CHAPTER VIII

INSURANCE

8.1 Intro to Insurance
8.2 Principles of Insurance
8.3 Classification of Insurance

Concepts & Issues that emerge from the content

- Insurance
  - +. Introduction
  - +. Risk
  - +. Importance of insurance
  - +. Insurance agreement

- Principles of insurance
  - +. Basic principles
  - +. Under-writing
  - +. Re-insurance

- Classification of insurance
  - +. Life insurance
  - +. General insurance

8.1 INTRODUCTION TO INSURANCE

What is Insurance?

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What are the special terms used in Insurance?

- ✓ Insurer
- ✓ Insured
- ✓ Insurance policy
- ✓ Insurance premium
- ✓ Insurance claim
- ✓ Third party
- ✓ Risk
- ✓ Cause
- ✓ Loss
- ✓ Damage

What are the methods of controlling Risk?

1. Prevention
2. Minimize
3. Bearing
4. Transfer

What are the risks that can be insured?

Risks that can be insured are the ones that can be measured by money. Any uncertainty that cannot be measured by monetary terms cannot be insured since the claim will be paid by money. Therefore all risks cannot be insured.

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Insurable Risks	Non-insurable Risks

What are the features of an Insurable Risk?

1. Predictability

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2. Casualty

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3. Un-connectedness

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4. Verifiability

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5. Uncertainty

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6. Insurable interest

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7. Legality

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What is an Insurance Agreement?

An insurance agreement is a written document representing contract between an insurer & the insured which was accepted by the insurer after an insurance proposal being submitted by the insured. It shall contain all legal facts pertaining to the policy & binds both parties into a legal contract. Without an agreement there cannot be an insurance policy. The parties found in an insurance agreement are;

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What is an Insurance Policy?

An Insurance policy is a written certificate given by an insurer to the insured after getting into an insurance agreement. It is the evidence of the agreement of insurer to bear any risks of the insured for an agreed payment. Once the policy certificate has been issued legally there is no room for either party to escape from their insurance related obligations.

What is an Insurance Policy Application?

This is a written application form submitted by a potential insurer to the insured by including the necessary & required details & requesting for an insurance policy cover. In order to obtain an insurance policy, first the potential insurer should submit an application form. Only if it is accepted, both insurer & insured can get into an agreement & an insurance policy can be issued.

The type of application form & the required information will differ from policy to policy & insurer to insurer. Therefore some type of policies want more information & while some want less. A standard insurance application will request the following information;

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What are the elements for a valid insurance agreement?

1. Idea of legal obligation
2. Insurance offer / proposal
3. Acceptance
4. Legal validity
5. Ability for legal obligation by parties

What are the Principles of Insurance?

These are the set of principles followed by all parties related to insurance in order to ensure a good insurance industry beneficial to all parties, trustworthiness, ensure no insured makes profit from insurance & be legally fair.

1. Insurable interest
2. Utmost good faith
3. Indemnity
4. Contribution
5. Subrogation
6. Proximate cause

How can the Insurance Principles be explained in detail?

1. **Insurable interest**

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2. **Utmost good faith**

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3. **Indemnity**

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4. **Contribution**

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5. **Subrogation**

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Note – **Subrogation Letter** –

6. Proximate cause

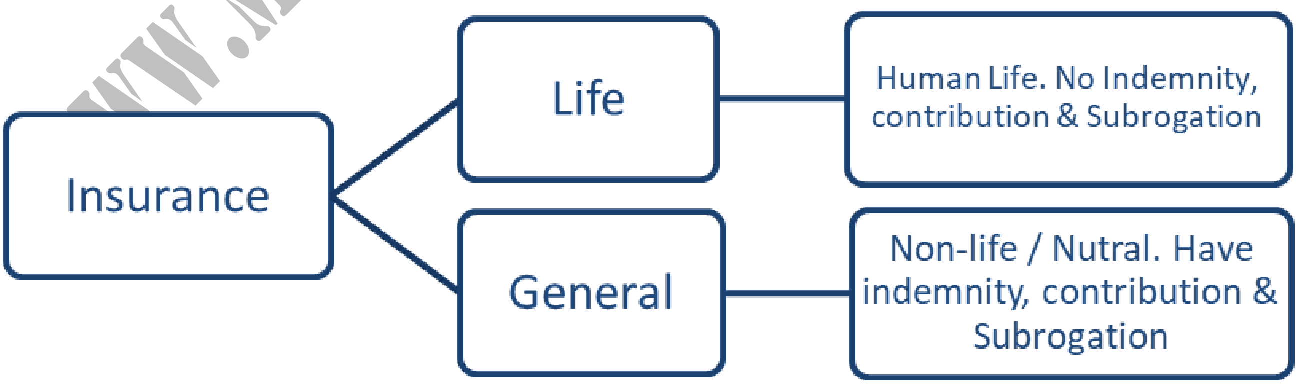
What are the situations where utmost good faith may be breached?

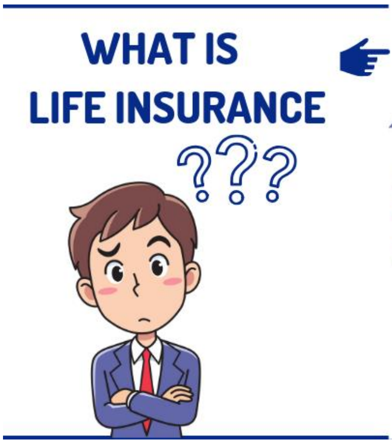
1. Non-revealing
2. Hiding
3. Innocent misrepresentation
4. Fraudulent misrepresentation

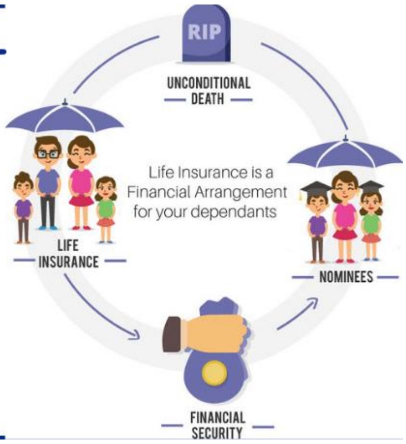
What is Over-Insurance & Under-Insurance?

Over Insurance	Under Insurance

How can we classify Insurance?







What is Life Insurance?

An insurance policy taken to cover losses to a human life in death or accidents, where the insured or his / her dependents may receive financial benefits. In other words, Life insurance is a contract between an insurer & an insured in which the insurer guarantees payment of a death benefit to named beneficiaries upon the death of the insured. The insurance company promises a death benefit in consideration of the payment of premium by the insured.

The purpose of life insurance is to provide financial protection to surviving dependents after the death of an insured. It is essential for applicants to analyze their financial situation and determine the standard of living needed for their surviving dependents before purchasing a life insurance policy. Life insurance agents or brokers are instrumental in assessing needs and establishing the type of life insurance most suitable to address those needs.

How can we classify Life Insurance based on personal requirements?

1. Family
2. Wealth creation
3. Special needs
4. Wealth growth

What are the benefits to an insured from Life Insurance?

What are the types of Life Insurance policies?

1. Term life insurance policy

2. **Whole-life insurance policy**

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3. **Endowment insurance policy**

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4. **Annuities**

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5. **Children Insurance policy**

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6. **Joint life insurance policy**

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7. **Group life insurance policy**

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8. **Disability insurance policy**

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9. Hospitalization cover

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What is a Lapsed Policy?

This is the deactivation of the life insurance policy before the agreed time period due to the non-payment of agreed premium by the insured. In other words, the policy for which all benefits to the policy holder cease & is terminated due to a non-payment of premium on the due date or even after the grace period.

Such a policy can be revived / reinstated / reactivated by an ordinary reactivation or special reactivation. But if the insured is unable to continue. He may opt for either taking the surrender value or convert into a paid up policy.

Ordinary revival

The policy holder can easily revive the lapsed policy by simply paying the unpaid premiums along with interest charges applicable. Such revival can be done within 5 years from the initial lapse.

Special revival

The policy holder will have to fulfill special conditions in addition to paying the lapsed premium plus interest like a new medical test, Special amendments, new conditions etc. This criteria changes from insurer to insurer.

Surrender Value

This is the amount receivable by an insurer after he surrenders his life insurance policy to the insurer. Under normal circumstances. The insurer has to pay premium for at least 3 years to acquire any surrender value.

Paid-up Policy

Here the policy wont lapse but automatically continues with a reduced sum being assured. In other words, the value of the policy will reduce according to the payments made where in case of a loss, a reduced amount from the original amount will be paid.

How to differentiate Surrender Value & Paid-up Policy?

Surrender Value	Paid-up Policy

What is General Insurance?

In simple terms, any insurance other than life insurance is general insurance. In other words, insurance policies covering any non-human life aspect or risk such as home, car, business, investments, livestock etc is considered as general insurance. Here what is insured is neutral & the principles of indemnity, contribution & subrogation are applicable.

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How can we differentiate Life insurance & General insurance?

Life Insurance	General Insurance

What are the types of General Insurance policies found?

1. Arson Insurance
2. Marine insurance
3. Burglary Insurance
4. Motor vehicle insurance
5. Natural disaster insurance

6. Goods in transit insurance
7. Cash in transit insurance
8. Liability insurance
9. Luggage insurance
10. Credit insurance
11. Aviation insurance
12. Fidelity insurance
13. Engineering insurance
14. Contractors insurance
15. Machinery insurance

What is Fire / Arson Insurance?

In simple terms, fire insurance is the insurance taken out to cover the cost of damage caused by fire. This is the insurance policy covering any losses to property, assets & stocks belonging to the insured from fire & related causes. The premium is based on value of asset & probability of catching fire.

The purchase of fire insurance in addition to homeowner's or property insurance helps to cover the cost of replacement, repair, or reconstruction of property, above the limit set by the property insurance policy. The risks that can be covered by fire insurance can be;

1. Strikes & protests
2. Short circuits
3. Explosions
4. Earthquakes
5. Floods
6. Hail storms
7. Lightning strikes
8. Aircraft crashes
9. Consequential loss

What is Consequential Loss Insurance?

This is the policy covering the loss of income from business until restoration, due to the business & its assets being damaged from fire & other causes. This insurance policy will provide a financial support to the insured until his business is fully restored where he can continue to earn. Therefore this policy provides a business peace of mind.

What is Marine Insurance?

This is the insurance policy taken by persons with interest covering any losses to the ship, its crew & cargo for certain time, journey or route. In other words, Marine insurance is the policy that covers the loss or damage of ships, cargo, terminals, & any transport by which the property is transferred, acquired, or held between the points of origin & the final destination. Marine insurance can be classified into 2 as follows;

Hull Insurance	Cargo Insurance
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The types of policies found under Hull Insurance can be; A. All risk policy B. Total loss only policy C. Ports policy D. Hull construction policy E. Repair policy	The types of policies found under Cargo Insurance can be; A. Valued policy B. Open policy C. Floating policy

What are the risks that can insured in Marine Insurance?

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What are the risks that fall under the “inherent – vice” in Marine Insurance?

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What is Deviation of Voyage & Jettison?

Deviation of Voyage	Jettison
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What is Motor Insurance?

This is the insurance policy taken by a vehicle owner to cover any anticipated losses to the vehicle, its passengers & external parties & property by the vehicle. As per the law, it is compulsory to insure all vehicles by their owners to cover any anticipated losses to external parties & property on & using the roads. Therefore it's called, "Compulsory insurance certificate".

What are the types of Motor Insurance policies?

1. Comprehensive Motor Insurance cover

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2. Third party Arson & Burglary cover

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3. Third party insurance cover

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What is Liability Insurance?

This is the insurance policy taken by property owners & businessmen to cover any losses to third parties from their products, property & other external persons. In other words, liability insurance is a Policy that covers civil liabilities to third parties, arising from bodily injury, property damage, or other wrongs due to the action or inaction of the insured. It covers only civil liabilities & not criminal liabilities.

What are the types of Liability Insurance covers found?

1. Property owners liability cover

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2. **Product liability cover**

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3. **Employer's liability cover**

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4. **Professional liability cover**

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5. **Public liability insurance cover**

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What is Fidelity Insurance?

This is simply an insurance policy taken out by an employer against losses incurred through dishonesty by employees. In other words, A Fidelity Insurance policy covers losses sustained by the employer as a result of an act of forgery, fraud or dishonesty from an employee. The loss can be of money or goods, for the duration of the policy.

This policy is also known as Fidelity Bond, where the cover may be required in respect of a single employee or a group of employees. There are certain circumstances that will determine whether or not Fidelity Insurance is an appropriate cover for your business. They can be;

- ✓ The record, standing and reputation of the employee
- ✓ The "bonafides" of the employer
- ✓ The systems in place for checking accounts
- ✓ General supervision of the employee

The Key Things to Remember in Fidelity insurance can be;

- ✓ The insurance covers a direct financial loss, not a consequential one
- ✓ The loss should be of money or goods of the insured

- ✓ The act should be committed in the course of the worker's duties
- ✓ The theft must be committed by an employee
- ✓ Losses that may have been caused by bad accountancy are not payable, they must be supported by evidence of acts of dishonesty

What is Burglary / Theft Insurance?

Burglary insurance is an insurance policy that provides financial compensation for loss or damage caused to property and valuable items due to burglary or house breaking. In other words, the insurance policy covering any anticipated losses from thieves to businesses & property.

If any such loss takes place due to burglary activities, a compensation will be paid as per the policy. By paying an additional premium, some additional risks can be covered such as losses from riots & strikes. Such policy is called "joint fire & burglary insurance cover". The types of businesses that specifically select this policy are;

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What is Transit Insurance?

This is the insurance policy covering any anticipated losses to cash or goods that are being transported from one location to another. This policy comes into effect at the point loading & will cease effect at the point of unloading. This policy mostly covers losses for transit on land. The 2 types of transit insurance can be;

1. Cash in transit insurance
2. Goods in transit insurance

What is Luggage / Baggage Insurance?

This is the policy covering the baggage of travelers especially on overseas trips from various risks such as loss of baggage, theft, damage, misplacement etc. the premium will be decided on the value of the luggage, countries travelling & the time period of travelling.

What is Natural disaster Insurance?

This is policy covering property & persons from losses that could occur due to natural disasters such as floods, earthquakes, landslides, cyclones, tsunami etc. the premium is decided on the value of the property & probability of natural disasters.

What is Aviation Insurance?

This is the policy taken by airlines to cover airplanes, employees, passengers, cargo & related items from any anticipated losses & damages.

What is Credit Insurance?

This is the insurance policy covering any anticipated losses to be incurred by creditors due to bad debts of bankruptcy of their debtors. This policy may be taken by contractual employees who may face a non-payment by their contractual employees. This type of policies are taken by businesses who involve in foreign trade since the probability of bad debts are quite high.

What is Machinery Insurance?

This is the insurance policy covering the machinery & equipment from any anticipated losses & damages during work related activities.

What is Contractors Insurance?

This is the policy covering any losses & risks that can occur to the contractor until a project is completed & handed over. Such risks can be sudden price changes of materials, changes in weather, national emergency situations, labour strikes etc.

What is Re-insurance, Double insurance & Under-writing?

Re-insurance is an insurance policy taken by an insurer from another insurer covering the insurance policies it had undertaken from the insured. This is done to minimize the risk of the insurer & be able to undertake greater risks above capacity. The advantages of Re-insurance can be;

To the Insurer	To the Insured

Double insurance is where one asset has been insured in 2 or more insurance companies by the insured. Therefore one asset shall have 2 or more insurance policies. Here the sum of all policies taken for one given asset should exceed the value of the asset. This is fine with life insurance but a waste in general since due to the principle of indemnity & contribution, cannot get a higher claim.

Ex-

Underwriting is where a higher value asset is being insured in 2 or insurance companies in proportions. Therefore one insurer is liable only a given portion. This is done since some insurers are reluctant to undertake the risk of a large valued asset alone but instead prefer a small portion. Therefore the asset will be insured in portions in many insurers. Here the sum of all those policies should equal the value of the asset.

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What is an Insurance Agent & Insurance Broker?

1. Insurance Agent

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2. Insurance Broker

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What is Insurance Regulatory Commission of Sri Lanka?

The is the government appointed developing, monitoring & controlling body for the insurance industry in Sri Lanka, incorporated under "Insurance industries standardization act no-43 of 2000". It was set up in 2001 as the "Insurance board of Sri Lanka.

But with effect from the 19th of October 2017, the organization was renamed as "Insurance regulatory commission of Sri Lanka" under "Insurance industries standardization act no-23 of 2017 (amended). The functions of the "Insurance Regulatory Commission of Sri Lanka" can be;

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What is SLECIC?

This is an insurance company setup & owned by the government to provide insurance & related services to the export sector in Sri Lanka. It was incorporated under "Sri Lanka Export Credit Insurance Corporation Act no-15 of 1978" with the intention of uplifting & developing exports. Some of its services can be;

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What is Agriculture & Agrarian Insurance board?

This is a government owned insurance organization established under the "Agricultural insurance board act no-27 of 1973" to provide insurance related benefits to farmers

What is CESS Tax?

This a surcharge deducted by the government from the value of policies as per the insurance industries standardization act no-43 or 2000 & deposited in the policy holders protection fund. The surcharge will be at 0.2% for life & 0.4 for general insurance.

What is Policy Holder's Protection Fund?

This is the fund created with the intention the policy holders / insured from any issues, problems & unethical activities by insurers. The funds are collected from the cess tax & it will be reinvested in government securities.

What is Insurance Association of Sri Lanka?

This is the association consisting all insurers registered at the insurance regulatory commission of Sri Lanka. This is an approved association by the insurance regulatory commission of SL.

What is Sri Lanka Insurance Brokers Association?

This is the association consisting all brokers registered at the insurance regulatory commission of Sri Lanka. This is an approved association by the insurance regulatory commission of SL.

What is Sri Lanka Insurance Institute?

This is a non-profit institution set up in 1982 with the intention of developing the skills & knowledge of persons who wish to pursue a career in insurance or engage in insurance. This is affiliated to the charted institute of insurers in London.

What are the advantages of Insurance Policies?

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What are the disadvantages of Insurance Policies?

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