business carried on in the premises render the policy ineffective.

Generally claims are settled on replacement basis. Insurers have got arrangements with manufacturers and suppliers of plate glass to replace the damaged plate glass at a discounted price.

FIDELITY GUARANTEE INSURANCE

Fidelity Guarantee Insurance (FGI) is a necessity in today's scenario, where each day new frauds are discovered. The necessity manifests itself in the insistence by the GOI and the State governments on their employees obtaining their policies. Fidelity Guarantee covers the employer against the direct pecuniary loss that may be caused to him due to dishonest employees in the course of employment.

Fidelity Guarantee insurance is non-tariff.

Three parties involved in the contract as against the usual two. Both the law of insurance and the suretyship are relevant in Fidelity Guarantee Insurance.

The popular policies of Fidelity Guarantee Insurance are as follows:

- **Individual policy** – where the behaviour of only one person is guaranteed. The individual's name is written in the policy.
- **Collective policy** – The behaviour of more than one individual (usually the whole staff) is indemnified in the single policy. The schedule of such a policy contains the names of all the individuals whose behaviour is guaranteed. The duties of the individual and the amount of guarantee for his behaviour are written along with each name. Additions and deletions of the names in the list (due to transfers, appointments, retirements, etc.) require the insurer's endorsement. .
- **Floating policy or the Floater** – The problem with the collective policy is the assignment of the amount of guarantee to each individual. It is difficult to estimate the amount of loss that an individual can create alone or with others. Moreover, fixing employees who are more likely to commit fraud may put the manager in dilemma. A floating policy provides the solution. In a floating policy, the guaranteed amount is not apportioned amongst the employees. Instead, it is floated over the whole group. If any individual, listed in the group commits fraud and a claim has to be paid, the guarantee amount is reduced unless reinstated or the policy is renewed.

The employer should be careful in fixing the total guaranteed amount. The amount should cover the maximum loss that can occur to the company due to individual or collective fraud.



- **Positions policy** – This policy is similar to a collective policy (actually an improvement over it). Instead of the names of the individual, the positions are listed in the policy with the duties and the amount guaranteed for their behaviour. The advantage of this policy is that it does not need to be reinstated if another replaces a person. Moreover, the amount guaranteed is usually associated with the positions and not the people. If the policy does not distribute the amount over different positions, but floats the single amount over all positions, it is floating policy.
- **Blanket policy** – As the name suggests, this policy covers the entire staff of an organisation. No name or position is shown in the policy. The policy is suitable for organisations with large staff.
- **Excess floating policy** – This is a mix of the floating and cumulative policies. The individual amounts are bundled with the names of each employee but for unforeseen to unusually big losses, an additional floating amount is fixed. That is why the policy is known as an excess floating policy.

In Fidelity Guarantee, an intangible thing is insured unlike other insurance policies. It is hence very difficult to assess the role involved. The value and risk involved can be assessed by physical examination of the property and security arrangements in fire policy, machinery policy, etc. In FGI (Fidelity Guarantee Insurance) various forms are required to be filled to estimate the trustworthiness of the employer.

- **Employers' form** – This forms the basis of contract between the employer and the insurer. It is similar to proposal forms in other policies
- **Applicants' form** – This is an important form to look into the moral hazard involved. The applicant fills the form and discloses the details of the extent of debts, private income, past employment and details of his life insurance policy and whether the applicant has ever been declared bankrupt or insolvent. Besides there are other general details like name, age, address, marital status, position in organisation, remuneration, etc.
- **Private referee's form** – The applicant names two persons who can be referred to verify his character. This is not very significant. The authenticity is doubtful, as the two people are the applicant's choice.
- **Previous employers form** – This is an important form, usually referred to while underwriting the policy. It contains the applicant's employment details for the previous 5 years and is filled by respective employers. The form also contains the reasons for the applicant leaving the previous jobs.
- **Collective proposals** – The employer fills this proposal form for collective, floating and blanket policies. Just as in the employers' form, he gives information about the whole group instead of the individual. He may categorise the people according to their responsibilities or work and give information about each category to ease his work.

The system of supervision and the enquiries made by the employer about the applicant before hiring are also contained in the proposal form.

The name of the employee leaving the organization is dropped from the policy. If he rejoins the organisation again, he is not automatically included in the list. He is treated as a new employee and all the formalities required to include a new employee in the list are carried out.

- The acts of dishonesty are covered, but loss due to inefficient accountancy, are not paid.
- Forgery, embezzlement, fraud

Other important terms related to FGI

- **Performance risk:** The performance of the work entrusted to the employee is guaranteed under this policy. If the employee does not carry out his responsibilities, the pecuniary losses suffered by the principal are reimbursed under this policy. This is more a branch of credit guarantee policy than FGI.
- **Service security policies:** When a new employee joins an organisation, the employer first spends money and time in training him suitably for the job. In return, the employee should give a minimum period of service. If he leaves before that, the expenditure on his training is futile. The organisation, hence, suffers. Service security policies cover such losses.
- **Counter Guarantee:** A counter guarantee is not required because of the principle of subrogation, so the insured executes this guarantee to the insurer.
- **Hazardous risks:** The following are considered as hazardous risks:
 - Collection agents whose financial limits are disproportionately high compared to their remuneration and the security deposit they give.
 - Jewellery travellers
 - Cashiers in eating houses, cinema houses and other places of entertainment
 - Estate agents
 - Treasurers of friendly societies or associations
 - Employees of bullion merchants

Different types of bonds are issued to indemnify the principal if the insured fails to discharge his duties. They are in the nature of guarantee or performance bonds though their scope is restricted and legally defined. Some examples are:

Court bonds: Liquidators, Receivers and Managers appointed by court of wards require these bonds since the court holds them liable if there is any lapse on their part in discharging their duties.



Custom bonds: Businessmen who are liable for payment of custom duty for their imported goods may store them in the bonded warehouses temporarily and give these bonds. They will pay duty when they finalise their transactions in the market. Similarly importers with export obligation also can offer these bonds till they fulfill their obligation.

Administration bonds: Bonds can also be issued for other administrative purposes in a variety of situations.

MONEY IN TRANSIT INSURANCE

Money shall mean and include Cash, Bank drafts, currency notes, cheques, postal orders and Current Postage stamps. The policy is divided into two sections:

Section – I

This section provides for loss of money in transit by the insured or insured's authorized employees occasioned by Robbery, Theft, and any other fortuitous cause. Money is differentiated into three categories:

- a. Money for Wages/ Salaries/ Petty cash in transit from bank to premises till paid out or otherwise kept in locked safe/strong room on the premises.
- b. Money other than (a) in the personal custody of the Insured/ employees while in transit between premises and bank/post office.
- c. Money other than (a) and (b) collected by Insured/employees during collection round upto 48 hours from collection.

Section – II

This section covers money loss by Burglary, Housebreaking, Robbery or Hold up whilst retained at Insured's premises in safe(s) or strong room.

The underwriting factors for premium calculation for this policy include maximum distance and areas through which the money will be passing, how it is to be carried, mode of transit, whether accompanied by armed guards, number of persons carrying money, the maximum amount carried at any one time. The estimates annual carryings form the basis of premium.

Exclusions

The policy does not cover the loss or damage in respect of:

- a) Shortage due to error or omission.
- b) Loss of money entrusted to any person other than the insured or an authorized employee of the insured.

- c) Loss of money where the insured or his employee is involved(except loss due to fraud or dishonesty of the cash carrying employee occurring whilst in transit and discovered within 48 hours).
- d) Loss occurring in the premises after the business hours unless the money is kept in the locked safe or strong room.
- e) Loss occasioned by riot, strike and terrorist activity.
- f) Theft of money from unattended vehicle.
- g) Loss of money from the safe by use of original keys to the safe or any duplicate there of belonging to the insured (unless such leys are obtained by force or threat).
- h) War
- i) Loss due to ionizing radiations, radio active contamination, nuclear weapons material.
- j) Consequential loss or legal liability of any kind.

However, on payment of extra premium, the policy can be extended to cover Riot & Strike.

JEWELLERS' BLOCK INSURANCE

The Jewellers Block insurance is a package policy devised to cater to the needs of the jewelers.

Policy Coverage: This policy is divided into 4 sections.

Section – I

This section covers loss or damage to property whilst contained in the premises where the insured's business is carried on/or at other premises where the insured property is deposited by fire, explosion, lighting, burglary, housebreaking, theft, riot and strike, hold-up, robbery, and Malicious damage only. Property kept in the bank lockers can also be covered provided separate register is maintained to record all deposits/withdrawals from the locker.

Section – II

This section covers loss or damage to property insured carried outside the specified premises for the purpose of insured's business by any cause whatsoever, except the causes excluded specially.



Section – III

This section covers loss or damage to the property insured by any cause whatsoever, except those specifically, whilst in transit in India by:

1. Insured Post parcel
2. Air Freight
3. Angadia

Section – IV

This section covers loss or damage to office furniture, fixture, fittings, and the property being used in connection with the insured's business by Fire, Explosion, Lightning, Burglary, Hold-up, Robbery, Housebreaking, and Theft only. Air conditioners, refrigerators, generators, closed circuit TV can be also covered under this section.

The policy also covers damage done by burglars and /or thieves to the premises and or landlord's furniture and fixtures for which the insured is legally responsible as tenant and such indemnity would be subject to a maximum of 1% of the sum insured under section IV.

The risks are classified as under

Class – I: Having 24 hours watchman for the premises employed by the insured

Class – II: Common watchman for 24 hours for the Building or separate night watchman for insured premises

Class – III: All others

The policy can also be extended to cover perils like earthquake, and STFI perils by charging additional premiums.

HORSE / DONKEY / MULE / PONY INSURANCE

These are some of the animal policies which are commonly taken to take care for the well being of the animals

The eligible age of the animals for insurance coverage is 2-8 years. The policy essentially covers death due to accident, or disease contracted/occurring during the policy period. Some of the exclusions include:

- Pleuro pneumonia
- Haemorrhagic septicaemia
- Anthrax and foot & mouth disease
- Theiliasis

- Pleuropneumonia
- Total or partial disability
- 15 days waiting period for diseases in respect of non-scheme animals
- Overloading, unskillful treatment or use for purpose other than stated in the policy

However, diseases like Canine Distemper, Hepatitis, Leptospirosis, and Rabies will be covered only when proper vaccination or immunization is given.

KIDNAP & RANSUM INSURANCE

Kidnap and Ransom Insurance or K&R Insurance is designed to protect individuals and corporations operating in high-risk areas around the world, such as Colombia and Peru. K&R insurance policies typically cover the perils of kidnap, extortion, wrongful detention and hijacking.

K&R policies are Indemnity policies – they reimburse a loss incurred by the insured. The policies do not pay ransoms on the behalf of the insured. The insured must first pay the ransom, thus incurring the loss, and then seek reimbursement under the policy. Losses typically reimbursed by K&R policies are ransom payments, Loss of Ransom-in-transit and additional expenses, such as medical expenses. The policies also typically indemnify Personal Accident losses caused by a Kidnap. These include Death, Dismemberment, and Permanent Total Disablement of a kidnapped person. They also typically pay for the Fees and Expenses of Crisis Management Consultants. These consultants provide advice to the insured on how to best respond to the incident. Policies typically require clients to restrict the knowledge of the existence of the coverage. The policies may be written to cover families and corporations. Some policies include kidnap prevention training.

Kidnap, Ransom and Extortion insurance provides numerous benefits and services to the applicant and the insured. Kidnap, Ransom & Extortion Insurance provides coverage for kidnappings and other events through a combination of financial indemnification and expert crisis management.

A basic policy can cover items such as ransom payment, loss of income, interest on bank loans and medical/psychiatric care. Besides insurance, companies can also utilize crisis management teams and employee training in what to do in a hostage situation to minimize losses due to kidnap or ransom. The Kidnap, Ransom and Extortion insurance covers named employees for individual or aggregate amounts, with deductibles requiring the insured to participate in about 10% of any loss. Kidnap and Ransom insurance plans provide assistance to the family and business with regard to independent investigations, negotiations, arrangement and delivery of funds, and numerous other services vital to a safe, speedy and satisfactory resolution. Generally extortionists do not discriminate. Any company of any size can be a target for extortion



threats against the company and its employees. People tend to associate business extortion and kidnapping with global companies. The fact is radical groups and criminals exist everywhere.

Kidnap, Ransom and Extortion Insurance in such situations helps to manage the costs associated with an extortion threat against products, proprietary information, computer system or employees that can push a small to medium-sized company to its financial limits. These risks may not look like everyday exposures, but too often they are. And when they happen, one may need financial assistance to meet extortion demands and the extensive costs associated with negotiation and recovery. Due to globalization of economies, multinational companies need to prepare for the possibility of attacks on their employees and facilities virtually anywhere in the world.

PACKAGE POLICIES

Package insurance policies are developed for individuals and business establishments to meet their insurance requirements under a SINGLE SIMPLIFIED PACKAGE. These policies contain generally more than five sections out of which some are compulsory sections and the policyholder may opt other sections in addition to the basic sections.

Two such policies are discussed in detail.

1. HOUSEHOLDERS INSURANCE

This is a comprehensive package policy designed to meet the insurance requirements of a householder. The main advantage of this policy is the wide coverage and discounts available upto 20% of the premium.

Section	Cover	Perils covered	Premium (Per mille)
I	Fire a) Building b) Contents	Fire, Lightning, Domestic gas explosion, Aircraft damage, RSMTD, STFI, EQ, Subsidence/Landslide, Impact damage, Bursting of Tanks/ pipes	0.50
II	Burglary & Housebreaking	Burglary, Housebreaking, Theft and Larceny	2.40
III	All Risks – Jewellery and Valuables	Accident and Misfortune	10.00
IV	Plate Glass	Accidental Breakage	10.00

V	Breakdown of Domestic Appliances	Mechanical or electrical Breakdown	2.50
VI	TV/VCR/VCP Personal Computer	Mechanical or electrical breakdown + Fire group of perils as per Section-I + Burglary/Housebreaking/ Theft + Legal Liability (Rs.25000)	10.00
VII	Pedal Cycle	Fire / Lightning / external explosion/ RSMTD/ STFI/ EQ + Burglary, Housebreaking, Theft & Legal Liability up to Rs.10,000/-	20.00
VIII	Baggage	Accident or Misfortune while on tour/ holiday anywhere in India	7.50
IX	Personal Accident	Death / Loss of Limbs/ PTD/ PPD/TTD (maximum Rs.1000/- per week)	As per guide rates
X	Public Liability	a) Third Party Liability b) W.C. Liability for domestic servants	0.50 as per tariff

Note: the premium rates have been given as examples. In the detariffed scenario, the companies have the freedom to fix their premiums based on their claims experience.

2. SHOPKEEPERS PACKAGE INSURANCE POLICY

Section	Cover	Perils covered	Premium (Per mille)
I	Fire a) Building b) Content Note: TSI under items A&B should not exceed Rs. 10,00,00,000/.	Fire, Lightning, domestic gas explosion, Aircraft damage, RSMTD, STFI, EQ, Subsidence/Landslide, Impact damage, Bursting of Tanks	2.55
II	Burglary & Housebreaking Contents (Value equivalent to I (b))	Theft following violent and forcible entry and exit.	2.55



III	Money Insurance a) In Transit (max Rs.1,00,000/-) single carrying b) In Safe (max 2% of sec I. SI or Rs.100,000/ w.e.I c) In Till/ Counter (max 1% of section I SI or Rs.50,000/- w.e.I	Accident and Misfortune	2.55
IV	Pedal Cycle	Fire / Lightning / external explosion/RSMTD/ STFI/ EQ + Burglary, Housebreaking, Theft & Legal Liability up to Rs.10000/-	20.05
V	Plate Glass (10% of the sum insured under section I or Rs.5,00,000/- which ever is less)	Accidental Breakage	10.05
VI	Neon Sign / Glow Sign (max 2% of section I or Rs.2,00,000/- w.e.I	Accidental external means, Fire, Lightning, external explosion, Theft of sign board, RSMDT, STFI	10.05
VII	Baggage (max 2% of section I SI or Rs. 20,000/- w.e.I)	Accident or Misfortune	7.55
VIII	Personal Accident (Age Group between 12-70 years)	Bodily injury due to accidental, external, violent and visible means	As per guide rates
IX	Fidelity Guarantee (10% of section I SI or Rs. 10,00,000/-w.e.I	Fraud and Dishonesty of salaried employees	10
X	Public Liability Insurance (5% of the Section I SI or Rs. 5,00,000/- w.e.I	a) Public Liability b) W.C. Liability	0.50 as per WC Tariff

Note: the premium rates have been given as examples. In the detariffed scenario, the companies have the freedom to fix their premiums based on their claims experience.

Policyholder has to choose the sections he wants. Section I (b) and Section II are compulsory. Minimum 2 sections, apart from the compulsory sections are to be taken to avail of the policy

Group Discount in Premium is as follows:

- a) Where proposer opts for more than 4 sections: 15% discount on non-tariff premium
- b) Where proposer opts for more than 4 sections: 15% discount on non-tariff premium

Questions



1. How does the need for fidelity guarantee insurance arise?
2. Define the term burglary and house breaking in the context of burglary insurance.
3. Explain why there is a need for companies to secure a directors and officers liability insurance?
4. Against what contingencies do broker indemnity policy provide cover?
5. What losses are normally covered under plate glass insurance?

CHAPTER – 9

LIABILITY INSURANCE

OUTLINE OF THE CHAPTER

- Introduction
- Historical background and evolution of Liability insurance
- Fundamental principles governing Liability insurance policies
- Scope of Liability insurance policies
- Questions

LEARNING OBJECTIVES

- To understand the concept of liability insurance under the Law of torts
- To study the scope of risk coverage available under liability insurance for industrial and non-industrial risks
- To define the liability for professionals in their professional commitments
- To evaluate the scope of Directors and Officers liability for corporate losses

INTRODUCTION

Liability Insurance, of late in India, is visibly making a mark in the corporate sector as well as in other sectors. In the Western countries, liability insurance is very popular and commonly opted by individuals as well as professionals and corporate institutions. The liability generally arises out of negligence or breach of duty.

The purpose of Liability insurance is to provide indemnity to the insured in respect of financial consequences of legal liability. Whenever liability arises under Civil Law, compensation (damages) becomes payable. Besides this, there may be legal costs awarded against the insured and also legal costs of defence of the claim incurred by the insured.

Civil Liability may arise under the

- Law of Tort** – Due to negligence, bodily injuries and/or damage to the property of third parties may be caused for which damages become payable.

- ii. **Statutory law** – liability to pay for relief for personal injuries and/ or damage to property of third parties under any statutory laws or acts.
- iii. **Law of contract** – liabilities arising in the discharge of professional duties due to negligence.

Liability arises mainly under the Law of Torts. Tort means ‘Civil Wrong’ arising out of a breach of duty, for which damages are recoverable under law. Tort takes numerous forms, such as libel, slander, etc.

Negligence is also the reason for the liability loss exposures. In simple words, negligence means “absence of care”. Negligence can be established when the following conditions are satisfied:

- a) Existence of duty of care towards the injured party
- b) Breach of that duty
- c) Injury or damage as a consequence of the breach
- d) Casual connection between the breach of duty and injury or damage

Damages

In all liability claims the compensation that is awarded through the judiciary procedures is called as damages. The term ‘damages’ means the pecuniary compensation awarded by a court of law for breach of contract or for tort.

Damages for personal injury (fatal or non-fatal) claims fall into two categories:

- a) Special Damages - These relate to:
 - i. actual loss of earnings
 - ii. medical, nursing or other expenses
 - iii. funeral expenses
- b) General Damages - These comprise damages for:
 - i. pain, suffering and distress
 - ii. loss of enjoyment of life and loss of amenities
 - iii. loss of recreational ability
 - iv. loss of reduced expectation of life
 - v. prospective loss of income
 - vi. future medical expense
 - vii. loss of opportunity in the job market



HISTORICAL BACKGROUND AND EVOLUTION OF LIABILITY INSURANCE

Public Liability insurance originated in the U.K. in 1875, when the first policy was issued to cover TPL arising out of the use of horse driven carriages, later for lifts, boilers, building contracts etc. The Employers' Liability insurance was a result of the Employers' Liability Act, 1880 and Workmen's Compensation Act, 1897. The Products' liability insurance can be traced to the early 20th century, when public liability covers were extended to cover ' food and drink' risks, 'dermatitis' risks, etc. The National Insurance (Industrial injuries) Act, 1946, introduced a social insurance scheme for industrial accidents and diseases. In India the ESI Act and WC Act cover the same

FUNDAMENTAL PRINCIPLES

These liability policies are also basically governed by all the fundamental principles of insurance contracts such as:

- **Insurable Interest:** insured has insurable interest in the financial loss that arises when he has to pay damages under the law.
- **Indemnity:** the policy will indemnify the insured to the extent of damages and costs awarded, and legal costs incurred, subject to limits of liability (AOA; AOY).
- **Subrogation:** rights are transferable to insurer.
- **Contribution:** all insurers pay ratable share of loss.
- **Utmost Good Faith:** insured to disclose all material facts.

Let us now discuss in detail some of the important liability policies.

SCOPE OF LIABILITY INSURANCE POLICIES

Liability insurance mainly comprises the following policies:

- i. Personal Liability insurance
- ii. Policy under the Public Liability Act, 1991
- iii. Public Liability for industrial and non-industrial risks
- iv. Products liability
- v. Professional indemnities for Doctors and Solicitors etc.
- vi. Employers Liability (Workmen's Compensation policy)
- vii. Directors and Officers' Liability policy

The Policies I to IV are covered under Market Agreements, having same clauses, exclusions, and conditions. The Policy V is a Tariff class of business and the Policy VI is a non-tariff policy.

Liability insurance covers are granted as a part policy cover in other insurance policies such as in Motor insurance policy, Marine hull, and Aviation insurance and also in Householders' and shopkeepers comprehensive policies. Extensions of liability cover are also available under material damage policies such as in Contractors' All Risks policy, Erection All risks policy and in Boiler Explosion, which come under the broader title of engineering insurance policies.

Let us discuss some of the policies in detail.

i) Personal Liability Insurance

Personal liability insurance provides protection against the legal liability, which arises due to insured's personal acts. The insurance company will pay for legal defence to third party damages or injuries up to policy limit. Except legal liability, which arises due to automobile accidents and professional liability, most other personal acts are covered under personal liability insurance.

The personal liability insurance covers damages caused to properties and injuries to other people due to the negligence of the insured.

Under this policy, the insurance company is bound to defend the insured should the matter go to court of law. It can also settle the matter out of court by negotiating with parties for a settlement within the policy limit. Personal liability policy offers very wide coverage.

The following instances of loss, damages or injuries caused by an insured individual come under the purview of personal liability insurance in which coverage will be available up to the policy limit.

- Accidental fire to neighbours house as a result of insured's negligence
- Accidental injury to a third party while playing
- Damaging costly antique accidentally belonging to neighbour
- Injuring another person while riding a bicycle.

ii) Public Liability Insurance for – Industrial Risks

This policy is mainly for all industrial units exposed to liability arising out of accidents during the course of their business operations.

As the prevailing public law is stringent and the courts are awarding huge sums arising out of liabilities, it is prudent to take such an insurance cover even in cases where it is not mandatory.



The main benefits of the policy are -

1. The following additional covers can also be obtained
 - (a) Pollution risks: caused by a sudden, unintended and unexpected cause which takes place at a specific time and place during the policy period.
 - (b) Transportation risks: outside the premises arising out of an accident directly caused by dangerous materials or hazardous substances while being transported by rail, road, or pipeline.
 - (c) Cover for multiple units: Non manufacturing premises of the insured such as offices, depots, go-downs etc. located at different places, incidental to insured's business activities can be covered.
 - (d) Technical collaborators liability: This can be included in the main policy subject to reinsurer's approval.
2. Discounts are offered for opting for higher excess.

How does the Policy Work?

1. This policy indemnifies against amounts one is legally liable to pay as damages to the third party victims of an accident which include:
 - (a) Compensation for accidental death, bodily injury or disease to third parties.
 - (b) Damage to or loss of property belonging to third parties arising out of an accident, including legal costs incurred with the prior consent of the insurer.
 - (c) Legal and civil liabilities of the directors and officers of the company.
2. Policy covers all amounts one is legally liable to pay the third party during the policy period including legal costs and expenses subject to the limit of indemnity terms and conditions of the policy.
3. Policy cannot be issued for unlimited liability.

This policy is suitable for all industrial units exposed to liability arising out of accidents during the course of their business operations.

Premium

- Premium rates are fixed for the four hazard groups classified.
- Premium payable further depends on the limit of liability and annual anticipated turnover.
- Insurance companies at their discretion may permit mid term increase/decrease in the limit of indemnity during the policy period.
- All policies subject to a minimum excess which is applied on the limit of indemnity per any one accident.
- Discounts are offered for opting for higher excess.

The Public Liability Act, 1991: The Policy

As a follow up of Environment Protection Act of 1986, Public liability Insurance is mandatory in respect to those who handle hazardous substances by virtue of Public Liability Insurance Act of 1991. The names of hazardous substances and the quantity of each, is listed in the 'Act' and the quantity of the substance can be as low as one kilogram for Act purposes.

How does the Policy Work?

1. It is a modified version of public liability (Industrial) policy and the term 'handling' is wide enough to include baileys or any other intermediaries and transport operators. The transport operators who transport substances like liquefied petroleum Gas, certain acids, hexane and other toxic substances are required to compulsorily obtain Public liability policy.
2. The policy benefits will accrue only to third parties who may suffer personal injury or damage to their property as a direct result of handling of the 'hazardous' substances.
3. Courts can pass awards against insurance companies direct as privities is created by the compulsory insurance policy.
4. The sum insured is based on annual turnover of those handling the substances, with a minimum sum fixed by the act at Rs. 3 crores. The annual freight receipts of a transport operator would be their limit.
5. The Act also provides and therefore enshrined in MV Act, that the drivers operating road vehicles carrying the 'hazardous substances' have to possess a special endorsement on their driving license.
6. If there is any short fall between the award of a Court and the claim payable under the policy, same is met out of Environment Protection Fund maintained by the Central Govt.

The insurance is compulsory. Heavy penalties are imposed, which includes prosecution, for violation of the Act provisions. The compensation payable for bodily injury or property damage is based on the capacity of the parties to pay compensation.

If however there is any short fall between the award of a Court and the claim payable under the policy, the same is met out of Environment protection fund maintained by Central Govt.

The transport operators who transport substances like liquefied petroleum gas, certain acids, hexane and other toxic substances are required to compulsorily obtain Public liability policy.



Premium

The rate of premium is based on annual turnover of an industry to that of sum insured selected, as provided for in the Act. In addition to the gross premium arrived at, as above, the proposing party is required to contribute equal amount towards environment protection fund maintained by the Central Government. The fund is collected along with the premium and remitted to the Central Government. While the premium element is subject to Service tax, the fund do not.

iii) Product Liability Insurance

Product Liability commonly arises out of

1. Tort or common law
2. Statutory law – quite often it is absolute or no fault liability
3. Contract

The risk associated with insurance does not end with production. It is a phenomenon that continues even after the production. Thus if a third party gets injured because of the insured's product, the producer or the manufacturer would be liable to pay the damages.

Product liability insurance covers the damages arising in such cases. And the damages arising or the compensation that is required to be paid in such case is huge. Hence all the industries that are exposed to such risks should go for product liability insurance cover, even if it is not mandatory for them to avail this cover.

Inclusions and Exclusions

The product liability insurance covers all the damages that may arise due to the defects in the product. It includes accidental death or disease or injury caused to the third party due to any defect in the product.

If the domestic sales of the manufacturer are insured then the exports can also be covered. That is, if a manufacturer sells his goods both in the domestic as well as the foreign market, he cannot insure only the exports.

Vendor's liability extension and technical collaborator's liability can be included in the policy on payment of additional premium. Similarly, products manufactured by sub-contractors / licensed manufacturers under their own brand name can also be covered under the same policy.

Premium

To charge the premium according to the risk associated with the products and the size of the damage that might arise from their being defective, the industries are classified into seven groups. The rate to be applied on the annual gross turnover is specified for each group.

For exports, additional premium is charged based on total exports turnover to each country.

All policies are subject to a minimum excess of Rs. 2000 or ½% of limit indemnity per any one accident (except for exports to USA/Canada which have double these limits).

All extensions carry additional rates. For the policies involving large sums, discounts are offered.

Benefits

The policy covers all the claims arising out of accidents, injury, diseases or pollution due to defects in the product covered under the policy during the policy period.

The employees of the insured are also covered under the policy. Indemnity is also extended to officers, committees and members of insured's welfare associations and personal representatives of the estate.

The policy covers all the incidental expenses like costs, fees and expenses incurred in investigation, defence and settlement of claim made against the insured, cost of representation at any inquiry or other proceedings in respect of matters that have direct relevance to the claim made against the insured. But the amount should not exceed the overall limit stated in the policy.

Covered Risks

The policy pays for all the claims that arise out of the acts and/or omissions committed during the policy period. The claims must be first made in writing during the policy period itself. The claim also covers legal costs and expenses incurred, with the prior consent of insurer and subject to the limits of indemnity.

Major exclusions

- Criminal act or violation of law or ordinance
- Services rendered while under the influence of intoxicants or narcotics.

iv) Professional Indemnity Insurance

We have gone through the various insurance covers available to producers. Besides production, another industry that is significant is the service industry. And the service industry faces no lesser risk. The counterpart of the product liability insurance in the service industry is the professional indemnity insurance. As the product liability cover provides protection against liabilities that may arise due to the product, professional indemnity insurance covers the professionals against all the liabilities that may arise due to the negligence or failure in providing the service. That is why this policy is also called Errors and Omissions Insurance (E&O Insurance) or malpractice insurance.



Professional liability insurance is an important insurance cover. In certain cases like physicians or surgeons, it benefits not only the insured but also the client. In the absence of such insurance cover surgeons fearing liability arising from failure of treatment would have refused very critical cases. This means that the doctor would not be available when he is required the most.

Initially the policy was designed for professionals like doctors, lawyers, architects or engineers but now the policy is widening its scope to accommodate emerging professions. The policy now includes various professions like psychiatrists, marketing or technology consultants, software designers, environmental consultants, insurance agents, brokers etc.

The professional liability insurance differs from other liability insurance policies in a few ways. These are as follows:

1. Usually only one major insuring clause is written under professional liability insurance. And no distinction is made between bodily injury and property damage liability. There is usually a maximum limit for each claim, but there is no limit per occurrence. Consider a situation where the claim limit in the policy is \$1 million and the aggregate limit \$4 million and the patient as well as his family claims damages for the same error. The maximum that would be paid for the claims would be \$2 million. The other liability insurance policies usually specify the 'per occurrence limit' as well.
2. Professional liability insurance is not restricted to accidental acts: faulty diagnosis or faulty performance is also covered. Deliberate acts giving unintended results are also covered in the policy. But illegal and criminal acts are not covered.
3. Professional liability policies usually cover the damage caused to the property in the custody or care of the insured as well.
4. The professional liability policy usually excludes the agreement guaranteeing the results. For example, if a surgeon guarantees the success of an operation and fails, the liability arising on account of it would not be covered in the policy. This is particularly in contrast to the product liability policies that cover the claims arising out of the breach of warranty. For example, if a shopkeeper says the product is good for a certain purpose and the product causes any harm during use, the claims arising would be covered by the product liability policy.
5. In professional liability insurance an extended reporting period endorsement is usually added. This signifies that the claims for errors committed during the term of the policy will be covered even if claims are made after the termination of the period of the policy.
6. Professional liability insurance does not allow the settlement of the claim without the prior approval of the insured. The consent to pay the claim is equivalent to

admission of guilt for the professionals that might affect their reputation. Hence a professional might insist on the insurer to defend the suit even if the insurer finds it less expensive to pay the claim. The new policies however do not retain this restriction, as they believe that few suits do not affect the reputation of established professionals.

The professional liability insurance provides a broad coverage including all the liabilities that may arise due to error of omission in rendering the service by the insurer or any of his/her employee (however a nurse is not included as an insured in the medical liability policy). But it cannot substitute the general liability insurance as it covers only the acts that come under the purview of professional service. Other things causing the damage are not covered in this policy. For example, injury caused to a patient from the furniture in the doctor's clinic would not be covered by the professional liability policy.

The professional liability insurance policy for doctors and chartered accountants is discussed in brief.

Professional Indemnity Policy for Doctors and Medical Practitioners

This policy is for the doctors who are registered with the IMA (Indian Medical Association). All acts of the insured that results in any legal liability to the third party will be indemnified in the policy.

- ❑ The acts of qualified assistants and employees of the insured who are named in the policy are also covered in the policy
- ❑ The acts of qualified assistants and employees of the insured who are named in the policy are also covered in the policy
- ❑ The claims should relate to the acts or omissions committed during the period of the policy
- ❑ The limit of the indemnity granted under the policy for Any One Accident (AOA) Any One Year (AOY) (per accident per policy year) will be identical
- ❑ No short period policies are permitted
- ❑ All claims for compensation must be legally established in a court of law. Jurisdiction applicable will be Indian courts.

The medical practitioners are classified into 21 categories under this policy. The last category is an open category for other practitioners.

Major exclusions

Criminal acts, services rendered under the influence of intoxicants or narcotics, third party public liability, claims under cosmetic plastic surgery, hair transplants, punch grafts, flap rotations, etc.



Even judges are not above the law

Today when we talk about professional liability insurance we have in mind, physicians, surgeons, lawyers, engineers and even accountants. But do you know even brokers and agents have been charged in US, Canada and other countries for what has now come to be termed as 'malpractice for acts of commission and omission'. Here is some more news on the subject. In the US, in 1984 a Virginia Judge was convicted for putting behind the bars two persons for a non-jailable offence. Later the US Supreme Court also held that judges were liable in such cases. Now you have judicial malpractice insurance that does not come cheap – only \$800 for coverage for a million dollar.

Professional Indemnity Errors & Omissions Insurance for Chartered Accountants/ Financial Accountants/ Management Consultants/ Lawyers/ Advocates/ Solicitors/ Counsels

Just like the policy for doctors and medical practitioners, this policy indemnifies errors and/or omissions while rendering services by accountants/lawyers as well as their partners and employees named in the policy. These include chartered accountants, financial accountants, management consultants, advocates, solicitors or counsels, insurance brokers and agents.

In normal course all claims for compensation have to be legally established in a court of law.

v) Directors and Officers Insurance – Scope and Future

Though Directors' and Officers' (D&O) liability insurance has been in existence for ages, it has come into the fore only in the past few years. Today's business scenario is characterised by extreme volatility and a slew of big-ticket litigation fiascos like Enron and Tyco. The onus of protecting the interests of shareholders and customers is thus on the directors and officers. They are also answerable to employees and creditors of the firm, not to mention the government and other regulatory bodies.

Directors and Officers are exposed to potential risks that might come in the form of:

- Misrepresentation of the firm's financial status
- Lack of diligence and failure of supervision
- Conflicts of interest
- Imprudent decisions and
- Mismanagement of funds

The risk of claims is accentuated in case of a merger, acquisition, takeover or liquidation. Directors especially in banking institutions have been held individually responsible by the institution, shareholders and regulatory authorities.

D&O insurance was construed as 'sleep insurance'. It enables the directors to work peacefully with the knowledge that somebody else will take care of the losses in case the company fails to fulfill all its obligations. It offers a broad protection to the insured. Though not mandatory, most of the top corporations in the west purchase D&O insurance.

Liabilities covered under D&O Insurance

Every insurer has his own proposal form, agreement conditions and list of exclusions. There is no fixed standard. Therefore, directors should have a clear understanding of coverage items that are most relevant to their profile and responsibilities. They should ensure that the policy addresses their needs adequately. It is important that the director gets in touch with the individual in the insurance company who is in charge of insurance maintenance. He should be competent and trust worthy. In case he is found to be unsatisfactory, the advice of an independent insurance expert will be necessary.

Exclusions

Every insurer would naturally look for more exclusions that would reduce his losses in case of a claim. The board should ensure that the critical areas affecting a director exposure are not excluded. It should keep an eye particularly on issues relating to securities laws, change of control issues, payments and gratuities and litigation issues.

The claim period is another issue to be dealt with carefully. D&O policies normally respond to claims made during the policy period. This poses a problem for directors whose policies are cancelled, who retire or who are excluded from the surviving board in case of a merger. The 'Notification' provision allows the policyholder to maintain coverage for incidents that have the potential of becoming claims later. It is valid even after the policy has been cancelled or allowed to lapse. The underwriter is responsible for loss-coverage. In case of cancellation of a policy, the 'extended discovery' provision allows the insured to purchase coverage for an extended period of time of 12 to 24 months.

The Indian picture

The Indian insurance industry offers a vast scope for D&O insurance. Awareness is on the rise. However, underwriting and pricing face two problem areas. India has poor accounting standards. Also the huge proportion of family-managed businesses and the laws of bankruptcy aren't well defined.

Insurers will have to evaluate the company's financial standing and assess the inherent risks. Pricing takes into account factors like asset size and composition, financial history of the company, organisational structure, claims history and amount insured. Information on some of the parameters is not easy to find. Companies like Infosys, voluntarily roped in independent credit rating agencies to evaluate their corporate



governance. If others follow suit, the underwriters will find it easier to assess the risk. The companies would benefit too, because if the risks are not assessed accurately the pricing will be higher. With good corporate governance ratings, a company actually pays lesser premium.

vi) Workmen's Compensation Insurance

An employer is exposed to the risk of job related accidents to his workers or employees. According to Workmen's Compensation Act, 1923 the employer is liable to pay compensation in respect of

- Death
- Permanent or partial disablement temporary disablement of the workmen involved in a work related accident.

In India, Workmen's Compensation Act was passed in 1923 and amended in 1934 and 1946 (and subsequently also). According to this act, employer is required to pay compensation to his workers who are injured during the employment period.

The employer may also be liable for third person injuries caused by an accident whether the person is a workman or any other person under the Fatal Accidents Act, 1855.

Insurer covers the employer's liability under the Workmen's Compensation Act through a policy, which is known as Workmen Compensation insurance.

Workmen compensation policy is essential to every employer who employs 'workmen' as defined under the Workmen's Compensation Act in order to protect himself against the legal liabilities arising out of death or bodily injury to this workman.

Scope of Coverage

Workmen's compensation insurance provides coverage for all fatal accidents and injuries to workers during the working hours in an organisation. It also extends coverage through reimbursement of medical, surgical and hospitalisation expenses including transportation costs on payment of additional premium. It will pay medical expenses of workers up to policy limit specified. The liabilities arising out of diseases that are defined u/s 3C of the workmen's compensation act are also covered. The sum insured is fixed on the basis of annual income employees will earn during the policy period.

Exclusions

Workmen's compensation insurance will not provide coverage for the following losses:

- Any accident or injury caused due to war, invasion, nuclear activities etc.
- Any employee who is not considered as 'workman' under Workmen Compensation Act
- Change in the policy provisions after the policy has commenced

- Removal of safety guards intentionally
- Intentional disobedience of orders, which are meant for employee's safety
- Accident to a worker who is under the influence of alcohol or drugs
- It will not cover risks, which are not as per provisions of Workmen's Compensation Act (not during the course of employment. It is not 24 hour cover).

Workmen's Compensation Act, 1923

The Workmen's Compensation Act 1923 had been framed on the model of the English Employer's Liability Act, 1880. The act was later amended in 1934 and 1946.

The objective of this Act is to take over the liability of the employer under the Act in return for payment of appropriate premium to the insurer.

It provides compensation for workers for death and disability due to accident arising out of and during the course of employment for which the employer is liable under the Workmen's Compensation Act, 1923.

The objective of this act is to prevent any sort of delay in settlement of claims arising out of employment injuries or death. In the event an employee is injured while at work, the employer becomes liable to pay the compensation to him within a month of the accident. The act restricts the employer from delaying the payment. It requires the employer to deposit a provisional amount with the employee or the Commissioner within a month even if he wishes to contest the claim for any reason. In case he fails to do so, interest at the rate of 6% would be levied for the period of delay. Such penalty can be imposed to the maximum limit of 50% of the compensation amount. Moreover, the act states that the compensation amount is not liable to any assessment, charge or attachment. The Act thus provides a comprehensive protection for the timely payment of compensation to the injured employee.

The Act has set the amount to be paid in the event of death, permanent, total or partial disablement and in the case of temporary disablement. The compensation amount is directly proportionate to the wages drawn by the employee.

If the accident has been caused directly because of:

- The influence of intoxicants consumed by the worker
- His wilful removal or disregard of any safety guard or other device meant for his safety or
- His wilful disobedience to any express order or rule meant for his safety; then the employer is only liable if it results in death and not otherwise.



Legal mechanism for settlement of claims under this act:

Employer's liability for compensation is absolute in the following circumstances wherein,

1. If personal injury is caused to a workman by accident arising out of and in the course of his employment his employer shall be liable to pay compensation in accordance with the provisions of this Chapter:

Provided that the employer shall not be so liable -

- (a) in respect of any injury which does not result in the total or partial disablement of the workman for a period exceeding three days;
 - (b) in respect of any injury not resulting in death or permanent total disablement caused by an accident which is directly attributable to -
 - (i) the workman having been at the time thereof under the influence of drink or drugs or
 - (ii) the wilful disobedience of the workman to an order expressly given or to a rule expressly framed for the purpose of securing the safety of workmen or
 - (iii) the wilful removal or disregard by the workman of any safety guard or other device he knew to have been provided for the purpose of securing the safety of workman.
2. If a workman employed in any employment specified in Part A of Schedule III contracts any disease specified therein as an occupational disease peculiar to that employment

Amount of compensation

- (1) Subject to the provisions of this Act the amount of compensation shall be as follows namely: -
 - (a) where death results from the injury an amount equal to fifty per cent of the monthly wages of the deceased workman multiplied by the relevant factor; or an amount of fifty thousand rupees whichever is more;
 - (b) where permanent total disablement results from the injury an amount equal to sixty per cent of the monthly wages of the injured workman multiplied by the relevant factor; or an amount of sixty thousand rupees whichever is more.

Notice and claim

No claim for compensation shall be entertained by a Commissioner unless notice of the accident has been given by the employer as soon as practicable after the happening within two years of the occurrence of the accident or in case of death within two years from the date of death.

Reference of Commissioners

The legal authority to settle claims under this act is the Commissioner if any question arises in any proceedings under this Act as to the liability of any person to pay compensation or as to the amount of duration of compensation payable. Further, no Civil Court shall have jurisdiction to settle decided or deal with any question which is by or under this Act required to be settled decided or dealt with by a Commissioner or to enforce any liability incurred under this Act.

Appointment of Commissioners

The Commissioners are appointed by the State Government for Workmen's Compensation for such area as may be specified in the notification. Every Commissioner shall be deemed to be a public servant within the meaning of the Indian Penal Code (45 of 1860).

Venue of proceedings and transfer

Where any matter under this Act is to be done by or before a Commissioner the same shall subject to the provisions of this Act and to any rules made hereunder be done by or before the Commissioner for the area in which -

- (a) the accident took place which resulted in the injury; or
- (b) the workman or in case of his death the dependant claiming the compensation ordinarily resides; or
- (c) the employer has his registered office:

Powers and procedure of Commissioners

The Commissioner shall have all the powers of a Civil Court under the Code of Civil Procedure 1908 (5 of 1908) for the purpose of taking evidence on oath and of enforcing the attendance of witnesses and compelling the production of documents and material objects.

Appeals

- (1) An appeal shall lie to the High Court from the following orders of a Commissioner namely: -
 - (a) an order as awarding as compensation a lump sum whether by way of redemption of a half-monthly payment or otherwise or disallowing a claim in full or in part for a lump sum;
 - (b) an order awarding interest or penalty under Section 4A;
 - (c) an order refusing to allow redemption of a half-monthly payment;



- (d) an order providing for the distribution of compensation among the dependants of a deceased workman or disallowing any claim of a person alleging himself to be such dependant;
- (e) an order allowing or disallowing any claim for the amount of an indemnity under the provisions of sub-Section (2) of Section 12; or
- (f) an order refusing to register a memorandum of agreement or registering the same or providing for the registration of the same subject to conditions:

Provided that no appeal shall lie against any order unless a substantial question of law is involved in the appeal and in the case of an order other than an order such as is referred to in clause (b) unless the amount in dispute in the appeal is not less than three hundred rupees:

- (2) The period of limitation for an appeal under this Section shall be sixty days.
- (3) The provisions of Section 5 of the Limitation Act, 1963 (36 of 1963) shall be applicable to appeals under this Section.

Recovery

The Commissioner may recover as an arrear of land revenue any amount payable by any person under this Act whether under an agreement for the payment of compensation or otherwise and the Commissioner shall be deemed to be a public officer within the meaning of Section 5 of the Revenue Recovery Act, 1890 (1 of 1890).

Questions



1. Discuss the liability implications under the law of torts.
2. Explain the fundamental principles as applicable to liability insurance policies.
3. Discuss the scope of cover available under a product liability insurance policy
4. Discuss the liability of an employer for any work-related injuries and diseases.
5. Explain the scope of D&O liability insurance policy in the Indian markets.

CHAPTER – 10

HEALTH INSURANCE

OUTLINE OF THE CHAPTER

- Introduction
- Health Risks
- Importance of Health Insurance
- Health Insurance policies offered in US and India
- Future of Health Insurance in India
- Areas that need to be addressed for better health insurance coverage

LEARNING OBJECTIVES

- To understand the concept and importance of health insurance as a risk mitigation tool for health risks
- To study the scope of coverage offered by health insurance policies in USA and India
- To evaluate the areas that need to be addressed to make health insurance coverage more comprehensive and affordable

INTRODUCTION

With the growth of mechanized life styles, human beings are increasingly getting exposed to life and health hazards. More than facing the consequences of these hazards, financing the cost of health care has become a serious issue of concern for the individual, his family and for the government even in the most developed countries. Hence, there is a continuous search for alternatives to cope up with the rising expenses on healthcare. Even governments across the globe are making efforts to meet the growing demands for the provisioning of health care systems on one hand and financing of such health care systems on the other. Besides health care, other challenges for the governments include incessantly growing population, hostile economic environment, and ever increasing pressures on the availability of the general tax bases.

Hence, at the national, regional, community, family and individual levels, the basic endeavor is to arrive at a mechanism to meet the growing needs and demands of health care provisioning and financing. While a section of the population may have



faith in the reliability on private mechanism, a majority of them would undoubtedly benefit through a collective approach.

HEALTH RISKS

The risk of poor health includes both the payment of catastrophic medical bills and the loss of earned income. Unless human beings have adequate health insurance, or private savings or financial assets, or other sources of income to meet these expenditures, they will otherwise feel insecure. The matter becomes more catastrophic if old age added with ill health or some form of disability persists with no or inadequate financial support. For health care, more than any thing else financing the healthcare expenses becomes a major issue. The loss of earned income becomes a cause of still greater insecurity if the disability is severe. In the case of long-term disability, besides substantial loss of earned income, medical bills are incurred, employee benefits may be lost or reduced, savings are often depleted, and the most difficult part of the whole problem is that someone must take care of the disabled insured person.

IMPORTANCE OF HEALTH INSURANCE

For better understanding of the concept of health insurance, let us define what health insurance is all about.

Definition

“Health insurance is an insurance, which covers the financial loss arising out of poor health condition or due to permanent disability, which results in loss of income.”

Health insurance rightly provides timely and affordable medical help. But unfortunately not all those who need are able to take this insurance cover. The reasons could be many, including high premiums, applicability of too many conditions and a host of exclusions. Health insurance can be seen as a weapon of social and economic empowerment of the poor.

A systematic plan for financing medical expenses is an important and integral part of a risk management plan. With rising health care costs it is no longer possible for an individual to meet the heavy cost of treatment involving hospitalisation. In the US as much as 47% of health care expenses are met by the government through medical benefit schemes administered by it known as Medicare and Medicaid. While 19% of the expenditure is taken care of by own resources, 35% of health care expenditure comes from private insurance companies through various health insurance policies sold by them.

In India, health spend from own resources is 75% and out of the balance 25%, share of Central Govt. is 5.2%, States 15.2%, Employers and others 3.3% and Local Govt. and donors 1.3%. From the this, it is clear that there is a vast scope for Health Insurance in India.

Health insurance can be organized either on private or public basis - for individuals and families against uncertain events. In developing countries, the potential for expanding health care sector through government financing is very limited because of a very narrow tax base. In such a situation, health care financing by individuals and families who can afford, goes a long way in reducing the burden of the government.

Health insurance as a mechanism is already widespread in the developing countries. The market for health insurance is growing both in terms of awareness and necessity levels. Health insurance can be financed and organized in a number of ways. It can be purchased by an individual, or by groups consisting of the self – employed, or retired persons, or persons between jobs, part-time, temporary, or contract workers not covered by their employers.

The reasons for rise in health care costs across the globe are

- Increase in medical treatment costs.
- Technological advancements in medical equipment
- High labour costs
- Corporatisation and the increasing overheads

HEALTH INSURANCE POLICIES OFFERED IN AMERICA

Generally, there are five types of health insurances policies offered by companies in the US.

- Disability income insurance
- Medical expense insurance
- Long-term care insurance
- Major medical insurance
- Medicare supplement insurance

Other forms of health plans are, (though they are not strictly insurance policies)

- Health saving accounts
- Health Annuities

Disability Income insurance

Disability income insurance is one of the oldest coverages offered by health insurers. Disability income insurance provides compensation to the insured when he is unable to perform his regular duties due to sickness or due to injuries arising out of an accident. It provides security against loss of income. These policies can be short term or long-term. Disability income insurance is provided by life insurance companies and other insurance companies specialised in health insurance. Disability income insurance is offered to



groups and to individuals. In the US, a majority of the health insurance policies are group policies.

Definitions

Injury: Injury can be defined as “any bodily injury caused due to an accident during the period of the policy”.

Disability: An insured individual is stated to be disabled if he is rendered incapable of performing his duties in his occupation due to ill health or sickness for a particular period.

The disablement can be temporary or permanent or total which results in loss of income. Disability insurance provides regular income benefits to the insured person during the period of disablement.

Exclusions: There are some common exclusions under disability insurance policies. They are as follows:

- This policy does not covers disability due to wars, intentional injuries, and normal pregnancies
- In individual policies and group policies, pre-existing conditions are excluded.

Medical Expense Insurance

Medical expense insurance coverage is extended only when the insured is hospitalised for the treatment of the insured for injuries or sickness. Medical expense insurance policies are offered to groups and to individuals as in the case of disability insurance and life insurance policies.

People who are not covered under group medical insurance policies like students, retired people, unemployed people; temporary workers are covered under individual medical expense insurance policies. Insurers directly pay the actual medical expenses to the concerned hospital where the insured took treatment. Premium is fixed based on the benefits offered and period of the policy.

Long-term Care Insurance

Long-term care (LTC) insurance was developed in the 1980s. The need for this coverage arises out of the increase in life expectancy of individuals resulting in a large number of people who had to be cared for in special hospitals at huge cost for an indefinite period. But in the present scenario it is difficult to provide long-term care at home due to the following reasons:

- Increase in the number of working women
- Fewer children per family making it difficult to take care of older people
- Increase in the number of families with no children

In order to pay for the care of such older people, long-term care insurance was developed. LTC covers nursing home care and community care.

Major Medical Insurance

Major medical insurance policy covers major medical expenses incurred by the insured person. It will not reimburse the whole medical expenses. The insurer pays a part of medical expenses and the remaining has to be borne by the insured. This is called participation provision. The medical expenses will be reimbursed only after subtracting the deductible amount.

Medicare Supplement Insurance

Medicare supplement insurance is the supplement to the medicare programme. This policy will only pay the deductible amount and the extra amount, which the insured has to bear over and above the medicare limit.

HEALTH INSURANCE POLICIES IN INDIA

In India, both general and life insurers offer health insurance products though the later class is a recent entrant. Indemnity policies are offered only by general insurers.

The health insurance policies available in India are:

- Indemnity Policies (hospitalization policies)
- Agreed Value policies (critical illness, hospital cash, HIV care (for AIDS))
- There is also a variant of agreed value policies is Unit Linked policies from LIC, Reliance, etc.

Some examples are:

- ❑ Mediclaim Policy (individuals and groups)
- ❑ Overseas Mediclaim Policy
- ❑ Videsh Yatra Mitra
- ❑ Standard cover (remove this)
- ❑ Raj Rajeshwari Mahila Kalyan Yojna
- ❑ Bhagyashree Child Welfare Policy
- ❑ Janata Personal Accident Policy



- ❑ Cancer Insurance Policy
- ❑ Bhavishya Arogya Policy
- ❑ Jan Arogya Bima Policy
- ❑ Personal Accident Policy
- ❑ Gramin Personal Accident Policy
- ❑ Universal Health Insurance Policy

Mediclaim Policy (group and individual)

Mediclaim policy is offered to individuals and to groups exceeding 50 members. It covers hospitalisation for diseases or sickness and also for injuries. Under group mediclaim policy, group discount is allowed to groups exceeding 101 people. The medical expenses will be reimbursed only if the insured is admitted in the hospital for a minimum duration of 24 hours. The insured can insure between Rs.15000 to 500000. This policy is available for the people of age between 5 to 80 years and children between three months and 5 years.

Mediclaim policy offers the following benefits:

- Medical or hospitalisation expenses
- Expenses related to boarding, Doctors' fees, nurses' fees, etc., can also be claimed.
- If any one person from the insured's family opts for coverage under the policy, he can avail the family discount of 10%.
- It will pay the health check up costs equal to 1% of insured sum every 4 years, if the insured does not make any claim during this period. However this benefit is available only under individual policies.
- Cumulative bonus of 5% will be offered at the end of every year provided there is no claim during the period. This bonus will be provided for a maximum of up to 10 years. If insured claims during this period, the sum insured with cumulative bonus will be reduced by 10%.
- If the premium is paid by cheque, it will be exempted under income tax act up to a maximum of Rs. 10,000/- under section 80D of Income Tax Act with an increase limit of Rs. 15,000/- for senior citizens.

Exclusions

This policy will not cover the following:

- Any sickness or illness for first 30 days during the policy
- Any medical expenses relating to pregnancy

- Diseases caused by war, invasion or due to nuclear weapons etc.
- Any expenses incurred for spectacles, cosmetic treatment etc.
- Medical expenses incurred for purchasing tonics, vitamins unless incurred as part of the treatment.

Conditions

- Any situation in which insured claims the sum insured should be informed to the insurer with the details about his injuries, admission etc., into hospital within 7 days.
- Insured should file the claim with the insurer within 30 days after discharge from hospital and show all medical bills and other information required by the insurer.
- The insurer can appoint any medical practitioner to observe the injuries and diseases that requires hospitalisation.
- The medical treatment should be taken within Indian boundaries and compensation is paid in rupees.
- The insurance company will not pay the compensation in case the claim is proved to be fraudulent.

Overseas Mediclaim Policy

In 1984, the Overseas Mediclaim Policy was developed. This policy will reimburse the medical expenses incurred by Indians upto 70 years of age while travelling abroad. The premium will be charged based on their age, purpose of travel, duration and plan selected by the insured under the policy. Employment study policy was introduced in 1991 for the citizens who live temporarily outside India. This policy is provided to businessmen, people going on holiday tour, travelling for educational professional and official purposes. Overseas mediclaim policy provides two types of policies namely Standard cover and Videsh Yatra Mitra. Under standard cover, three types of plans are offered with different coverages and under videsh yatra mitra three plans are offered with very wide coverage.

Benefits

- This policy reimburses the medical expenses when the insured stays abroad.
- In the event of claims, M/s Mercury International Assistance will provide the services anywhere. It has worldwide coverage. It will pay claim amount directly to the hospitals.
- M/s. Mercury International Assistance will also bear all the expenses to send the insured person to home country because of sickness or due to injuries.



- Reimbursement of medical expenses will be done in home currency of the country visited.
- If the insured person is not able to contact Mercury Company he can collect all expenses after coming back to India by showing all the relevant documents and bills

Exclusions

- The medical expenses incurred for non-emergency illness and for treatment already planned
- The treatment expenses incurred on pre-existing diseases
- Injuries while participating in any adventure sports.

Raj Rajeshwari Mahila Kalyan Yojna: It is a personal accident policy offered by an insurance company for the welfare of women. It is offered to women residing in rural and urban areas. Women between 10-75 years of age are eligible for this policy irrespective of their occupation and income level. This coverage is provided on 24 hours basis.

Bhagyashree Child welfare policy: This policy is offered to girls between 0-18 years. The age of parents of the girls should not be more than 60 years. It provides coverage to one girl child in a family who loses her father or mother in an accident. It provides insurance coverage to the girl child and also her parents against death and disability for 24 hours.

Janata Personal Accident Policy: Any individual between 10-70 years of age is eligible for coverage under this policy. This policy offers coverage in the event of death or loss of limbs due to an accident. Amount of premium charged is Rs.15 p.a. per individual. The premium charged under this policy is comparatively less when compared to other policies as this policy is meant for the weaker sections of society. Other policies can be taken along with this policy. This policy can be taken for any period up-to 5 years.

Cancer Insurance Policy: Cancer insurance policy is designed for cancer patients aid association members. The members of this association are eligible for this policy except those members who are already suffering from cancer. The persons insured under this policy will pay premium to their association along with the membership fee. This policy will offer coverage to the insured in case he develops cancer. All the expenses incurred for treatment of cancer not exceeding the sum insured will be paid directly to the insured person.

Jan Arogya Bima Policy: This policy provides medical insurance to poorer sections of the people. This policy covers illnesses like heart attack, jaundice, food poisoning, and accidents etc. that require immediate hospitalisation. This policy is applicable to individuals between 5-70 years.

Gramin Personal Accident Insurance: This policy is designed for the rural people in the country. This policy has fixed insured sum of Rs.10,000/- and the premium charged is Rs. 5/- The individuals falling in the age group of 10-70 are eligible for this policy.

FUTURE OF HEALTH INSURANCE

With the emergence of new life style and social order, awareness of health is growing at a faster pace, so also the new types of health conditions, including those related to one's occupation. New developments in health care sector have introduced sophistication at a higher cost. Thus, health insurance is fast emerging as growing segment of non-life insurance particularly because of reasons which include increasing awareness amongst the public about medical insurance, vast number of 'uncovered' population for health risk, increasing cost of health care, newer developments in the medical sphere, corporatisation of health care providers etc.

Another important factor for the growth of this segment is because of the declining share of Public expenditure on health care, which is currently not only 0.9% of GDP. Although in terms of amounts a considerable part of the public funds are used for provisioning of health care services, yet about 80% of health costs are still paid by patients out of pocket thus resulting in either increased level of debt/erosion of savings or in inadequate level of healthcare, which in turn resulting in death or reduced earning capacity.

Health care provisioning in India normally takes three forms namely: State funded, Employer funded and Self funded. Examples of State funded insurance schemes are tailor made schemes (such as Rajiv Aarogyasri Scheme of Andhra Pradesh). The beneficiaries are mainly the poor. Other schemes such as ESI are implemented by the Govt. with contributions from other stakeholders. Employer funded schemes have become an essential part of the package offered to the employees. For others, almost total healthcare expenditure is met from own savings. This leaves a large scope for health insurance business.

To augment growth in this segment, Section 3 (2AA) of Insurance Act 1938 provides for special treatment for new insurance companies which opts to operate exclusively in health insurance. Further IRDA also prioritizes in giving license to companies having health insurance in their portfolio. Some of the companies operating as stand alone Health insurance companies are in fact designing a variety of tailor made health insurance plans to suit to the requirements of all the segments of the society as stand alone products.

As observed from the growth trends of the health insurance industry, although health insurance penetration is low at present, the pace at which it is growing indicates the latent potential demand existing in this segment. Presently, Health Insurance is the second largest portfolio, second only to Motor Insurance. A recent estimate puts the potential health insurance market at current levels at Rs.15,000 crores and another



estimate puts the asset based insurance premium being only 25% of the real health insurance potentials. Health insurance is becoming more of a necessity than an option whether voluntary or as a beneficiary.

Some of the new creative health products available in the Indian markets include:

- Critical illness cover
- Hospital cash
- Family Floater
- Special policies for Diabetics and HIV patients

These policies also have a facility of Cashless settlements through the Third Party Administrators (TPAs), which is a Western model, where in the payments are made directly to the treating hospitals. The Indian market is further trying to adopt some of the Western healthcare providers to bring in more innovative products such as Health Saving Accounts, Health Annuities, Managed Health Care through organizations acting as facilitators such as Health Maintenance Organizations (HMO), Preferred Provider Organizations (PPO), Point-of-Service (POS) plans, etc.

In coming future, the focus of the insurers is more on provisioning of 'holistic health' rather on 'financing for health' which is possible only through products with reasonable and adequate cover at optimum premiums. Thus, with increased activities and innovative plans, the Regulator and the Government will act as facilitators with the required legislations and administrative mechanisms. Further, the regulations will regulate not only the health insurers but also health service providers, viz., hospitals, doctors, diagnostic laboratories, etc.

Health insurance in India is still in the developing stage. The increasing health care costs in the country is likely to contribute to the development of more health insurance products. Health insurance is not at present recognized as a separate segment in Indian insurance industry. The present health insurance policies available in the Indian markets have some inherent limitations.

IRDA is very seriously considering breaking insurers into three broad categories from the current two, i.e., Life, Non-life & Health. Already, as mentioned earlier, section 32AA provides for special treatment in the matter of issuing licence for exclusive health insurers.

Even the solvency margin is going to be risk based for health insurance instead of the current 1.5, which is fixed.

Some of the areas that need to be focussed from the coverage perspective are

- Old age Health care – mostly required at old age to take care of health problems associated with aging.

- Long-term care – for a term of three to five years.
- Disability income insurance, which is not provided in basic policy cover.
- Mental care – to provide financial assistance for the caring parents.
- Health cover for the daily wage earners seasonal workers casual laborers, construction workers, etc.
- Workers employed in the seasonal factories.
- Juvenile insurance- to meet ill health/medical expenses associated with health related problems of children.
- Special/exclusive health care policies for ‘women’ for gender related diseases.
- Health cover for the informal sector/unorganized sector.
- Rural health policies to be tailor-made for the members, to suit to their needs.

Thus, a health insurance policy to be meaningful should be designed in such a way that the basic needs of health care are met. The Insurance Regulatory and Development Authority (IRDA) on its part is also taking initiative to increase the penetration of the health insurance markets in India. The IRDA is also looking into regulatory issues to allow stand alone health insurance companies with lesser capital requirements. Probably, with such exclusive health insurance companies, there would be better choice available to consumers to choose policies that would be suitable for their requirements. On the other hand, the companies can also have greater freedom in designing policies with fair premiums depending upon the riskiness of insured individual.

Questions



1. Discuss how a health insurance policy can be a tool for managing health risk exposures.
2. Discuss the salient features of disability income coverages available in the United States of America. Can it be replicated in India?
3. Enumerate and explain at least two health insurance policies available in India.
4. Explain why health insurance is not taking off in Indian markets.
5. Which are the areas that need to be addressed to make a health policy more comprehensive?

CHAPTER – 11

GENERAL INSURANCE CLAIMS

OUTLINE OF THE CHAPTER

- Introduction
- Preliminary procedures for claims
- Investigation and Assessment of claims
- Settlement of claims
- Questions

LEARNING OBJECTIVES

- To study the principles and practice of general insurance claims
- To understand the legal procedures to be followed for processing a claim
- To study the importance of evaluating and assessing genuine claims
- To explain the settlement practice for a covered loss

INTRODUCTION

The settlement of claims constitutes one of the important functions in an insurance organization. Indeed, the payment of claims may be regarded as the primary service of insurance to the public. It is the purpose for which an insurance contract is entered into. The proper settlement of claims requires a sound knowledge of the law, principles and practices governing insurance contracts and ,in particular, a thorough knowledge of the terms and conditions of the standard policies and various extensions and modifications thereunder.

In addition, the prompt and fair settlement of claims is the hallmark of good service to the insuring public. It is equally important that claims negotiations should be on the basis of patience, tact and courtesy.

The procedure in respect of claims under various classes of insurance follows a common pattern and may be considered under three broad headings –

- Preliminary stage
- Investigation stage
- Settlement stage

PRELIMINARY PROCEDURE

Notice of Loss

It is most essential that insurers receive early notification of the loss. The time limits within which notice of loss shall be given by the insured are provided for in policy conditions. Some policies provide for immediate or forthwith notification whereas others require notice to be given as early as practicable after the loss. The purpose of an immediate notice condition is to allow the insurer to investigate a loss at its early stages. It would also enable the insurer to suggest measures to minimize the loss and to take steps to protect salvage.

Undue delay in notification would adversely affect the insurers position. Therefore, non-compliance with these provisions will relieve the insurer of liability if the non-compliance materially affects the insurers position. However, whether there is delay in notification or not or whether the delay is material will be ultimately decided by the Courts based on the facts of individual cases.

The notice of loss condition in liability policies provides for two aspects:

1. notification of the happening of the accident immediately, followed by
2. notification of the receipt of claim or suit filed against the insured.

Under certain types of policies (e.g. Burglary) notice is also to be given to police authorities.

Loss Minimisation

At Common law, there is a duty on the part of the insured to observe good faith during the currency of the policy, especially when a loss occurs.

This duty of good faith means that, at all times, the insured has to act as if he is uninsured. When a loss occurs it is the legal duty of the insured to do his utmost to minimize the loss.

Procedural issues

On receipt of intimation of loss or damage insurers check that:

1. the policy is in force on the date of occurrence of the loss or damage;
2. the loss or damage is by a peril insured by the policy;
3. the subject matter affected by the loss is the same as is insured under the policy;
and
4. notice of loss has been received without undue delay.

After this check up the loss is allotted a number and entered in the Claims Register. A separate file is opened for the claim with a copy of the policy, or relevant extracts thereof filed with the claim papers. Thereafter, a claim form is issued to the insured.



Claim Forms

The contents of the claim form vary with each class of insurance. In general the claim form is designed to elicit full information regarding the circumstances of the loss, such as date of loss, time, cause of loss, extent of loss, etc.

The other questions vary from one class of insurance to another. For example, motor claim form provides for a rough sketch of the accident, burglary claim form contains a question regarding notification to the police; where the insurance is subject to pro-rata average a question is asked on the values of the property at the time of loss. In those classes of policies which are contracts of indemnity, a question is asked to ascertain the other policies held by the insured covering the same subject matter and whether any third party was responsible for the loss. This information is necessary to enforce contribution and subrogation.

The issue of a claim form does not constitute an admission of liability on the part of the insurers. The insurers make this position very clear by making a remark on the form to that effect. All letters that the insurers send to the insured in connection with the claim are also sent without prejudice to their rights and hence they carry the remark without prejudice. These words are intended to make it clear that although the insurers are engaged in correspondence and processing of the loss, the question of liability under the policy is left open. Thus claim forms are issued without prejudice, which means that by the issue of the claim form liability is not admitted under the policy.

Claim forms are invariably used in fire and accident insurance. They are not used in marine insurance except in respect of inland transit claims. (The practice varies)

INVESTIGATION AND ASSESSMENT

On receipt of the claim form duly completed from the insured, the insurers decide about investigation and assessment of the loss. If the loss is small, the investigation to determine the cause and extent of loss is done by an Officer of the insurers (upto Rs.20,000). Sometimes even this may be waived and the loss settled on the basis of the claim form only.

The investigation of larger or complicated claims is entrusted to independent professional surveyors who are specialists in their line. The practice of assessment of loss by independent surveyors is based on the principle that since both the insurers and insured are interested parties, the opinion of an independent professional person should be acceptable to both the parties as well as to a court of law in the event of any dispute.

The appointment of a surveyor is intimated to the claimant. The surveyor is furnished with all relevant claim papers such as claim form, copy of policy, etc. However, many a times, surveyor is appointed and survey is carried out immediately on receipt of notice of loss, that is, even before claim form could be issued.

Section 64 UM of the Insurance Act provides that no claim in respect of a loss which has occurred in India and requiring to be paid or settled in India equal to or exceeding Rs.20,000 on any policy of insurance shall be admitted for payment or settled by the insurer unless he has obtained a report on the loss from a person who holds a license to act as a Surveyor or Loss Assessor.

Under the provisions of the Insurance (amendment) Act, 1968 a Surveyor and Loss Assessor is required to hold a valid license issued by the Controller of Insurance. The license is valid for a period of five years and is granted subject to submission of application form and payment of fee as prescribed under the Act.

Claims Documents

In addition to the claim form, independent survey report etc., certain documents are required to be submitted by the claimant or secured by the insurers to substantiate the claim. For example, for fire claims, a report from the Fire Brigade is obtained; in burglary claims, a report from the Police; for Workman's Compensation Fatal Claims a report from the Coroner, Police report and post mortem report; for motor claims; driving license, registration book, police report etc.

In marine cargo claims, the nature of documents varies according to the type of loss i.e., total loss, particular average, inland transit claims etc. For example, the documents required for total loss claims are: (under Evidence Act and Civil Procedure Code, all the documents should be in original and not copies, otherwise, no recovery is possible)

- (i) Original Policy
- (ii) Invoice
- (iii) Bill of Lading
- (iv) Bill of Entry
- (v) Copy of Protest, i.e., statement made by the Captain of the Vessel on the loss before a Notary Public (if relevant)
- (vi) Non-delivery or short landing certificate (if relevant)
- (vii) Landed but missing certificate (if relevant)
- (viii) Letter of subrogation and Power of Attorney, Notice of loss to the carrier under section 10 (carriers act) correspondence exchanged with Carriers, Port Trust etc. regarding claims filed against them.

Arbitration

Arbitration is distinct from litigation and is a method of settling disputes under contract in accordance with the Arbitration Act, 1940.



The normal method of enforcing a contract or settling of dispute thereunder is an action in a court of law. Litigation, however, involves considerable delay and expense. The Arbitration Act allows the parties to submit disputes under a contract to the more informal, less costly and private process of arbitration. Fire and most accident policies contain an arbitration condition which provides for settlement of differences by arbitration. There is no arbitration condition in marine insurance policies.

According to the Arbitration condition in the fire policies, if the liability under the policy is admitted by the company, and there is a difference concerning quantum to be paid, such a difference must be referred to the arbitration, in terms of the Arbitration Act, 1940.

The procedure in arbitration is along the following lines. The dispute is submitted to the decision of a single arbitrator to be appointed by the parties, or in the event of any disagreement between them upon a single arbitrator, to the decision of two arbitrators each appointed by the parties. These two arbitrators appoint umpire, who presides at the meetings. The procedure during these meetings resembles that of a court of law. Each party states his case, if necessary with the help of a counsel and witnesses are examined. If the two arbitrators do not agree on a decision, the matter is submitted before the umpire, who makes his award. Costs are awarded at the discretion of the arbitrator/arbitrators or umpire making the award.

Policy conditions provide for limitation to apply to claims. For example, the fire policy provides that in no case whatsoever shall the Company be liable for any loss or damage after the expiration of 12 months from the happening of the loss or damage unless the claim is subject to pending action or arbitration; it being expressly agreed and declared that if the Company shall disclaim liability for any claim hereunder and such claim shall not within 12 calendar months from the date of the disclaimer have been made the subject matter of a suit in a court of law then the claim shall for all purposes be deemed to have been abandoned and shall not thereafter be recoverable hereunder.

SETTLEMENT

The claim is processed on the basis of:

- (i) the claim form;
- (ii) independent report from surveyors, legal opinion, medical opinion, etc., as the case may be;
- (iii) various documents furnished by the insured; and
- (iv) any other evidence secured by the insurers
- (v) Final & full satisfaction discharge is a must. Otherwise claimant can go to court for payment of additional amounts after realizing the claim cheque. There are many case laws saying that the discharge voucher was obtained by the insurer due to misrepresentation, undue influence, etc.

If the claim is in order, settlement is effected by cheque. The payment is entered in the claims register as well as in the relevant policy record. Appropriate recoveries are made from the co-insurers, if any.

Before effecting payment, it is essential to decide whether the claimant is entitled to receive the claim monies. For example for payment of fatal claim under personal accident insurance, probate or letters of administration or succession certificates have to be produced by legal heirs. If the property insured under a fire policy is mortgaged to the bank, then according to the agreed bank clause, claim monies are to be paid to the bank, whose receipt will be a complete discharge to the insurers. Similarly claims for Total Loss on vehicles subject to hire purchase agreements are paid to financiers. Marine cargo claims are paid to the claimant who produces the marine policy duly endorsed in his favour.

Post Settlement Action

The action taken after settlement of the claim in relation to underwriting varies from one class of business to another. For example, sum insured under a fire policy stands reduced to the extent of the amount of claim paid. However, it can be reinstated on payment of pro-rata premium. On payment of the capital sum insured under a personal accident policy, the policy, stands cancelled. Similarly, payment of a claim under fidelity guarantee policy automatically terminates the policy. With a total loss claim on a motor vehicle, the policy is returned to the insurers.

Recoveries

Recoveries may be in the form of salvage or from third parties under subrogation rights. Recoveries of salvage are to be entered in the claims register. After settlement of claim, the insurers under the law of subrogation, are entitled to succeed to the rights and remedies of the insured and to recover the loss paid from a third party who may be responsible for the loss under respective laws applicable. Thus, insurers can recover the loss from shipping companies, railways, road carriers, airlines, Port Trust Authorities. For example, in the case of non-delivery of consignment, the carriers are responsible for the loss. Similarly, the Port Trust is liable for goods which are safely landed but subsequently missing.

For this purpose, a letter of subrogation duly stamped is obtained from the insured. The letter is worded along the following lines :



Insurance Co. Ltd.,

s.s.

In consideration of your paying to me/us a sum of Rs. _____ In respect of the undermentioned goods insured with you under Policy No. _____ I/We hereby assign and transfer to you all my/our right(s), title and interest in respect of the said goods, and all rights or claims against any person or persons in respect thereof.

AND I/We also authorize you to use my/our name in any action or proceedings you may bring in relation to any of the matters hereby assigned and transferred to you, and I/We undertake for myself/ourselves to concur in any matters or proceedings and to execute all documents which may be necessary, and generally to assist therein by all means in my/our power.

I/We further undertake if called upon by you to do so, myself/ourselves to undertake any such action or proceedings that you may direct on your behalf; it being understood that you are to indemnify me/us and any other persons whose names may necessarily be used against any costs, charges or expenses which may be incurred in respect of any action or proceedings that may be taken by virtue of this Agreement.

Date: _____

Signature

Salvage

Salvage refers to partially damaged property. On payment of loss, salvage belongs to insurers. For example, when motor claims are settled on total loss basis, the damaged vehicle is taken over by insurers. Salvage can also arise in fire claims, marine cargo claims etc.

Salvage is disposed off according to the procedure laid down by the companies for the purpose. Surveyors, who have assessed the loss, will also recommend methods of disposal.

Finally, recoveries have to be made from reinsurers, under relevant reinsurance arrangements, if applicable, and this is done at Head Office level.

Loss Minimization and Salvage

The primary duties of a surveyor are to determine the cause and extent of loss, to examine compliance with terms and conditions and warranties and to give a report on the basis of which insurers may take decision regarding settlement.

Surveyors also play a role in loss minimization and protection of salvage. In fire losses, for example, surveyors may recommend measures such as temporary repairs to roofs

etc., removal of clogged material from machinery so that production process is not interrupted, prevention of rust damage to machinery, removal of undamaged property to places of safety, separation of wet stocks for drying and reconditioning etc.

In house settlements

Independent surveys are dispensed with in respect of claims where documentary evidence of the cause of loss is available in the form of police reports. (minor theft claims), landed but missing certificates issued by Port Trust, non delivery certificates issued by Railway, lost overboard certificate issued by Port authorities where cargo loss has taken place during loading etc.

Questions



1. Discuss the issues to be considered at the preliminary stage by the insurer on getting a claim notification.
2. Explain why insurers insist on the adherence of utmost good faith at any occurrence of a contingent loss?
3. Discuss the three stages followed by the claims manager for evaluating a claim amount.
4. Enumerate and discuss the importance of the various claims documents required for substantiating a claim.
5. "Salvage management also calls for expertise and skill". Discuss.

CHAPTER – 12

GENERAL INSURANCE—INVESTMENT AND ACCOUNTING

OUTLINE OF THE CHAPTER

- Introduction
- General Insurance Investments
- IRDA guidelines
- Solvency Margins
- Financial Reporting
- Accounting Ratios
- Questions

LEARNING OBJECTIVES

- To study the investment philosophy of general insurance companies
- To study the guidelines for investments as prescribed by the regulator, IRDA
- To know about the procedures and practice of insurance accounting
- To understand the rationale for creation of reserves and maintain solvency margins
- To evaluate some accounting ratios for performance evaluation of insurance operations
- To understand the importance of accurate financial reporting

INTRODUCTION

Investment management of insurance companies have become a challenge in the present day scenario, with the convergence of financial institutions. The challenge is more seen in the areas of financial management which in fact determine the success of the insurance companies. Globally insurance companies are the most regulated for the only reason that they deal with public funds. Basically, insurance operations rely on the trust of policyholders. Hence, insurance companies' investments are subject to severe regulatory framework mainly to safeguard the interests of the policyholders. In India, the investment guidelines are issued by the IRDA, in the present paradigm following the opening up of the insurance sector.

GENERAL INSURANCE INVESTMENT

The aggregate investment activities of any country's life and health insurance industry are a major source of infrastructure capital for the national economic growth. Insurers invest in the debt and equity issues of all types of corporations, shopping malls, apartments and other real estate. They are the major purchasers of Government Securities. Assets or investments are classified according to the nature of the liabilities for which the assets are held and invested. Some assets are used to support contractual obligations for guaranteed fixed benefit payments normally held in general account. Assets held to support other liabilities associated with investment risk are held in special accounts called separate accounts. e.g. Valuable annuities, pension products, variable life insurance etc.

IMPORTANCE OF INVESTMENT PERFORMANCE

The investment performance of an insurance company affects profits, dividends, interest credits on term etc. Performance of specified assets held for specific liabilities affects variable life and annuity products and pension funds when benefits by contract depend upon investment results that are passed directly to contract holders (however this is not applicable for general insurers).

Moreover, the prices of insurance products are dependent on investment returns an insurer earns. Insurers that earn above average returns can price products favorably to retain customers in a competitive market. Investment management is a process involving asset-liability management, integration of investment management and product design management. For favorable pricing, other important economic constraints include inflation, monetary and fiscal policy of government, investments market opportunities, insurer's market share, competition, tax liabilities etc. Therefore, the primary objective of an investment policy is to create an investment portfolio with cash flows, that matches an insurer's expected liability cash flows and asset – liability risk management strategy, and striking a balance between solvency and profitability.

IRDA GUIDELINES ON REGULATION OF INVESTMENTS

4. (1) *General Insurance Business* – Without prejudice to section 27B of the Act. every insurer carrying on the business of General Insurance shall invest and at all time keep Invested his investment assets in the manner set out below:



No.	Type of Investment	Percentage
(i)	<i>Government Securities</i>	<i>Not less than 20% of Investment Assets</i>
(ii)	<i>Government Securities or Other Approved Securities</i>	<i>Not less than 30% of Investment Assets (incl (i) above)</i>
(ii)	<p><i>Investments as specified in Section 27B of Insurance Act, 1938 and Schedule II subject to Exposure / Prudential Norms specified in Regulation 5:</i></p> <p><i>a. Approved Investments and Other Investments (Out of '(iii)a' 'Other Investment' specified under 27B (3) of the Act, shall not exceed 25% of Investment Assets)</i></p> <p><i>b. Housing and loans to State Government for housing and fire fighting equipment, by way of subscription or purchase of:</i></p> <ol style="list-style-type: none"> <i>1. Bonds / debentures of HUDCO and National Housing Bank</i> <i>2. Bonds / debentures of Housing Finance Companies either duly accredited by National Housing Banks, for house building activities, or duly guaranteed by Government or carrying current rating of not less than 'AA' by a credit rating agency registered under SEBI (Credit Rating Agencies) Regulations, 1999</i> <i>3. Asset Backed Securities with underlying housing loans, satisfying the norms specified in the guidelines issued under these regulations.</i> <p><i>c. Investment in Infrastructure:</i> <i>(Explanation: Subscription or purchase of Bonds / Debentures, Equity and Asset Backed Securities with underlying infrastructure assets would qualify for the purpose of this requirement.</i> <i>'Infrastructure facility' shall have the meaning as given in clause (h) of regulation 2 of Insurance Regulatory and Development Authority (Registration of Indian Insurance Companies) Amendment Regulations, 2008)</i></p>	<p><i>Not exceeding 55%</i></p> <p><i>Not less than 5%</i></p> <p><i>Not less than 10%</i></p>

List of Approved Investments for General Business

'Approved investments' for the purpose of section 27B of the Act consist of the following:

- (a) *All investments specified in section 27B of the Act except*
 - (i) *Clause (b) of sub-section (1) of section 27A of the Act;*
 - (ii) *Immovable property situated in another country as stated in clause (n) of sub-section (1) of section 27A of the Act;*
 - (iii) *First mortgages on immovable property situated in another country as stated in clause (i) of sub-section (1) of section 27B of the Act.*
- (b) *In addition the following investments shall be deemed as approved investments by the Authority under the powers vested in it vide clause (j) of sub-section (1) of section 27B of the Act:*
 - (i) *All loans secured as per Insurance Act, 1938, secured-debentures, secured bonds and other debt instruments rated as per Note appended to Regulations 3 and 4 Equity shares, preference shares and debt instruments issued by All India Financial Institutions recognized as such by Reserve Bank of India – investments shall be made in terms of investment policy guidelines, benchmarks and exposure norms, limits approved by the Board of Directors of the insurer.*
 - (ii) *Bonds or debentures issued by companies rated not less than AA or its equivalent and P1 or Equivalent ratings for short term bonds, debentures, certificate of deposits and commercial papers by a credit rating agency, registered under SEBI (Credit Rating Agencies) Regulations 1999 would be considered as 'Approved Investments'.*
 - (iii) *Subject to norms and limits approved by the Board of Directors of the insurers deposits (including fixed deposits as per section 27B (10) of Insurance Act, 1938) with banks (e.g. in current account, call deposits, notice deposits, certificate of deposits etc.) included for the time being in the Second Schedule to Reserve Bank of India Act, 1934 (2 of 1934) and deposits with primary dealers duly recognized by Reserve Bank of India as such.*
 - (iv) *Collateralized Borrowing & Lending Obligations (CBLO) created by the Clearing Corporation of India Ltd. and recognized by the Reserve Bank of India and exposure to Gilt, G Sec and liquid mutual fund forming part of Approved Investments as per Mutual Fund Guidelines issued under these regulations and money market instrument / investment.*
 - (v) *Asset Backed Securities with underlying Housing loans or having infrastructure assets as underlying as defined under 'infrastructure facility' in clause (h) of regulation 2 of Insurance Regulatory and Development Authority (Registration of Indian Insurance Companies) Amendment Regulations, 2008.*



(vi) Commercial papers issued by a company or All India Financial Institution recognized as such by Reserve Bank of India having a credit rating by a credit rating agency registered under SEBI (Credit Rating Agencies) Regulations 1999.

(vii) Money Market instruments as defined in Regulation 2 (cc) of this Regulation.

Form 3 B

Statement of investment of total assets – Compliance report to be submitted quarterly

Form - 3B

Company Name & Code:

Statement as on:

Statement of Investment Assets (General Insurer, Re-insurers)

(Business within India)

Periodicity of Submission: Quarterly:

No.	Particulars	Sch	Amount
1.	Investments	8	
2.	Loans*	9	
3.	Fixed Assets	10	
4.	Current Assets		
	a. Cash & Bank Balance	11	
	b. Advance & Other Assets	12	
5.	Current Liabilities		
	a. Current Liabilities	13	
	b. Provisions	14	
	c. Misc. Exp not Written Off	15	
	d. Debit Balance of P & L A/c		
	Application of Funds as per Balance Sheet (A)		0

	Less: Other Assets	Sch	Amount
1.	Loans (if any)	9	
2.	Fixed Assets (if any)	10	
3.	Cash & Bank Balance (if any)	11	
4.	Advances & Other Assets (if any)	12	
5.	Current Liabilities	13	
6.	Provisions	14	

No.	Particulars	Sch	Amount
7.	Misc. Exp not Written Off	15	
8.	Debit Balance of P & L A/c		
	Total (B)		0
	*Investment Assets As per FORM 3B	(A-B)	0

General Business

No.	Investment represented as	Reg.%	SH		PH	Book Value (SH + PH)	% Actual	FVC Amount	Total	Market Value
			Balance	FRSM*						
			(a)	(b)	(c)	d - (b+c)		(c)	(d + e)	
1.	G. Sec.	Not less than 20%								
2.	G. Sec or Other Approved Sec. (Incl. (I) above)	Not less than 30 %								
3.	Investment subject to Exposure Norms									
	1. Housing & Loans to SG for Housing and FEC, Infrastructure Investments	Not less than 15%								
	2. Approved Investments	Not exceeding 55%								
	3. Other Investments (not exceeding 25%)									
	Total Investment Assets	100%								

Certification:

Certified that the information given herein are correct and complete to the best of my knowledge and belief and nothing has been concealed or suppressed.

Date:

Signature: _____

Full Name:

Designation:

Note: (*) FRMS refers Funds representing Solvency Margin

(*) Pattern of Investment will apply only to SH funds representing FRMS

(*) Book Value shall not include funds beyond Solvency Margin

Other Investments are as premitted under Sec 27A(2) and 27B(3)



6. Returns to be submitted by an Insurer

Regulation 6 of the Insurance Regulatory and Development Authority (Investment) Regulations, 2000 shall be substituted for the following:-

6. *Every insurer shall submit to the Authority the following returns within such time, at such intervals and verified/certified in such manner as indicated there against.*

No.	Form No.	Description	Periodicity of returns	Time limit for submission	Verified / Certified by
1.	Form 1	Statement of Investment and Income on Investment	Quarterly	Within 45 days of the end of the Quarter	Chief Executive Officer / Chief of Investments
2.	Form 2	Statement of Downgraded Investments	Quarterly	Within 45 days of the end of the Quarter	Chief Executive Officer / Chief of Investments
3.	Form 3A (Part A,B,C)	Statement of Investments (Life Insurers) - Compliance Report	Quarterly	Within 45 days of the end of the Quarter	Chief Executive Officer / Chief of Investments
4.	Form 3B	Statement of Investment (General Insurer) – Compliance Report	Quarterly	Within 45 days of the end of the Quarter	Chief Executive Officer / Chief of Investments
5.	Form 4	Exposure and other norms - quarterly compliance certificate	Quarterly	Within 45 days of the end of the Quarter	Chief Executive Officer / Chief of Investments and Chief Finance Officer
6.	Form 4 (Part A, B, C)	Statement of Investment Subject to Exposure Norms - Investee Company	Quarterly	Within 45 days of the end of the Quarter	Chief Executive Officer / Chief of Investments
7.	Form 5	Statement of Investment Reconciliation	Quarterly	Within 45 days of the end of the Quarter	Chief Executive Officer / Chief of Investments
8.	Form 5A	Statement of Mutual Fund Investment	Quarterly	Within 45 days of the end of the Quarter	Chief Executive Officer / Chief of Investments
9.	Form 6	Certificate under sections 28 (2A), 28 (2B) and 28B (3) of the Insurance Act, 1938	Quarterly	Within 45 days of the end of the Quarter	Chief Executive Officer / Chief of Investments
10.	Form 7	Confirmation of Investment Portfolio Details	Quarterly	Within 45 days of the end of the Quarter	Chief Executive Officer / Chief of Investments
11.	Form 7A	Statement of Non Performing Assets	Quarterly	Within 45 days of the end of the Quarter	Chief Executive Officer / Chief of Investments

Note: All returns for the quarter ending March shall be filed within the period stipulated above based on provisional figures and later re-submitted with Audited figures within 15 days of adoption of accounts by the Board of Directors.

SOLVENCY MARGINS OF GENERAL INSURANCE COMPANIES

Solvency Surveillance

Insurance industry is highly regulated in all the countries, though the regulatory framework followed differs from country to country. In some countries, regulation is in the form of state monopoly and in some other countries, the Government controls important aspects of business like licensing, minimum tariff, product approval etc. Even in developed countries where liberalization and free market economy are the buzzwords, stringent 'front end' and 'back-end' regulations are in vogue. The framework depends on a host of factors like size of insurance market, type of customers and players in the market, degree of professionalisation, magnitude of transparency, etc.

Insurance companies collect premium in advance with a promise to settle claims at a future date in the event of named contingency. Thus, the entire business is based wholly on the financial strength and integrity of the management to meet its obligations. Insurance business is unique in many other aspects as well. Insurer assumes a dual role of **risk management** and **money management**. This exposes insurers to risk on both assets as well as liabilities side. Risk on the asset side arises mainly because of price fluctuations as a major portion of insurance funds are invested in financial assets. On the liability side, the difficulty in assessing the liability (Technical Reserves) accurately creates risk. Another unique aspect is that the stake of the shareholders and promoters is very small compared to the policyholders' interest. Due to these unique features insurance company operations are closely monitored.

Risk profile of non-life insurers is very different from life companies. Main difference is in the nature of the business. Life insurers collect level premium for offering risk coverage for a fairly long period of 15-30 years whereas non-life insurance contract is for a short term, generally for a year. In case of life insurance, the size of claims can somewhat be estimated as the companies 'assure' a specific sum in the event of a contingency and the number of claims can also be predicted based on mortality tables. But, quantum of loss in case of non-life business is not easily predictable as also the number of accidents. Moreover, in case of non-life business, it is essential to make a distinction between property and liability lines because of the different **time factor** involved in claim settlement. Liability is a long tail business as the loss may be reported over a number of years in future, long after the expiry of insurance policy. Huge (open-ended) liability to premium ratio and mandatory character of some lines are also factors to be reckoned with. In addition, involvement of third parties and direct settlement to them compounds the problem of loss assessment. Legal costs involved in settlement are sometimes astronomical and run-off claims are very common in this type of business.

Insurance companies make provisions for loss and invest the money in financial instruments as the settlement of claim takes time.



Solvency Margin

It is imperative to quantify each of the risk factors discussed above as they could lead to insolvency. In order to absorb sudden setbacks, it is necessary to have some safety margin. Financial strength needed for this purpose is generally provided by shareholders and promoters. That is why owners' funds in insurance entities are termed as 'policy holders surplus'. There are many ways by which the financial prowess of insurers are ascertained. Assessment of the proportion of owners' funds to outsiders' liability gives an idea of how much a company is geared. High gearing, though increases the profitability, raises the level of risk undertaken by any entity.

IRDA had tightened its monitoring by increasing the frequency of solvency reporting to quarterly. The filing of quarterly statements is required to be made as per the following schedule:

Solvency report as on	To be submitted on or before
30th June	15th August
30th September	15th November
31st December	15th February

Methods of determining solvency margins

Regulators are interested in short term solvency of insurance entities mainly because failure of an insurance company can produce severe and far reaching consequences like shrinkage in market capacity, high premium rates, foreign exchange loss, disruption of working of commercial enterprises etc. Supervisory authorities follow any one of the following methods for determining solvency of insurance companies.

1. **Absolute Margin:** Minimum margin which is calculated as assets over liabilities.
2. **Percentage Method:** Margin calculations are based on a fixed percentage of premium and /or claims, net of reinsurance.
3. **Risk-weighted Method:** Margin calculations are based on the quantification of risks relating to assets and liabilities. Weights are assigned to various risk categories for quantification.

In order to determine the level of solvency / capital adequacy it is necessary to understand the type of regulatory framework in existence. In India selective prescriptions in key areas like minimum price tariff, investments, reinsurance and administration expenses are already in vogue. Freedom is given to insurers in other areas like reserving, volume and portfolio mix; rear-end supervision is in the form of submission of return in prescribed format. Assuming that the present structure of regulation will be continued in the liberalized set up, the moot question is how to determine the level of solvency.

Requirement of Solvency Margin

Pricing or rating risk which is measured by exposure ratio will be higher than the solvency ratio used to quantify reserving risks in case of new business/companies. For well-established companies it has been observed that solvency ratio is higher than exposure ratio. Therefore, it is suggested that these two ratios to be quantified as given above and the greater of the amounts should be taken as the minimum required amount for solvency.

Margin of Safety

Keeping the required margin of solvency as the bench mark, the actual adjusted * solvency margin may be expressed as the multiplier which becomes the indicator of margin of safety. Available margin of safety ratio is determined thus =

$$\frac{\text{Actual Adjusted Solvency Margin}^*}{\text{Required Solvency Margin}}$$

* Appropriate deductions are to be made from available solvency from non-compliance of front-end regulatory prescriptions (e.g. non-admitted assets).

Higher the margin, greater is the index of security against subsequent adverse variations.

TRIGGER POINTS OF REGULATORY INTERVENTIONS

Depending upon the margin of the safety levels, the following interventions are suggested:

A) Absolute Method

Margin of Safety more than 2 times – No intervention

Less than 2, more than 1.5 – Calling for additional Necessary

Less than 1.5 more than 1 – On site supervision

Less than 1 – Stop writing business

B) Relative Method

Absolute method suggests intervention levels based only on a particular company's margin of safety ratio. An alternative method based on the performance of the insurance industry as a whole may be used as supplement to the above trigger levels. Margin of safety ratio for the industry can be calculated by taking the average of this ratio of all the companies in the industry. For categorizing companies for Supervisory Rating, standard deviation of margin of safety in relation to industry average can be considered in the following ways:



1. Companies having Margin of safety ratio above and equal to industry average – **SECURE**
2. Companies with margin of safety below industry average
 - a) Between industry average – **BARELY SECURE**
 - b) Between ½ standard deviation and 1 standard deviation below average – **VULNERABLE**
 - c) More than 1 standard deviation below average – **UNSECURE**

DETERMINATION OF SOLVENCY MARGINS – GENERAL INSURERS

1. Interpretation. – In this Schedule –

- (a) “Available Solvency Margin” means the excess of value of assets (furnished in Form IRDA-Assets- AA) over the value of liabilities (furnished in Form HG), with further adjustments as shown in Table III of Form KG.
- (b) “Solvency Ratio” means the ratio of the amount of Available Solvency Margin to the amount of Required Solvency Margin.

- 2. Determination of Solvency Margin. –** Every insurer shall determine the required solvency margin, the available solvency margin, and the solvency ratio in Form KG.

Form KG

Insurance Regulatory and Development Authority (Assets, Liabilities and Solvency Margin) Regulation, 2000.

TABLE I- STATEMENT OF SOLVENCY MARGIN: (General Insurers) as at 31st March, 20__.

Form Code: [][][][][][][][][][]	
Name of Insurer: _____	Registration Number: _____
Date of registration: _____	
Classification: _____	Business Within India/ Total Business
Classification Code: []	

TABLE I - REQUIRED SOLVENCY MARGIN BASED ON NET PREMIUM AND NET INCURRED CLAIMS (IN RS. LAKHS)

Item No.	Description (Class of business)	Gross Premiums	Net Premiums	Gross Incurred claims	Net Incurred Claims	RSM-1	RSM-2	RSM
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
01	Fire							
02	Marine: Marine Cargo							
03	Marine Hull:							
04	Miscellaneous: Motor							
05	Engineering							
06	Aviation							
07	Liability							
08	Rural Insurance							
09	Others							
10	Health Insurance:							
	TOTAL							

Notes: (1) RSM-1 in the above table means Required Solvency Margin based on net premiums, and shall be determined as twenty per cent. of the amount which is the higher of the Gross Premiums multiplied by a Factor A as specified below and the Net Premiums.

(2) RSM-2 in the above table means Required Solvency Margin based on net incurred claims, and shall be determined as thirty per cent. of the amount which is the higher of the Gross Net Incurred Claims multiplied by a Factor B as specified below and the Net Incurred Claims.:



Item No.	Description (Class of business)	Factor A	Fact or B
(1)	(2)	(3)	(4)
01	Fire	0.5	0.5
02	Marine: Marine Cargo	0.7	0.7
03	Marine Hull:	0.5	0.5
04	Miscellaneous: Motor	0.85	0.85
05	Engineering	0.5	0.5
06	Aviation	0.9	0.9
07	Liability	0.85	0.85
08	Rural Insurance	0.5	0.5
09	Others	0.7	0.7
10	Health	0.85	0.85

Business	Factor A	Factor B	Gross Premium	Net Premium	Gross Incurred Claims	Net Incurred Claims	RSM 1	RSM 2	RSM
Fire	0.5	0.5							
Marine	0.6	0.6							
Miscellaneous									
Motor	0.75	0.75							
Engineering	0.5	0.5							
Aviation	0.5	0.5							
Liability	0.75	0.75							
Rural	0.7	0.7							
Health	0.75	0.75							
Others	0.7	0.7							
TOTAL									

- (3) RSM means Required Solvency Margin and shall be the higher of the amounts of RSM-1 and RSM-2.

TABLE II - AVAILABLE SOLVENCY MARGIN AND SOLVENCY RATIO

Item	Description	Notes No.	Amount
(1)	(2)	(3)	(4)
01	Available Assets in Policyholders' Funds:		
02	Deduct:		
03	Liabilities		
04	Other Liabilities Excess in Policyholders' funds (01-02 - 03)		
05	Available Assets in Shareholders Funds:		
06	Deduct: Other Liabilities		
07	Excess in Shareholders' funds: (05 -06)		
08	Total ASM (04)+(07)		
09	Total RSM		
10	Solvency Ratio (Total ASM/Total RSM)		

Notes:

1. Item No. 01 shall be the amount of the Adjusted Value of Assets in respect of policyholders' funds as mentioned in Form IRDA-Assets-AA.
2. Item No. 02 shall be the amount of Total Liabilities as mentioned in Form HG.
3. Item No. 03 shall be the amount of other liabilities arising in respect of policyholders' funds and as mentioned in the Balance Sheet.
4. Items No. 05 shall be the amount of the Total Assets in respect of shareholders' funds as mentioned in Form IRDA-Assets-AA.
5. Item Nos. 06 shall be the amount of other liabilities arising in respect of shareholders' funds and as mentioned in the Balance Sheet;



FINANCIAL REPORTING OF INSURANCE OPERATIONS

The purpose of financial reporting is to allow an assessment of the financial condition and current operating results of a company. Life insurance contracts are, on average, long-term. The profitability of a block of contracts over a time period depends upon:

- Persistency
- Mortality
- Morbidity
- Interest
- Expense Experience

To report the financial condition and current operating results, a life insurance company requires construction of a valuation. A **valuation** is a measure and comparison of an insurer's assets and liabilities.

Financial Reports

Financial information and reporting depends upon needs of the user. Users are classified into:

External users:

- Regulators
- Current policy owners and potential customers
- Rating agencies
- Creditors
- Potential Buyers
- The Internal Revenue Service
- Employees and Suppliers
- General business communities

Internal Users: Comprising the corporate managers. Besides they also use two measurement tools, to evaluate the financial performance –

- Managerial accounting including budgeting, cost accounting and audit and control functions.
- Economic value analysis – is used to evaluate the long term financial results of current management actions.

Financial Statements

The primary elements of the annual statement required by Insurance regulations are the

- Balance Sheet
- Summary of Operations
- A cash flow statement

The specimen schedules as per IRDA reporting norms are shown at the end of the chapter.

Balance Sheet: The purpose of Balance Sheet is to reflect the insurer's solvency by comparing the assets and liabilities. The final accounting equation for a company's balance sheet is

Assets = Liabilities + (capital stock + surplus)

Assets

Insurer assets can be divided into three major categories.

- Invested assets
- Other admitted assets
- Non-admitted assets

Invested assets produce interest, dividend, rent and capital gain income, and include

- Cash
- Bonds
- Common and Preferred Stocks
- Preferred Stock
- Mortgage Loan on Real Estate
- Real Estate
- Policy Loans and Premium Notes
- Collateral Loans

Certain other assets not included in investments shown in the balance sheet are

- Risk management assets
- Investment income due and accrued
- Premium due and uncollected
- Accrued interest
- Non investment assets



Liabilities

The greatest part of life insurer company's liabilities, including policy reserves supported by assets held to fund future benefits under the company contracts.

Other liabilities include:

- Amounts held on deposit
- Policy owner dividend allocated but not yet payable
- Claims incurred but not yet paid
- Other amounts unpaid
- The asset valuation reserve (AVR)
- Special Reserves
- Policy owner account balances
- Post retirement benefits
- IBNR provisions are also made (incurred but not reported)

SUMMARY OF OPERATIONS

The summary of operations represents an income statement for the reported year, providing a summary of company's income, disposition of income, a reconciliation of beginning and ending surplus.

Income:

The income of a life insurer includes

- Premium
- Investment income
- Deposits
- Miscellaneous income

Disposition of Income

The income of a life insurance company is devoted to the cost of doing an insurance business and includes

- benefits
- operating expense and taxes
- Increases in required policy reserves

Cash Flow Statement:

The cash flow statement reports an insurer's cash activities and may reveal potential liquidity problems. The cash flow statement reports the sources and uses of all insurer cash for a given reporting period for both insurance operations and investment activity.

MANAGERIAL ACCOUNTING

The insurer management requires accounting both for managerial purposes, which include

- Budget accounting
- Cost accounting
- Audit and control Procedures

ECONOMIC VALUE ANALYSIS

To measure adequately the long-term financial impact of current-year management decisions, it is necessary to avoid the limitations inherent in SAP and GAAP accounting statements.

The goals of management oriented measurement are as follows:

- No distortion of long-term results of surrenders.
- Recognize anticipated profits on future business
- Recognize the long-term value resulting from current investment
- Recognize the unrealized capital gains and losses associated with investment management programs.

The primary management objective of every (non life insurer is to ensure solvency at all times and meet the contractual liabilities arising out of each contract of insurance) life insurer is to create value for shareholders and in mutual companies for policy owners. Performance measurement systems based on the creation of value are increasingly being adopted by Life insurers as a standard for judging the effectiveness of management activity.

Two of the important techniques are

- Value added analysis
- Return on equity analysis



Value Added Analysis

Net worth is defined as statutory surplus, plus the present value of future statutory earnings on existing business, plus the present value of future statutory earnings on future business. Present values are calculated by taking appropriate discount rate on cash flows. Whenever the present value of future cash flows exceeds the investment under analysis, management is creating value for shareholders or policy owners.

Value added analysis for a given planning or analysis period is measured as follows:

Ending Net Worth

Less: Beginning Net worth

Plus: Stock and Policy owner Dividends paid

Less: Capital Infusions

Equals: Value added for the period.

Return on Equity Analysis

Return on equity method is used to calculate profitability as a return on an insurer investment in a product line or other venture. Return on equity is the implicit internal rate of return associated with the cash flow or statutory profits of a profit line or other venture.

When the return on equity exceeds the insurers cost of capital, value is created for shareholders or policy owners.

SOME IMPORTANT PROPHYLATIC RATIOS USED BY INSURERS

The system of solvency margin can be supplemented by a set of early warning system.

1. Margin of safety Ratio:		
*Adjusted Actual Solvency Margin	> 15 times	
Required Solvency Margin		
<i>*Adjustments to be made for non-compliance of various front-end regulatory prescriptions.</i>		
2. Leverage/Exposure ratios:		
	Property Business	Liability Business
	(Times)	
a) Growth in Net Premium Written	3	5
Growth in Net Worth		

b) Operating leverage ratios:		
i) Gross Premium Written	6	8
Net worth		
ii) Net Premium Written	3.5	5.5
Net Worth		
c) Financial Leverage Ratios:		
i) Technical Liabilities	1	2
Net Worth		
ii) Networth growth to liability growth ratio		
Growth Rate of Network		
Growth Rate of Liabilities		
3. Adequacy sufficiency Ratios:		
a) Reserve / Funds Adequacy		
Technical Liabilities + Net Worth	1.5	2.5
Net Premium Written		
b. Loss Reserve Development Coverage Adequacy		
Loss Reserve Development	<10%	25%
Net Worth		
c. Pricing Sufficiency Ratio:		
Actual Claim incurred Ratio	+ 20%	
Expected Claim Incurred Ratio		
4. Profitability ratios		
a. Overall Technical Performance Ratios*		
i) Loss Ratios		
Incurred Losses	> 80%	150%
Net Premium earned		
ii) Expense Ratio		
Net Commission +		
Management Expenses	<20%	
Net Premium Earned		
iii) Combined Ratio		
i) + ii)	<100%	100%



b. Overall Operating Ratio*		
Underwriting Profit / Loss		
Plus Net Investment	<95%	
Income & Other income / charges		
Net Premium Earned		
c. Underwriting/Investment performance Relativity Ratio		
Underwriting Profit / Loss	+ 25%	
Net Investment Income		
d. Yield on investments		
Net Investment Income	10%	12%
Average Invested Assets		
c. Return on Equity		
Net gain from Operation	10%	15%
Net worth in the beginning of the year		
*Separately for one year and two years		
5. Reinsurance		
a) i) Premium Retention		
Ratio Net Premium	<50%	50%
Gross Premium		
ii) R.I. Recovery Vulnerability Ratio		
Reinsurance Recoverable	<5%	5%
Networth		
b) R.I. Exposure Ratio		
Reinsurance Ceded + total		
Reinsurance Recoverables		
Networth	<25%	40%
6. Liquidity		
a) Quick Liquidity		
Quickly convertible Assets	30%	15%
Technical Liabilities		
b) Current Liquidity		
i) Liquidity Investments	100%	75%
Technical Liabilities		

ii) Investment in Affiliate Networth	<5%	
iii) Investment in Non-admitted Assets Networth	<10%	
iv) Net Cash Flow	>0	
7. Efficiency / Effectiveness ratio:		
a) R.I. Recovery Ratio		
Net Claim incurred Ratio		
Gross Claim incurred Ratio	<100%	
b) Expense Ratio		
Management Expenses	<18.5%	
Gross Direct Premiums		
c) Direct Commission	<5%	
Gross Direct Premium Written		
d) Net Reinsurance Commission		
Net Reinsurance Ceded	>25%	
e) Gross Premium Lapse	<20%	
Gross Premium Written in Previous Year		

Thus, investment management of an insurance company is very crucial for the sustainability and continual operations of the company. Ratio analysis is one of the scientific tools to help check the deviations from the operations of the company.

Specimen of financial statements Schedules for Life and Non-Life Insurance business as per IRDA norms shown below:

FINANCIAL STATEMENTS REGULATIONS AS PER IRDA REGULATIONS FOR LIFE AND NON-LIFE INSURANCE COMPANIES

1. Preparation of financial statements, management report and auditor's report. – (1) An insurer carrying on life insurance business, shall comply with the requirements of Schedule A.
2. An insurer carrying on general insurance business, after the commencement of these Regulations, shall comply with the requirements of Schedule B:

Note: enclosed the schedules formats as per IRDA regulations for Life and Non-Life insurance companies.



SCHEDULE A: LIFE INSURANCE BUSINESS

Accounting principles for preparation of financial statements

1. Applicability of Accounting Standards – Every Balance Sheet, Revenue Account [Policyholders' Account], Receipts and Payments Account [Cash Flow statement] and Profit and Loss Account [Shareholders' Account] of an insurer shall be in conformity with the Accounting Standards (AS) issued by the ICAI, to the extent applicable to insurers carrying on life insurance business, except that:
 - (i) Accounting Standard 3 (AS 3) – Cash Flow Statements – Cash Flow Statement shall be prepared only under the Direct Method.
 - (ii) Accounting Standard 17 (AS 17) – Segment Reporting – shall apply irrespective of whether the securities of the insurer are traded publicly or not.

Preparation of Financial Statements

- (1) An insurer shall prepare the Revenue Account [Policyholders' Account], Profit and Loss Account [Shareholders' Account] and the Balance Sheet in Form A-RA, Form A-PL and Form A-BS, as prescribed in this Part, or as near thereto as the circumstances permit.

Provided that an insurer shall prepare Revenue Account for the undermentioned businesses separately and to that extent the application of AS 17 shall stand modified:-

- a) Participating policies and Non-participating policies;
 - b) Linked, Non-Linked, and Health Insurance;
 - c) Business within India and Business outside India.
- (2) An insurer shall prepare separate Receipts and Payments Account in accordance with the Direct Method prescribed in AS 3 – “Cash Flow Statement” issued by the ICAI.

FORM A-RA**Name of the Insurer:****Registration No. and Date of Registration with the IRDA****REVENUE ACCOUNT FOR THE YEAR ENDED
31ST MARCH, 20____.**

Policyholders' Account (Technical Account)

Particulars	Schedule	Current Year (Rs.'000)	Previous Year (Rs.'000)
Premiums earned – net			
(a) Premium	1		
(b) Reinsurance ceded			
(c) Reinsurance accepted-			
Income from Investments			
(a) Interest, Dividends & Rent – Gross			
(b) Profit on sale/redemption of investments			
(c) (Loss on sale/ redemption of investments)			
(d) Transfer/Gain on revaluation/change in fair value*			
Other Income (to be specified)			
TOTAL (A)			
Commission	2		
Operating Expenses related to Insurance Business	3		
Other Expenses (to be specified)			
Provisions (other than taxation)			
(a) For diminution in the value of investments (Net)			
(b) Others (to be specified)			
TOTAL (B)			
Benefits Paid (Net)	4		
Interim Bonuses Paid			
Change in valuation of liability against life policies in force			
(a) Gross**			
(b) Amount ceded in Reinsurance			
(c) Amount accepted in Reinsurance			
TOTAL (C)			



SURPLUS/ (DEFICIT) (D) =(A)-(B)-(C)			
APPROPRIATIONS			
Transfer to Shareholders' Account			
Transfer to Other Reserves (to be specified)			
Balance being Funds for Future Appropriations			
TOTAL (D)			

Notes:

*Represents the deemed realised gain as per norms specified by the Authority.

**Represents Mathematical Reserves after allocation of bonus.

The total surplus shall be disclosed separately with the following details:

- (a) Interim Bonuses Paid:
- (b) Allocation of Bonus to policyholders:
- (c) Surplus shown in the Revenue Account:
- (d) Total Surplus: [(a)+(b)+(c)]

FORM A-PL**Name of the Insurer:****Registration No. and Date of Registration with the IRDA****PROFIT & LOSS ACCOUNT FOR THE YEAR ENDED 31ST
MARCH, 20____.****Shareholders' Account (Non-technical Account)**

Particulars	Schedule	Current Year (Rs.'000)	Previous Year (Rs.'000)
Amounts transferred from / to the Policyholders Account (Technical Account)			
Income From Investments			
(a) Interest, Dividends & Rent – Gross			
(b) Profit on sale/redemption of investments			
(c) (Loss on sale/ redemption of investments)			
Other Income (To be specified)			
TOTAL (A)			
Expense other than those directly related to the insurance business			
Bad debts written off			
Provisions (Other than taxation)			
(a) For diminution in the value of investments (Net)			
(b) Provisions for doubtful debts			
(c) Others (to be specified)			
TOTAL (B)			
Profit/(Loss) before tax			
Provision for Taxation			
Profit/(Loss) after tax			
APPROPRIATIONS			
(a) Brought forward Reserve/Surplus from the Balance Sheet			
(b) Interim dividends paid during the year			
(c) Proposed final dividend			
(d) Dividend distribution on tax			
(e) Transfer to reserves/other accounts (to be specified)			
Profit carried forward to the Balance Sheet			

**Notes:**

- (a) Premium income received from business concluded in and outside India shall be separately disclosed.
- (b) Reinsurance premiums whether on business ceded or accepted are to be brought into account gross (i.e. before deducting commissions) under the head reinsurance premiums.
- (c) Claims incurred shall comprise claims paid, settlement costs wherever applicable and change in the outstanding provision for claims at the year-end.
- (d) Items of expenses and income in excess of one percent of the total premiums (less reinsurance) or Rs.5,00,000 whichever is higher, shall be shown as a separate line item.
- (e) Fees and expenses connected with claims shall be included in claims.
- (f) Under the sub-head “Others” shall be included items like foreign exchange gains or losses and other items.
- (g) Interest, dividends and rentals receivable in connection with an investment should be stated as gross amount, the amount of income tax deducted at source being included under ‘advance taxes paid and taxes deducted at source’.
- (h) Income from rent shall include only the realised rent. It shall not include any notional rent.

FORM A-BS

Name of the Insurer:

Registration No. and Date of Registration with the IRDA
--

BALANCE SHEET AS AT 31ST MARCH, 20__.

Particulars	Schedule	Current Year (Rs.'000)	Previous Year (Rs.'000)
SOURCES OF FUNDS			
<i>Shareholders' Funds:</i>			
Share Capital	5		
Reserves And Surplus	6		
Credit/[Debit] Fair Value Change Account			
Sub-total			
Borrowings	7		

PRINCIPLES AND PRACTICE OF GENERAL INSURANCE

<i>Policyholders' Funds:</i>			
Credit/[Debit] Fair Value Change Account			
Policy Liabilities			
Insurance Reserves			
Provision for linked liabilities			
Sub-total			
Funds for future appropriations			
Total			
Application of Funds			
Investments			
Shareholders'	8		
Policyholders'	8A		
Assets held to cover linked liabilities	8B		
Loans	9		
Fixed Assets	10		
Current Assets			
Cash and Bank Balances	11		
Advances and Other Assets	12		
Sub-total (A)			
Current Liabilities	13		
Provisions	14		
Sub-total (B)			
Net Current Assets (C) = (A – B)			
Miscellaneous Expenditure (to the extent not written off or adjusted)	15		
Debit Balance in Profit & Loss Account (Shareholders' Account)			
TOTAL			



CONTINGENT LIABILITIES

	Particulars	Current Year	Previous Year
		(Rs.'000).	(Rs.'000).
1.	Partly paid-up investments		
2.	Claims, other than against policies, not acknowledged as debts by the company		
3.	Underwriting commitments outstanding (in respect of shares and securities)		
4.	Guarantees given by or on behalf of the Company		
5.	Statutory demands/ liabilities in dispute, not provided for		
6.	Reinsurance obligations to the extent not provided for in accounts		
7.	Others (to be specified)		
	TOTAL		

SCHEDULES FORMING PART OF FINANCIAL STATEMENTS

SCHEDULE – 1

PREMIUM

	Particulars	Current Year (Rs.'000).	Previous Year (Rs.'000).
1	First year premiums		
2	Renewal Premiums		
3	Single Premiums		
	TOTAL PREMIUM		

SCHEDULE – 2

COMMISSION EXPENSES

Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
Commission paid		
Direct – First year premiums – Renewal premiums – Single premiums		
Add: Commission on Re-insurance Accepted		
Less: Commission on Re-insurance Ceded		
Net Commission		

Note:

The profit/commission, if any, are to be combined with the Re-insurance accepted or Re-insurance ceded figures.

SCHEDULE – 3

OPERATING EXPENSES RELATED TO INSURANCE BUSINESS

Particulars	Current Year (Rs.'000).	Previous Year (Rs.'000).
1. Employees' remuneration & welfare benefits		
2. Travel, conveyance and vehicle running expenses		
3. Training Expenses		
4. Rents, rates & taxes		
5. Repairs		
6. Printing & stationery		
7. Communication expenses		
8. Legal & professional charges		
9. Medical fees		
10. Auditors' fees, expenses etc		
a) as auditor		
b) as adviser or in any other capacity, in respect of (i) Taxation matters (ii) Insurance matters (iii) Management services; and		
c) in any other capacity		



11.	Advertisement and publicity		
12.	Interest & Bank Charges		
13.	Others (to be specified)		
14.	Depreciation		
	TOTAL		

Note: *Items of expenses and income in excess of one percent of the total premiums (less reinsurance) or Rs. 5,00,000 whichever is higher, shall be shown as a separate line item.*

SCHEDULE – 4

BENEFITS PAID [NET]

Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1. Insurance Claims: (a) Claims by Death, (b) Claims by Maturity, (c) Annuities/Pensions in payment, (d) Other benefits, specify		
2. (Amount ceded in reinsurance): (a) Claims by Death, (b) Claims by Maturity, (c) Annuities/Pensions in payment, (d) Other benefits, specify		
3. Amount accepted in reinsurance: (a) Claims by Death, (b) Claims by Maturity, (c) Annuities/Pensions in payment, (d) Other benefits, specify		
TOTAL		

Notes:

- (a) *Claims include claims settlement costs, wherever applicable.*
- (b) *The legal and other fees and expenses shall also form part of the claims cost, wherever applicable.*

SCHEDULE – 5

SHARE CAPITAL

	Particulars	Current Year (Rs.'000).	Previous Year (Rs.'000).
1.	Authorised Capital		
	Equity Shares of Rs..... each		
2.	Issued Capital		
	Equity Shares of Rs.each		
3.	Subscribed Capital		
	Equity Shares of Rs.....each		
4.	Called-up Capital		
	Equity Shares of Rs.each		
5.	Less: Calls unpaid		
	Add: Shares forfeited (Amount originally paid up)		
	Less: Par value of Equity Shares bought back		
	Less: Preliminary Expenses Expenses including commission or brokerage on Underwriting or subscription of shares		
	TOTAL		

Notes:

- (a) *Particulars of the different classes of capital should be separately stated.*
- (b) *The amount capitalised on account of issue of bonus shares should be disclosed.*
- (c) *In case any part of the capital is held by a holding company, the same should be separately disclosed.*



SCHEDULE – 5A
PATTERN OF SHAREHOLDING
[As certified by the Management]

Shareholder	Current Year		Previous Year	
	Number of Shares	% of Holding	Number of Shares	% of Holding
Promoters				
• Indian				
• Foreign				
Others				
TOTAL				

SCHEDULE – 6
RESERVES AND SURPLUS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Capital Reserve		
2.	Capital Redemption Reserve		
3.	Share Premium		
4.	Revaluation Reserve		
5.	General Reserves Less: Debit balance in Profit and Loss Account, if any Less: Amount utilized for Buy-back		
6.	Catastrophe Reserve		
7.	Other Reserves (to be specified)		
8.	Balance of profit in Profit and Loss Account		
	TOTAL		

Note: Additions to and deductions from the reserves should be disclosed under each of the specified heads.

SCHEDULE – 7

BORROWINGS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Debentures/Bonds		
2.	Banks		
3.	Financial Institutions		
4.	Others (to be specified)		
	TOTAL		

Notes:

- (a) *The extent to which the borrowings are secured shall be separately disclosed stating the nature of the security under each sub-head.*
- (b) *Amounts due within 12 months from the date of Balance Sheet should be shown separately*

SCHEDULE – 8

INVESTMENTS – SHAREHOLDERS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
	LONG TERM INVESTMENTS		
1.	Government securities and Government guaranteed bonds including Treasury Bills		
2.	Other Approved Securities		
3.	Other Investments		
	(a) Shares		
	(aa) Equity		
	(bb) Preference		
	(b) Mutual Funds		
	(c) Derivative Instruments		
	(d) Debentures/Bonds		
	(e) Other Securities (to be specified)		
	(f) Subsidiaries		
	(g) Investment Properties – Real Estate		
4.	Investment in Infrastructure and Social Sector		
5.	Other than Approved Investments		



SHORT TERM INVESTMENTS			
1.	Government securities and Government guaranteed bonds including Treasury Bills		
2.	Other Approved Securities		
3.	Other Investments (a) Shares (aa) Equity (bb) Preference (b) Mutual Funds (c) Derivative Instruments (d) Debentures/Bonds (e) Other Securities (to be specified) (f) Subsidiaries (g) Investment Properties - Real Estate		
4.	Investments in Infrastructural and Social Sector		
5.	Other than Approved Investments		
	TOTAL		

Note: Refer notes under Schedule 8B

SCHEDULE – 8A

INVESTMENTS – POLICYHOLDERS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
	LONG TERM INVESTMENTS		
1.	Government securities and Government guaranteed bonds including Treasury Bills		
2.	Other Approved Securities		
3.	(a) Shares (aa) Equity (bb) Preference (b) Mutual Funds (c) Derivative Instruments (d) Debentures/Bonds (e) Other Securities (to be specified) (f) Subsidiaries (g) Investment Properties - Real Estate		
4.	Investments in Infrastructure and Social Sector		
5.	Other than Approved Investments		
	SHORT TERM INVESTMENTS		
1.	Government securities and Government guaranteed bonds including Treasury Bills		

2.	Other Approved Securities		
3.	(a) Shares (aa) Equity (bb) Preference (b) Mutual Funds (c) Derivative Instruments (d) Debentures/Bonds (e) Other Securities (to be specified) (f) Subsidiaries (g) Investment Properties - Real Estate		
4.	Investments in Infrastructure and Social Sector		
5.	Other than Approved Investments		
	TOTAL		

SCHEDULE – 8B

ASSETS HELD TO COVER LINKED LIABILITIES

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
	LONG TERM INVESTMENTS		
1.	Government securities and Government guaranteed bonds including Treasury Bills		
2.	Other Approved Securities		
3.	(a) Shares (aa) Equity (bb) Preference (b) Mutual Funds (c) Derivative Instruments (d) Debentures/Bonds (e) Other Securities (to be specified) (f) Subsidiaries (g) Investment Properties - Real Estate		
4.	Investments in Infrastructure and Social Sector		
5.	Other than Approved Investments		
	SHORT TERM INVESTMENTS		
1.	Government securities and Government guaranteed bonds including Treasury Bills		
2.	Other Approved Securities		



3.	(a) Shares (aa) Equity (bb) Preference (b) Mutual Funds (c) Derivative Instruments (d) Debentures/Bonds (e) Other Securities (to be specified) (f) Subsidiaries (g) Investment Properties - Real Estate		
4.	Investments in Infrastructure and Social Sector		
5.	Other than Approved Investments		
	TOTAL		

Notes: (applicable to Schedules 8, 8A and 8B:)

- (a) Investments in subsidiary/holding companies, joint ventures and associates shall be separately disclosed, at cost.
- (i) Holding company and subsidiary shall be construed as defined in the Companies Act, 1956.
- (ii) Joint Venture is a contractual arrangement whereby two or more parties undertake an economic activity, which is subject to joint control.
- (iii) Joint control – is the contractually agreed sharing of power to govern the financial and operating policies of an economic activity to obtain benefits from it.
- (iv) Associate – is an enterprise in which the company has significant influence and which is neither a subsidiary nor a joint venture of the company.
- (v) Significant influence (for the purpose of this schedule) – means participation in the financial and operating policy decisions of a company, but not control of those policies. Significant influence may be exercised in several ways, for example, by representation on the board of directors, participation in the policy making process, material inter-company transactions, interchange of managerial personnel or dependence on technical information. Significant influence may be gained by share ownership, statute or agreement. As regards share ownership, if an investor holds, directly or indirectly through subsidiaries, 20 percent or more of the voting power of the investee, it is presumed that the investor does have significant influence, unless it can be clearly demonstrated that this is not the case. Conversely, if the investor holds, directly or indirectly through subsidiaries, less than 20 percent of the voting power of the investee, it is presumed that the investor does not have significant influence, unless such influence is clearly demonstrated. A substantial or majority ownership by another investor does not necessarily preclude an investor from having significant influence.

- (b) Aggregate amount of company's investments other than listed equity securities and derivative instruments and also the market value thereof shall be disclosed.
- (c) Investments made out of Catastrophe reserve should be shown separately
- (d) Debt securities will be considered as "held to maturity" securities and will be measured at historical costs subject to amortisation
- (e) Investment Property means a property [land or building or part of a building or both] held to earn rental income or for capital appreciation or for both, rather than for use in services or for administrative purposes.
- (f) Investment maturing within twelve months from balance sheet date and investments made with the specific intention to dispose of within twelve months from balance sheet date shall be classified as short-term investments.

SCHEDULE – 9

LOANS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	SECURITY-WISE CLASSIFICATION		
	Secured		
	(a) On mortgage of property		
	(aa) In India		
	(bb) Outside India		
	(b) On Shares, Bonds, Govt. Securities, etc.		
	(c) Loans against policies		
	(d) Others (to be specified)		
	Unsecured		
	TOTAL		
2.	BORROWER-WISE CLASSIFICATION		
	(a) Central and State Governments		
	(b) Banks and Financial Institutions		
	(c) Subsidiaries		
	(d) Companies		
	(e) Loans against policies		
	(f) Others (to be specified)		
	TOTAL		



3.	PERFORMANCE-WISE CLASSIFICATION		
	(a) Loans classified as standard (aa) In India (bb) Outside India		
	(b) Non-standard loans less provisions (aa) In India (bb) Outside India		
	TOTAL		
4.	MATURITY-WISE CLASSIFICATION		
	(a) Short Term		
	(b) Long Term		
	TOTAL		

Notes:

- (a) *Short-term loans shall include those, which are repayable within 12 months from the date of balance sheet. Long term loans shall be the loans other than short-term loans.*
- (b) *Provisions against non-performing loans shall be shown separately.*
- (c) *The nature of the security in case of all long term secured loans shall be specified in each case. Secured loans for the purposes of this schedule, means loans secured wholly or partly against an asset of the company.*
- (d) *Loans considered doubtful and the amount of provision created against such loans shall be disclosed.*

SCHEDULE – 10

FIXED ASSETS

(Rs.'000)

Particulars	Cost/ Gross Block				Depreciation				Net Block	
	Opening	Additions	Deductions	Closing	Upto Last Year	For The Year	On Sales/ Adjustments	To Date	As at year end	Previous Year
Goodwill										
Intangibles (specify)										
Land - Freehold										
Leasehold Property										
Buildings										
Furniture & Fittings										
Information Technology Equipment										
Vehicles										
Office Equipment										
Others (Specify nature)										
TOTAL										
Work-in-Progress										
GRAND TOTAL										
PREVIOUS YEAR										

Note:

Assets included in land, property and building above exclude Investment Properties as defined in note (e) to Schedule 8.



SCHEDULE – 11

CASH AND BANK BALANCES

	Particulars	Current Year (Rs.'000).	Previous Year (Rs.'000).
1.	Cash (including cheques, drafts and stamps)		
2.	Bank Balances		
	(a) Deposit Accounts		
	(aa) Short-term (due within 12 months of the date of Balance Sheet)		
	(bb) Others		
	(b) Current Accounts		
	(c) Others (to be specified)		
3.	Money at Call and Short Notice		
	(a) With Banks		
	(b) With other Institutions		
4.	Others (to be specified)		
	TOTAL		
	Balances with non-scheduled banks included in 2 and 3 above		
	CASH & BANK BALANCES		
1.	In India		
2.	Outside India		
	TOTAL		

Note: Bank balance may include remittances in transit. If so, the nature and amount should be separately stated.

SCHEDULE – 12

ADVANCES AND OTHER ASSETS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
	ADVANCES		
1.	Reserve deposits with ceding companies		
2.	Advances to ceding companies		
3.	Application money for investments		
4.	Prepayments		
5.	Advances to Officers/ Directors		
6.	Advance tax paid and taxes deducted at source		

7.	Others (to be specified)		
	TOTAL (A)		
	OTHER ASSETS		
1.	Income accrued on investments		
2.	Outstanding Premiums		
3.	Agents' Balances		
4.	Foreign Agencies' Balances		
5.	Due from other entities carrying on insurance business		
6.	Due from subsidiaries/ holding company		
7.	Deposit with Reserve Bank of India [Pursuant to section 7 of Insurance Act, 1938]		
8.	Others (to be specified)		
	TOTAL (B)		
	TOTAL (A+B)		

Notes:

- (a) *The items under the above heads shall not be shown net of provisions for doubtful amounts. The amount of provision against each head should be shown separately.*
- (b) *The term 'officer' should conform to the definition of the word 'officer' under the Companies Act, 1956.*
- (c) *Sundry debtors will be shown under item 8 (others)*

SCHEDULE – 13

CURRENT LIABILITIES

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Agents' Balances		
2.	Balances due to other insurance companies		
3.	Advances from Treaty Companies		
4.	Deposits held on re-insurance ceded		
5.	Premiums received in advance		
6.	Sundry creditors		
7.	Due to subsidiaries/holding company		
8.	Claims Outstanding		



9	Annuities Due		
10.	Due to Officers/Directors		
11.	Others (to be specified)		
	TOTAL		

SCHEDULE – 14

PROVISIONS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	For taxation (less payments and taxes deducted at source)		
2.	For proposed dividends		
3.	For dividend distribution tax		
4.	Others (to be specified)		
	TOTAL		

SCHEDULE – 15

MISCELLANEOUS EXPENDITURE

(To the extent not written off or adjusted)

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Discount Allowed in issue of shares/debentures		
2.	Others (to be specified)		
	TOTAL		

Notes:

- (a) *No item shall be included under the head “Miscellaneous Expenditure” and carried forward unless:*
1. *some benefit from the expenditure can reasonably be expected to be received in future, and*
 2. *the amount of such benefit is reasonably determinable.*
- (b) *The amount to be carried forward in respect of any item included under the head “Miscellaneous Expenditure” shall not exceed the expected future revenue/other benefits related to the expenditure.*

SCHEDULE B: NON-LIFE INSURANCE BUSINESS

Accounting principles for preparation of financial statements

1. Applicability of Accounting Standards – Every Balance Sheet, Receipts and Payments Account [Cash Flow statement] and Profit and Loss Account [Shareholders' Account] of the insurer shall be in conformity with the Accounting Standards (AS) issued by the ICAI, to the extent applicable to the insurers carrying on general insurance business, except that:
 - (i) Accounting Standard 3 (AS 3) – Cash Flow Statements – Cash Flow Statement shall be prepared only under the Direct Method.
 - (ii) Accounting Standard 13 (AS 13) – Accounting for Investments, shall not be applicable.
 - (iii) Accounting Standard 17 (AS 17) – Segment Reporting – shall apply irrespective of whether the securities of the insurer are traded publicly or not.

Preparation of Financial Statements

- (1) An insurer shall prepare the Revenue Account, Profit and Loss Account [Shareholders' Account] and the Balance Sheet in Form B-RA, Form B-PL, and Form B-BS, or as near thereto as the circumstances permit.

Provided that an insurer shall prepare Revenue Account separately for fire, marine, and miscellaneous insurance business.
- (2) An insurer shall prepare separate Receipts and Payments Account in accordance with the Direct Method prescribed in AS 3 – “Cash Flow Statement” issued by the ICAI.



FORM B-RA

Name of the Insurer:

Registration No. and Date of Registration with the IRDA

REVENUE ACCOUNT FOR THE YEAR ENDED 31ST MARCH, 20__.

(To be prepared separately fire, marine, and miscellaneous insurance)

	Particulars	Schedule	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Premiums earned (Net)	1		
2.	Profit/Loss on Sale/redemption of Investments			
3.	Others (to be specified)			
4.	Interest, Dividend & Rent – Gross			
	TOTAL (A)			
1.	Claims Incurred (Net)	2		
2.	Commission	3		
3.	Operating Expenses related to Insurance Business	4		
	TOTAL (B)			
	Operating Profit/(Loss) from Fire/Marine/Miscellaneous Business C = (A - B)			
	APPROPRIATIONS			
	Transfer to Shareholders' Account			
	Transfer to Catastrophe Reserves			
	Transfer to Other Reserves (to be specified)			

FORM B-PL**Name of the Insurer:****Registration No. and Date of Registration with the IRDA****PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31ST
MARCH, 20__.**

	Particulars	Schedule	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	OPERATING PROFIT/(LOSS)			
	(a) Fire Insurance			
	(b) Marine Insurance			
	(c) Miscellaneous Insurance			
2.	INCOME FROM INVESTMENTS			
	(a) Interest, Dividend & Rent – Gross			
	(b) Profit on sale of investments			
	Less: Loss on sale of investments			
3.	OTHER INCOME (To be specified)			
	TOTAL (A)			
4.	PROVISIONS (Other than taxation)			
	(a) For diminution in the value of investments			
	(b) For doubtful debts			
	(c) Others (to be specified)			
5.	OTHER EXPENSES			
	(a) Expenses other than those related to Insurance Business			
	(b) Bad debts written off			
	(c) Others (To be specified)			
	TOTAL (B)			
	Profit Before Tax			
	Provision for Taxation			
	APPROPRIATIONS			
	(a) Interim dividends paid during the year			
	(b) Proposed final dividend			
	(c) Dividend distribution tax			
	(d) Transfer to any Reserves or Other Accounts (to be specified)			
	Balance of profit/ loss brought forward from last year			
	Balance carried forward to Balance Sheet			



FORM B-BL

Name of the Insurer:

Registration No. and Date of Registration with the IRDA

BALANCE SHEET AS AT 31ST MARCH, 20__.

	Schedule	Current Year (Rs.'000)	Previous Year (Rs.'000)
SOURCES OF FUNDS			
SHARE CAPITAL	5		
RESERVES AND SURPLUS	6		
FAIR VALUE CHANGE ACCOUNT			
BORROWINGS	7		
TOTAL			
APPLICATION OF FUNDS			
INVESTMENTS	8		
LOANS	9		
FIXED ASSETS	10		
CURRENT ASSETS			
Cash and Bank Balances	11		
Advances and Other Assets	12		
Sub-Total (A)			
CURRENT LIABILITIES	13		
PROVISIONS	14		
Sub-Total (B)			
NET CURRENT ASSETS (C) = (A - B)			
MISCELLANEOUS EXPENDITURE (to the extent not written off or adjusted)	15		
DEBIT BALANCE IN PROFIT AND LOSS ACCOUNT			
TOTAL			

CONTINGENT LIABILITIES

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Partly paid-up investments		
2.	Claims, other than against policies, not acknowledged as debts by the company		
3.	Underwriting commitments outstanding		
4.	Guarantees given by or on behalf of the Company		
5.	Statutory demands/ liabilities in dispute, not provided for		
6.	Reinsurance obligations to the extent not provided for in accounts		
7.	Others (to be specified)		
	TOTAL		

SCHEDULES FORMING PART OF FINANCIAL STATEMENTS

SCHEDULE – 1 PREMIUM EARNED [NET]

Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
Premium from direct business written		
Add: Premium on reinsurance accepted		
Less: Premium on reinsurance ceded		
Net Premium		
Adjustment for change in reserve for unexpired risks		
Total Premium Earned (Net)		

Notes: Reinsurance premiums whether on business ceded or accepted are to be brought into account, before deducting commission, under the head of reinsurance premiums.



SCHEDULE – 2

CLAIMS INCURRED [NET]

Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
Claims paid		
Direct		
Add: Re-insurance accepted		
Less: Re-insurance Ceded		
Net Claims paid		
Add: Claims Outstanding at the end of the year		
Less: Claims Outstanding at the beginning		
Total Claims Incurred		

Notes:

- a) *Incurred But Not Reported (IBNR), Incurred but not enough reported [IBNER] claims should be included in the amount for outstanding claims.*
- b) *Claims includes specific claims settlement cost but not expenses of management.*
- c) *The surveyor fees, legal and other expenses shall also form part of claims cost.*
- d) *Claims cost should be adjusted for estimated salvage value if there is a sufficient certainty of its realisation.*

SCHEDULE- 3

COMMISSION

Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
Commission paid		
Direct		
Add: Re-insurance Accepted		
Less: Commission on Re-Insurance Ceded		
Net Commission		

Note:

The profit/commission, if any, are to be combined with the Re-insurance accepted or Re-insurance ceded figures.

SCHEDULE – 4**OPERATING EXPENSES RELATED TO INSURANCE BUSINESS**

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Employees' remuneration & welfare benefits		
2.	Travel, conveyance and vehicle running expenses		
3.	Training expenses		
4.	Rents, rates & taxes		
5.	Repairs		
6.	Printing & stationery		
7.	Communication		
8.	Legal & professional charges		
9.	Auditors' fees, expenses etc.		
	(a) as auditor		
	(b) as adviser or in any other capacity, in respect of		
	(i) Taxation matters		
	(ii) Insurance matters		
	(iii) Management services; and		
	(c) in any other capacity		
10.	Advertisement and publicity		
11.	Interest & Bank Charges		
12.	Others (to be specified)		
13.	Depreciation		
	TOTAL		

Notes:

- (a) *Items of expenses in excess of one percent of the total premium (less reinsurance) or Rs.5,00,000 whichever is higher, shall be shown as a separate line item.*



SCHEDULE – 5

SHARE CAPITAL

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Authorised Capital		
	Equity Shares of Rs..... each		
2.	Issued Capital		
	Equity Shares of Rs.each		
3.	Subscribed Capital		
	Equity Shares of Rs.....each		
4.	Called-up Capital		
	Equity Shares of Rs.each		
5.	Less: Calls unpaid		
	Add: Equity Shares forfeited (Amount originally paid up)		
	Less: Preliminary Expenses Expenses including commission or brokerage on Underwriting or subscription of shares		
	TOTAL		

Notes:

- (a) *Particulars of the different classes of capital should be separately stated.*
- (b) *The amount capitalised on account of issue of bonus shares should be disclosed.*
- (c) *In case any part of the capital is held by a holding company, the same should be separately disclosed.*

SCHEDULE – 5A
SHARE CAPITAL
PATTERN OF SHAREHOLDING
[As certified by the Management]

Shareholder	Current Year		Previous Year	
	Number of Shares	% of Holding	Number of Shares	% of Holding
Promoters				
• Indian				
• Foreign				
Others				
TOTAL				

SCHEDULE – 6
RESERVES AND SURPLUS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Capital Reserve		
2.	Capital Redemption Reserve		
3.	Share Premium		
4.	General Reserves Less: Debit balance in Profit and Loss Account Less: Amount utilized for Buy-back		
5.	Catastrophe Reserve		
6.	Other Reserves (to be specified)		
7.	Balance of Profit in Profit & Loss Account		
	TOTAL		

Note:

Additions to and deductions from the reserves should be disclosed under each of the specified heads.



SCHEDULE – 7

BORROWINGS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Debentures/Bonds		
2.	Banks		
3.	Financial Institutions		
4.	Others (to be specified)		
	TOTAL		

Notes:

- (a) *The extent to which the borrowings are secured shall be separately disclosed stating the nature of the security under each sub-head.*
- (b) *Amounts due within 12 months from the date of Balance Sheet should be shown separately.*

SCHEDULE – 8

INVESTMENTS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
	LONG TERM INVESTMENTS		
1.	Government securities and Government guaranteed bonds including Treasury Bills		
2.	Other Approved Securities		
3.	Other Investments		
	(a) Shares (aa) Equity (bb) Preference (b) Mutual Funds (c) Derivative Instruments (d) Debentures/Bonds (e) Other Securities (to be specified) (f) Subsidiaries (g) Investment Properties - Real Estate		
	SHORT TERM INVESTMENTS		
1.	Government securities and Government guaranteed bonds including Treasury Bills		
2.	Other Approved Securities		

3.	Other Investments		
	(a) Shares		
	(aa) Equity		
	(bb) Preference		
	(b) Mutual Funds		
	(a) Derivative Instruments		
	(b) Debentures/Bonds		
	(c) Other Securities (to be specified)		
	(d) Subsidiaries		
	(g) Investment Properties - Real Estate		
4.	Investment in Infrastructure and Social Sector		
	TOTAL		

Notes:

- (a) Investments in subsidiary/holding companies, joint ventures and associates shall be separately disclosed, at cost.
- (i) Holding company and subsidiary shall be construed as defined in the Companies Act, 1956.
- (ii) Joint Venture is a contractual arrangement whereby two or more parties undertake an economic activity, which is subject to joint control.
- (iii) Joint control – is the contractually agreed sharing of power to govern the financial and operating policies of an economic activity to obtain benefits from it.
- (iv) Associate – is an enterprise in which the company has significant influence and which is neither a subsidiary nor a joint venture of the company.
- (v) Significant influence (for the purpose of this schedule) – means participation in the financial and operating policy decisions of a company, but not necessarily control of those policies personnel or dependence on technical information. Significant influence may be gained by share ownership, statute or agreement. As regards share ownership, if an investor holds, directly or indirectly through subsidiaries, 20 percent or more of the voting power of the investee, it is presumed that the investor does have significant influence, unless it can be clearly demonstrated that this is not the case. Conversely, if the investor holds, directly or indirectly through subsidiaries, less than 20 percent of the voting power of the investee, it is presumed that the investor does not have significant influence, unless such influence is clearly demonstrated. A substantial or majority ownership by another investor does not necessarily preclude an investor from having significant influence.
- (b) Aggregate amount of company's investments other than listed equity securities and derivative instruments and also the market value thereof shall be disclosed.



- (c) Investments made out of Catastrophe reserve should be shown separately.
- (d) Debt securities will be considered as “held to maturity” securities and will be measured at historical cost subject to amortisation.
- (e) Investment Property means a property [land or building or part of a building or both] held to earn rental income or for capital appreciation or for both, rather than for use in services or for administrative purposes.
- (f) Investments maturing within twelve months from balance sheet date and investments made with the specific intention to dispose of within twelve months from balance sheet date shall be classified as short-term investments.

SCHEDULE – 9

LOANS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	SECURITY-WISE CLASSIFICATION		
	Secured		
	(a) On mortgage of property		
	(aa) In India		
	(bb) Outside India		
	(b) On Shares, Bonds, Govt. Securities		
	(c) Others (to be specified)		
	Unsecured		
	TOTAL		
2.	BORROWER-WISE CLASSIFICATION		
	(a) Central and State Governments		
	(b) Banks and Financial Institutions		
	(c) Subsidiaries		
	(d) Industrial Undertakings		
	(e) Others (to be specified)		
	TOTAL		
3.	PERFORMANCE-WISE CLASSIFICATION		
	(a) Loans classified as standard		
	(aa) In India		
	(bb) Outside India		
	(b) Non-performing loans less provisions		
	(aa) In India		
	(bb) Outside India		
	TOTAL		
4.	MATURITY-WISE CLASSIFICATION		
	(a) Short-Term		
	(b) Long-Term		
	TOTAL		

Notes:

- (a) *Short-term loans shall include those, which are repayable within 12 months of the balance sheet date. Long term loans shall be the loans other than short-term loans.*
- (b) *Provisions against non-performing loans shall be shown separately.*
- (c) *The nature of the security in case of all long term secured loans shall be specified in each case. Secured loans for the purposes of this schedule, means loans secured wholly or partly against an asset of the company.*
- (d) *Loans considered doubtful and the amount of provision created against such loans shall be disclosed.*

SCHEDULE – 10**FIXED ASSETS**

(Rs.'000)

Particulars	Cost/ Gross Block Depreciation				Net Block					
	Opening	Addi- tions	Deduc- tions	Closing	Upto Last Year	For the Year	On Sales/ Adjust- ments	To Date	As at year end	Previous Year
Goodwill										
Intangibles (specify)										
Land-Freehold										
Leasehold Property										
Buildings										
Furniture & Fittings										
Information Technology Equipment										
Vehicles										
Office Equipment										
Others (Specify nature)										
TOTAL										
Work-in-progress										
GRAND TOTAL										
PREVIOUS YEAR										

Note:

Assets included in land, building and property above exclude Investment Properties as defined in note (e) to Schedule 8.



SCHEDULE – 11

CASH AND BANK BALANCES

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Cash (including cheques, drafts and stamps)		
2.	Bank Balances		
	(a) Deposit Accounts		
	(aa) Short-term (due within 12 months)		
	(bb) Others		
	(b) Current Accounts		
	(c) Others (to be specified)		
3.	Money at Call and Short Notice		
	(a) With Banks		
	(b) With other Institutions		
4.	Others (to be specified)		
	TOTAL		
	Balances with non-scheduled banks included in 2 and 3 above		

Notes:

Bank balance may include remittances in transit. If so, the nature and amount should be separately stated.

SCHEDULE – 12

ADVANCES AND OTHER ASSETS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
	ADVANCES		
1.	Reserve deposits with ceding companies		
2.	Application money for investments		
3.	Prepayments		
4.	Advance tax paid and taxes deducted at source (Net of Provision for taxation)		
5.	Others (to be specified)		
	TOTAL (A)		
	OTHER ASSETS		
1.	Income accrued on investments		
2.	Outstanding Premiums		
3.	Agents' Balances		

4.	Foreign Agencies' Balances		
5.	Due from other Entities carrying an Insurance Business (Including reinsurance)		
6.	Due from subsidiaries/ holding		
7.	Deposit with Reserve Bank of India [Pursuant to section 7 of Insurance Act, 1938]		
8.	Others (to be specified)		
	TOTAL (B)		
	TOTAL (A+B)		

Notes:

- (a) *The items under the above heads shall not be shown net of provisions for doubtful amounts. The amount of provision against each head should be shown separately.*
- (b) *The term 'officer' should conform to the definition of the word 'officer' given under the Companies Act, 1956.*
- (c) *Sundry Debtors will be shown under item 9 (Other)*

SCHEDULE – 13
CURRENT LIABILITIES

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Agents' Balances		
2.	Balances due to other insurance companies		
3.	Deposits held on re-insurance ceded		
4.	Premiums received in advance		
5.	Unallocated Premium		
6.	Sundry creditors		
7.	Due to subsidiaries/holding company		
8.	Claims Outstanding		
9.	Due to Officers/Directors		
10.	Others (to be specified)		
	TOTAL		



SCHEDULE – 14

PROVISIONS

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Reserve for Unexpired risk		
2.	For taxation (less advance tax paid and taxes deducted at source)		
3.	For proposed dividends		
4.	For dividend distribution tax		
5.	Others (to be specified)		
	TOTAL		

SCHEDULE – 15

MISCELLANEOUS EXPENDITURE

(To the extent not written off or adjusted)

	Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1.	Discount Allowed in issue of shares/ debentures		
2.	Others (to be specified)		
	TOTAL		

Notes:

- (a) No item shall be included under the head “Miscellaneous Expenditure” and carried forward unless:
1. some benefit from the expenditure can reasonably be expected to be received in future, and
 2. the amount of such benefit is reasonably determinable.
- (b) The amount to be carried forward in respect of any item included under the head “Miscellaneous Expenditure” shall not exceed the expected future revenue/other benefits related to the expenditure.

SCHEDULE C

AUDITOR'S REPORT

The report of the auditors on the financial statements of every insurer shall deal with the matters specified herein:

1. (a) That they have obtained all the information and explanations which, to the best of their knowledge and belief were necessary for the purposes of their audit and whether they have found them satisfactory;
 - (b) Whether proper books of account have been maintained by the insurer so far as appears from an examination of those books;
 - (c) Whether proper returns, audited or unaudited, from branches and other offices have been received and whether they were adequate for the purpose of audit;
 - (d) Whether the Balance sheet, Revenue account, Profit and Loss account and Receipts and Payments Account dealt with by the report are in agreement with the books of account and returns;
 - (e) Whether the actuarial valuation of liabilities is duly certified by the appointed actuary including to the effect that the assumptions for such valuation are in accordance with the guidelines and norms, if any, issued by the Authority, and/or the Actuarial Society of India in concurrence with the Authority.
2. The auditors shall express their opinion on:
 - (a) (i) Whether the balance sheet gives a true and fair view of the insurer's affairs as at the end of the financial year/period;
 - (ii) Whether the revenue account gives a true and fair view of the surplus or the deficit for the financial year/period;
 - (iii) Whether the profit and loss account gives a true and fair view of the profit or loss for the financial year/period;
 - (iv) Whether the receipts and payments account gives a true and fair view of the receipts and payments for the financial year/period;
 - (b) The financial statements stated at (a) above are prepared in accordance with the requirements of the Insurance Act, 1938 (4 of 1938), the Insurance Regulatory and Development Act, 1999 (41 of 1999) and the Companies Act, 1956 (1 of 1956), to the extent applicable and in the manner so required.
 - (c) Investments have been valued in accordance with the provisions of the Act and these Regulations.



- (d) The accounting policies selected by the insurer are appropriate and are in compliance with the applicable accounting standards and with the accounting principles, as prescribed in these Regulations or any order or direction issued by the Authority in this behalf.
3. The auditors shall further certify that:
- (a) they have reviewed the management report and there is no apparent mistake or material inconsistencies with the financial statements;
 - (b) the insurer has complied with the terms and conditions of the registration stipulated by the Authority.
4. A certificate signed by the auditors [which shall be in addition to any other certificate or report which is required by law to be given with respect to the balance sheet] certifying that:–
- (a) they have verified the cash balances and the securities relating to the insurer's loans, reversions and life interests (in the case of life insurers) and investments;
 - (b) to what extent, if any, they have verified the investments and transactions relating to any trusts undertaken by the insurer as trustee; and
 - (c) no part of the assets of the policyholders' funds has been directly or indirectly applied in contravention of the provisions of the Insurance Act, 1938 (4 of 1938) relating to the application and investments of the policyholders' funds.

Questions



1. Why is Investment function so critically important in the overall financial management of a life insurer company?
2. What are the factors to be taken into consideration in deciding an optimum investment portfolio of a life insurer?
3. Discuss the statutory requirements of solvency margins as specified by the IRDA.
4. How do the ROE and Value-added analysis helps the insurer measure the financial impact of the managerial decisions?
5. List out some of the ratios to evaluate the performance of the insurance operations.